Wellington International Airport Limited

Initial pricing proposal

For aeronautical prices for the period 1 April 2024 to 31 March 2029

31 July 2023

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APPENDICES

ELECTRONIC FILES ATTACHED

PART A: EXECUTIVE SUMMARY

Introduction and context

1. Prior to 2020, every day approximately 17,500 passengers travelled through Wellington International Airport (WIAL) following its highest annual growth in a decade for domestic travellers. International travellers were set to reach 1 million per annum for the first time, and the Airport planned substantial capital investment through its 2040 Masterplan to cater for the next 20 years of growth.

2. Covid-19 seriously impacted the entire aviation industry and WIAL was no exception. We acted quickly to resize, making the very difficult decision to inform 30% of staff their roles were being made redundant. We also immediately reprioritised capital expenditure to essential maintenance only, and restructured bank and bond finances to withstand the pandemic period. This included securing waivers of lender covenants and putting in place a $75.8 million shareholder support agreement with both Infratil and Wellington City Council. Shareholder dividends were foregone for two years. We have undertaken three bond issues since this time to extend and secure efficient long term funding.

3. WIAL also worked hard to ensure airlines were supported through this period as much as possible. This included deferring price setting consultation for the PSE4 period (FY20-24), holding airline charges flat for two years, deferring some airline payments into PSE5, and agreeing to a passenger washup which avoided a windfall gain for either airports or airlines. We also adopted a substantial discount against our own assessment of Weighted Average Cost of Capital (WACC), reducing our target return from 6.08% to 5.93%. An additional $15.1m revenue was deferred, further reducing the target return within the period to 5.43%.

4. Several headwinds remain in the short term, with high inflation, construction cost challenges, and higher cost of capital. We continue to work hard to retain material cost efficiencies achieved during the pandemic, however some cost increases such as rates, insurance and construction costs are largely outside of our control.

Constrained passenger numbers

5. Airports and airlines continue to bear the consequences of the pandemic, with passenger numbers yet to return to pre-Covid levels and airline capacity and competition constrained. On the plus side, demand for travel remains strong, and international borders are fully open with no sign of further restrictions.

6. The number of people travelling in and out of Wellington is climbing back to pre-Covid levels, with domestic passengers recovering to around 90% of previous levels and international to around 76% by the end of FY23. The Airport is expected to return to pre-Covid passenger numbers domestically by FY25/26, and internationally by FY27, indicating a 6-7 year deferral of volume expectations driven by the pandemic. Following this, we anticipate growth rates returning to previous levels of 3-3.5% per annum, informed by independent forecasts by InterVistas.

PSE4 deferrals and agreed sharing of risk

7. The Covid-19 pandemic also created immense difficulty in setting prices and obtaining accurate forecasts for PSE4. We were very conscious of the need to avoid cost increases for airline partners during this difficult time, and therefore deferred some revenue for collection in PSE5. We also agreed to a washup of revenue against actual passenger numbers, to manage the risks associated with PSE4 forecasts consulted upon up to March 2021 at the height of the pandemic.

8. The revenue deferral effectively subtracted $1.63 from the average charge paid by airlines by the end of PSE4. Similarly, the value of the passenger wash up would have added $2.44 per passenger if passenger numbers were accurately forecast for PSE4. Taken together, these amounts produce an

average charge at the end of PSE4 of $19.07 rather than the average $15.00 published charge paid by airlines. Once recovery of these PSE4 revenues is taken into account, the proposed PSE5 price increase is a relatively modest $4.13 per passenger across the five-year period or 4.0% per annum in nominal terms ($1.91 and 1.8% per annum in real terms).

Capital expenditure washup

9. The other material issue resulting from Covid-19 deferrals is that the capital expenditure forecasts used for PSE4 price setting are, in retrospect, inaccurate. Recovery was slower than anticipated by the March 2021 forecasts, resulting in less pressure on infrastructure and the ability to defer some plans. This means airlines have effectively funded capex for projects which did not occur. Recognising the unique circumstances of the pandemic-affected period, we are now proposing a wash-up of unspent PSE4 capital expenditure.

Cost of capital challenges

10. WIAL's cost of capital has increased since PSE4, due to increases in the risk-free rate and the revealed risk profile of airports in the wake of the Covid-19 pandemic.

11. The regulatory environment is currently challenging, given that the 2016 Input Methodologies (IMs) are out of date and have not taken the latest data into account; while the 2023 IMs are only in draft, and do not take effect until 2026. We have therefore taken a bespoke approach to estimating our WACC, and invite airline feedback on this approach.

12. Our proposed approach is to update asset beta estimates for the latest data, and incorporate an adjustment for WIAL's BBB credit rating. In order to de-weight the impact of Covid on WACC, we propose to adopt a 15-year estimation window for asset beta, which gives a more stable long-term view of asset beta.

13. Our bespoke estimate results in a WACC of 8.55%.

Revised capital expenditure programme

14. The 2040 Masterplan released in 2019 remains the foundation of our future planning. In our view, the Masterplan continues to provide the most efficient way for WIAL to eventually cater to passenger growth. This includes the relocation of the international operation from north to south, and expansion of apron over the southern Miramar Golf Course area to enable the development of sufficient contact stands to facilitate forecast movement volumes. These developments were broadly accepted by airlines in extensive consultation from 2018-2020.

15. However, the plan has naturally been set back by several years, and we have worked hard to reprioritise some aspects in order to reduce the impact on prices, while maintaining appropriate levels of service for airlines and passengers. Airlines have indicated a preference for WIAL to reduce expenditure and reconsider the scope of investment plans given the current high-cost environment, and we have done so in formulating our pricing proposal.

16. As a result, and in spite of material increases in construction costs, we propose reducing capital expenditure by approximately $210 million compared to pre-Covid PSE5 forecasts. This includes the deferral of terminal and apron development, which will now not impact pricing until PSE6. The seawall redevelopment project, which remains essential for resilience reasons, has been re-staged for progressive re-armouring of the seawall over the next 10 years. This will involve some additional maintenance costs but will bring down immediate capital expenditure requirements.

17. However, even while deferring these major projects, regulatory requirements, demand pressure, construction cost pressure and ageing buildings need to be addressed. Essential projects which have been retained include the replacement Airport Fire Station building as the current building is at

the end of its life; introduction of ECAC standard 3 security upgrades; and a new baggage handling system which is now urgently required. These projects have all been discussed with airlines previously in PSE4 consultation.

18. There are three areas proposed for capital expenditure additional to those already discussed with airlines in PSE4. These are:

- Interim terminal works designed to ease congestion while Master Plan developments are deferred;
- The transfer of airfield power and lighting from Airways to WIAL (PLEXIT),
- The installation of Engineered Material Arrestor Systems (EMAS) as an important runway safety initiative.

19. We welcome feedback on our proposed capital expenditure for PSE5.

Maintaining low operating costs per passenger

20. At the onset of Covid-19, WIAL responded quickly with a resizing of operations, including a 30% reduction in staffing levels, salary reductions, cutting many other costs including consultancy, marketing, and travel expenditure and reducing directors' fees. These savings were shared with airline customers in PSE4.

21. During the period of pandemic disruption and since that time, we have continued to closely manage our operating and capital expenditure commensurate with cashflows and the operating environment. This has included a focus on retaining the cost savings achieved where appropriate. At the same time, operating expenses have increased mainly due to Council rates, insurance, and variable costs in line with the growth in passenger numbers. Other increases in operational expenditure relate to PLEXIT and additional firefighters in line with a Task Resource Analysis.

22. Excluding these areas of unavoidable increases, WIAL's real costs per passenger in FY29 are forecast to remain below FY20 levels at $4.03 per passenger ($4.08 in FY20). We aim to continue this trend over the long-term with growing passenger numbers and associated economies of scale.

23. We consider that the PSE5 forecast is reasonable and demonstrates our commitment to operational efficiency whilst maintaining a high standard of airport with commensurate high quality of service. We also note that our operating costs continue to be low by comparison to other airports in both Australasia and worldwide.[1]

Asset valuation and revaluations

24. It is WIAL's usual practice to commission an updated land valuation prior to pricing, and to treat the real valuation gains as income as per the IMs. The uplift is allocated to airline customers as an opening carry forward adjustment, which has a downward impact on prices for the period.

25. Our updated valuation is appended to this proposal, showing an uplift of $38.7 million when rolled forward at CPI to 1 April 2024.

26. We have also forecast revaluations for the period using our previous method of estimating CPI. These forecast gains are also treated as income, which has a further downward impact on prices.

[1] Jacobs UK (formerly Leigh Fisher) 2021

27. There is also a remaining net revaluation carry forward from PSE4, with $5.98 million remaining to be returned to airline customers in PSE5. The history of this carry forward is outlined in the PSE4 consultation documents, which we are able to provide again if necessary.

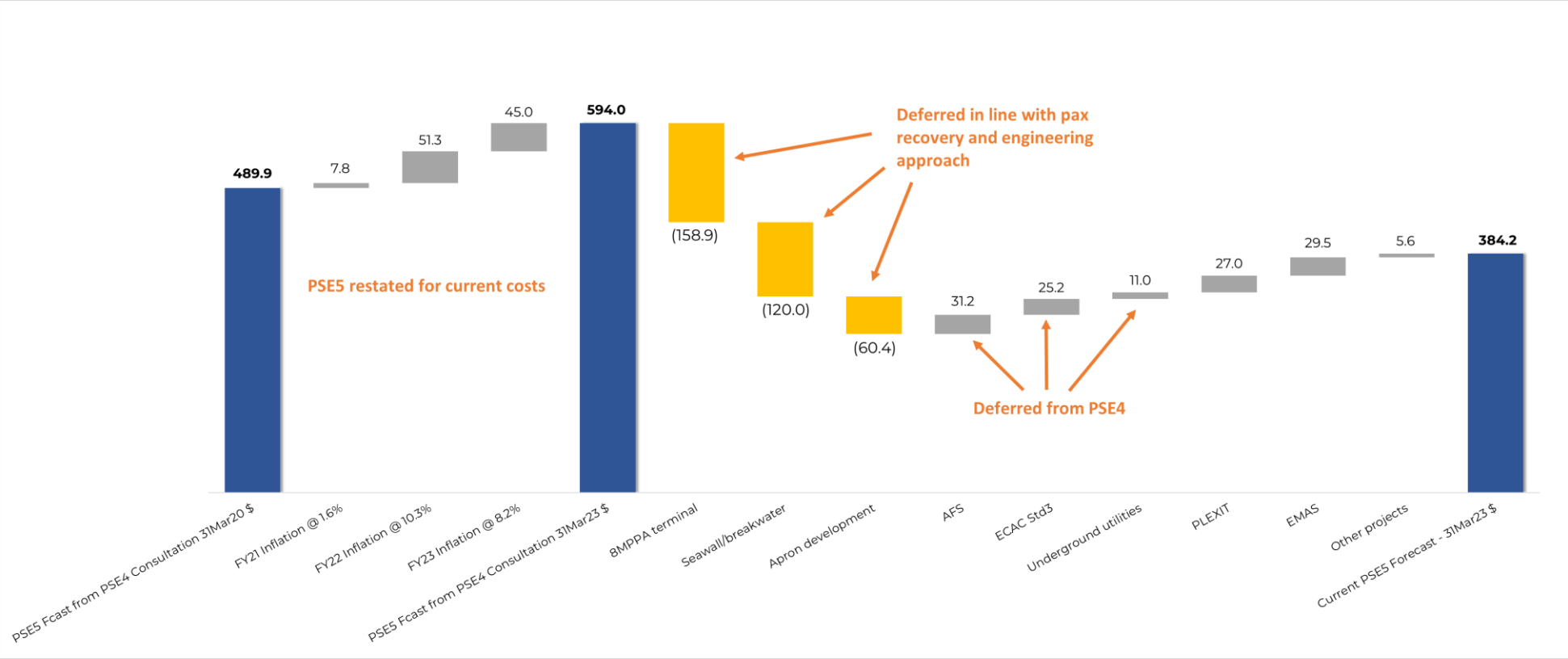
Outcome

28. The outcome of the proposed prices using the Building Block model is an increase in average charges from $19.07 in FY24 to $23.20 in FY29 (when counting the deferral and passenger wash up as PSE4 revenue). We consider this an excellent result for our customers when taking into account the uplift in regulatory WACC since the prior period, construction cost inflation, and a capex programme which remains significant despite reductions and deferrals.

29. We have currently structured prices with a step-up from FY24-25, and inflation adjustments thereafter. We recognise this creates an immediate price increase in the first year of the pricing period, however this mechanism enables revenue to be recovered from a larger passenger base (i.e. across the entire pricing period), while a smoothed revenue path would lead to higher prices in FY29. We are open to airline feedback about the best mechanism for smoothing revenue across the five years, and whether airlines prefer price increases to be allocated more steeply to the beginning or end of PSE5.

Summary of IPP components

Summary of capital expenditure revisions



PART B: COMMERCIAL AND REGULATORY CONTEXT

Introduction

30. Prior to 2020, every day approximately 17,500 passengers travelled through Wellington Airport following its highest annual growth in a decade for domestic travellers. International travellers were set to reach 1 million per annum for the first time, and the Airport planned substantial capital investment through its 2040 Masterplan to cater for the next 20 years of growth.

31. Covid-19 seriously impacted the entire aviation industry and WIAL was no exception. We acted quickly to resize, making the very difficult decision to inform 30% of staff their roles were being made redundant. We also immediately reprioritised capital expenditure to essential maintenance only, and restructured bank and bond finances to withstand the pandemic period. This included securing waivers of lender covenants and putting in place a $75.8 million shareholder support agreement with both Infratil and Wellington City Council. Shareholder dividends were foregone for two years. We have undertaken three bond issues since this time to extend and secure efficient long term funding.

32. WIAL also worked hard to ensure airlines were supported through this period as much as possible. This included deferring price setting consultation for the PSE4 period, holding airline charges flat for two years, providing rental abatements, deferring some airline payments into PSE5, and agreeing to a passenger washup to avoid windfall gains to either airports or airlines. We also offered a substantial discount against our own assessment of WACC, reducing our target return from 6.08% to 5.93%.

33. Several headwinds remain in the short term, with high inflation, construction cost challenges, and relatively high cost of capital. We continue to work hard to retain material cost efficiencies achieved during the pandemic, however some cost increases such as rates, insurance and construction cost inflation are largely outside of our control.

Sustainable economic growth for Wellington

34. At the same time as dealing with these headwinds, our focus over the last year has been on preparing for the return to growth over the medium term. Land use roadblocks have been removed, new space is available for development and projects are underway to cater for the continued growth in travel expected over the coming decades. We have secured designations over the airport's main site area and the recently acquired Miramar Golf Course land to the east, and have completed the first stage of development on the former Miramar South School site.

35. The growth and development of WIAL will be of great benefit to the wider city and region. As the international gateway for central New Zealand, the Airport supports businesses to prosper and tourism to flourish, generating employment and income for tens of thousands of Wellingtonians across the tourism, hospitality, entertainment, retail and transport sectors.

36. We make an effort to support this growth and economic activity in a way that is sustainable and sensitive to our neighbours. In the last year, WIAL has launched a new community sponsorship fund, established a community newsletter, and employed a Community Engagement Advisor in order to further our efforts in our local community. We are cognisant of the need to take community views and amenity into account as our footprint expands, and have established more effective channels for community consultation on key projects.

37. Some aspects of our pricing proposal are directly related to sustainability. Our capital expenditure plan includes the decarbonisation of our terminal buildings, proposing to finally rid the Airport of gas boilers and enable us to move entirely to renewable energy. We are partway through investing in an Airport Fire Station to replace the current outworn, poorly insulated building with a more energy

efficient one. And we propose to continue the decarbonisation of our vehicle fleet and partner with airlines to electrify ground service equipment and ensure we can cater to electric aircraft.

38. We are also working closely with our local community to reduce the impact of airport noise, through the successful Quieter Homes programme. A summary of the programme is included in Part O.

Economic regulation

39. Since the introduction of Information Disclosure requirements in 2010, extensive time and effort has been put into the refinement of the regulatory regime by airports, airlines and government agencies. Over WIAL's first four price setting events, airport regulation demonstrably matured and common ground increased, guided by the Commerce Commission's IMs. Airports welcome the transparency and public accountability introduced by Information Disclosure requirements.

40. The draft IM update released in June 2023 has reintroduced contention to the regulatory system, by proposing fundamental changes to the Commerce Commission's WACC methodology.

41. In WIAL's view, neither the 2016 nor the draft 2023 IMs can be directly applied for current purposes. The 2016 IMs rely on outdated data which does not reflect the obvious impact of Covid-19 on airports. The 2023 draft IMs offer no better guidance as they are still subject to consultation, and do not take effect until 2026 in any case.

42. We have therefore opted to calculate a bespoke WACC based on our best assessment of an updated WACC for airports, and leaving the 2023 draft IMs aside. Our WACC inputs are based largely on a report commissioned from HoustonKemp prior to the release of the draft IMs.

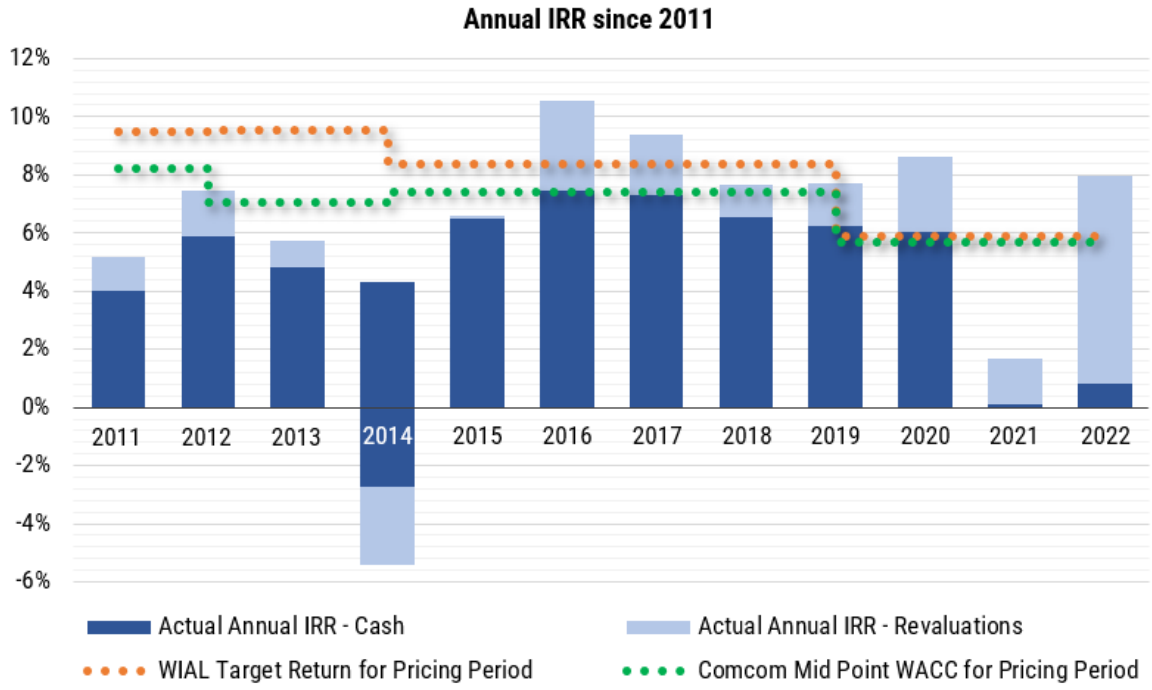
43. We have also proposed a small number of other non-IM compliant approaches, in areas that have been tested and endorsed previously by the Commerce Commission.

44. In our view, economic regulation is working to ensure airports consult thoroughly with airline customers, set prices within known boundaries and provide extensive transparency to interested parties. There is clear evidence that regulation is working, as demonstrated by WIAL's decision to reset prices in 2014 and Auckland Airport's decision to lower its prices in 2019 following reviews by the Commission.

45. However, while promoting careful price setting, the regulatory system must also enable and encourage investment, and ensure it is delivered in time rather than delayed. The regime must also ensure that airports' costs are recovered and that airports are able to earn a reasonable return to sustain investment, particularly in times of high cost of capital and high construction costs.

Wellington Airport's regulatory returns to date

46. An important consideration for any party evaluating WIAL's performance is the outcomes achieved since commencement of the Information Disclosure regime. The chart below shows WIAL's actual returns compared with key benchmarks since 2011. The total IRR over this period is 7.35% or 6.05% excluding revaluations:



47. We note that following the 2016 IMs review, the Commission concluded that from 2018 onwards it would only publish a midpoint WACC for airports. WIAL's prices for PSE1–PSE3 were set prior to this decision and were based on the airport's 75th percentile WACC at the time (target for PSE1 was 9.50%, PSE2 9.51%, PSE3 8.36% and PSE4 5.88%).

48. WIAL targeted a total IRR of 5.88% for the current PSE4 period. After 3 years, the period-to-date IRR is 6.06% compared with forecast of 4.55% (or 2.33% versus forecast of 3.07% excluding asset revaluations). This predominantly reflects a $22.5m deficit in regulatory income due to a slower than assumed recovery in passenger numbers, offset by the impact of high CPI on revaluations.

Price increases are unavoidable but we have worked hard to limit them

49. WIAL has worked hard to limit price increases in the prices proposed for PSE5, despite the drivers of our essential capital expenditure programme and unavoidable higher WACC.

50. It is important to recall that much of the price increase for this period is from the revenue deferral and passenger washup consulted on in PSE4. The outcome of that deferral and washup is that prices must increase in order to recover the deferred amounts. Airlines benefited from a real decrease in charges in PSE4 as WIAL worked to support its partners throughout Covid-19. Unfortunately, our cost of capital has also increased since PSE4, which is also leading to increased prices.

51. WIAL's charges remain among the lowest of major airports in Australasia. Operating costs are also low and we are striving to maintain efficiencies achieved during Covid-19 while improving services. Our capital expenditure programme has been modified in acknowledgement of the current environment and the delay in return to previous passenger levels.

52. We have proposed a price structure with the majority of the increase in the first year of the pricing period, followed by smaller increases for the next four years. This is the best way to spread revenue across a larger passenger base, thereby limiting the increase in per-passenger charges. The result is a lower price in FY29 than if price increases were smoothed over the period.

Commitment to consultation

53. WIAL is committed to consulting airline customers with an open mind regarding inputs to pricing. To date, we have:

- Provided an overview of proposed capital expenditure projects, including a site visit, to Substantial Customers;
- Presented consultation timetables and parameters for openness and transparency, while protecting confidentiality where required;
- Extended consultation to include the Board of Airline Representatives of New Zealand as an interested party.

54. Our consultation includes a six-week period for airline customers to respond to an Initial Pricing Proposal and a five-week period to respond to a Revised Pricing Proposal. WIAL will carefully consider feedback at each of these stages. We intend to issue final prices in early March 2024.

55. A complete consultation timetable is included as Appendix A.

PART C: CONSTRAINED PASSENGER NUMBERS

56. WIAL has commissioned InterVistas to provide demand forecasts for PSE5. The forecasting methodology is consistent with that applied for the Master Planning forecasts in 2017 and PSE4 forecasts in 2020/21. The methodology uses a combination of top-down econometric demand forecasting, accounting for trends in markets driven by GDP and air travel elasticities, and bottom-up supply assumptions, which consider anticipated schedule and aircraft changes particularly over the short-term. Supply assumptions are based on announced future changes to fleet and networks, and anticipated trends relating to future fleet and network changes accounting for exogenous growth.

57. Over the last 5 years, there have been significant changes to New Zealand's aviation market. The impact of Covid-19 saw a curtailing of air travel demand resulting in a downsizing of resourcing across the sector, the storage of aircraft, the deferral of aircraft maintenance and purchases, and behavioural changes in the way people choose to travel. As travel restrictions have gradually been removed, the sector has been challenged to restart services to meet surprisingly strong pent-up demand, resulting in bottlenecks across the system, slower recovery of capacity and higher than pre-Covid airfares.

58. InterVistas has prepared a forecast covering the current financial year (FY24) and then the 10-year period covering PSE5 and PSE6 (FY25-FY34) considering the wider aviation industry context, anticipated recovery to pre-Covid levels, and updated supply and demand assumptions. The forecasts were developed at the end of FY23 (March 2023) and will continue to be updated through the consultation process based on new information, updated trends and airline feedback. More detail on the passenger forecasts is available in the InterVistas forecasting report attached at Appendix B.

59. It should be noted that the first three months of FY24 have resulted in weaker than anticipated domestic passengers as a result of the grounding of some Air NZ A320/321 aircraft as well as lower than anticipated load factors in what continues to be a higher than pre-Covid airfare environment. Domestic capacity was 88% and passengers 83% of 2019 levels during April-June 2023, with passengers in July continuing a similar rate of recovery. International demand is also starting to weaken due to the reversal of pent-up demand while fares remain high. Further, on 19 May, Qantas announced the restart of Wellington-Brisbane from 29 October using a daily E190 aircraft, 1 year earlier than capacity increases assumed in the forecasts. The forecasts will be adjusted in the next stage of consultation to account for the new service.

60. Total passengers are forecast to increase from 5.8 million in FY24 to 7.1 million in FY29, a compound annual growth rate of 4.0% over the PSE5 period. Domestic traffic is expected to increase from 5.1 million passengers to 6.0 million with a CAGR of 3.2% and recovery to FY19 levels in 2025. International growth is forecast to be stronger, increasing from 694,000 in FY24 to 1.1 million in FY29, with a CAGR of 9.5% and recovery to FY19 levels in FY27.

61. Underpinning the forecasts are supply-side assumptions following route development changes over PSE5:

62. Domestic

- Air NZ A321Neo domestic capacity is forecast to continue to increase over the period with more aircraft in the fleet, freeing up ATR for more flying on larger regional markets, with marginal frequency improvements throughout the period through increased efficiencies. The Q300 replacement is anticipated to be deferred to beyond PSE5, and it is assumed a widebody domestic service will be introduced on WLG-AKL at the end of the period;

- Jetstar marginal frequency increases are forecast, limited by a fixed pool of aircraft with no anticipated up gauging; and

- Ancillary operators' incremental load factor is expected to increase, with introduction of larger electric aircraft towards the end of PSE5.

63. International

- Continued recovery of capacity on the Tasman is forecast by existing Tasman carriers in the absence of Virgin Australia;
- Ongoing frequency increases are included on OOL/NAN;
- The return of a fifth freedom widebody service is forecast in the middle of PSE5;
- Introduction of a new Australian short haul destination and seasonal Pacific Island service are included toward the end of the period.

Table: IPP Passenger Forecasts

		PSE5					
	2024	2025	2026	2027	2028	2029	CAGR 2024-29
Domestic	5,135,367	5,404,356	5,581,908	5,726,483	5,864,380	5,997,750	3.2%
International	693,882	752,321	836,489	931,479	1,009,180	1,090,666	9.5%
Total	5,829,248	6,156,677	6,418,398	6,657,962	6,873,560	7,088,417	4.0%

PART D: PSE4 DEFERRALS AND WASH UPS

64. During PSE4 consultation, weeks prior to WIAL's intended price setting date, the Covid-19 pandemic struck and created immense difficulty in setting prices and obtaining accurate forecasts. We were also very conscious of the need to avoid cost increases for airline partners during this difficult time, and despite WIAL's own destabilised financial circumstances, made the difficult decision to defer some revenue for collection in PSE5.

65. This history has led to two unique aspects of PSE5 pricing, which act to increase prices in the upcoming period. We acknowledge this reality, however this is a direct consequence of the wash up consulted on during the Covid-19 period in order to ease prices and risk at that time, when the most extreme negative consequences of the pandemic were similarly affecting all participants in the aviation industry.

Passenger wash up

66. Forecasting passenger numbers in the Covid-19 environment proved exceptionally challenging. In April 2020, WIAL set most pricing inputs, but due to the emerging pandemic we proposed a "pricing reset" in 2021 to take into account the impact of Covid on capital expenditure plans and passenger numbers.

67. Unfortunately, in the course of that year the pandemic did not become more settled. As we approached the pricing reset, the opening of the trans-Tasman bubble was imminent, and there were many positive indicators for the return of tourism and travel. On the other hand, many uncertainties remained including the possibility of localised lockdowns, and unwillingness of many people to travel in the circumstances. WIAL was cognisant of the downside risks in its forecasts, while airlines anticipated a faster recovery. It was unusual to see such disparity between WIAL and its airline customers in predictions of passenger numbers over a pricing period.

68. As a result, Air New Zealand proposed the following solution:

> *Noting the inherent uncertainty in forecasting, and particularly in the current circumstances, Air NZ considers there would be value in adopting a risk sharing mechanism in respect of passenger forecasts over the remainder of PSE4, where actual passenger revenue – based on actual passenger numbers – is used to calculate the revenue shortfall carry forward adjustment at the end of the period, rather than the forecast shortfall, as per the Proposal. With such a mechanism in place, WIAL would achieve a guaranteed full recovery over PSE4, including for the period impacted directly by Covid-19 (unlike other players in the sector), and the lower charges over PSE4 and PSE5 (assuming the recovery is faster than WIAL is forecasting) would enable Air NZ to maintain lower fares over the period.*

69. WIAL sought feedback on the Air NZ proposal from other airlines. BARNZ supported the proposal, and Qantas did not provide a view.

70. We noted in our Final Readjusted Prices covering document in April 2021:

> *WIAL agrees with Air NZ that this is the most sensible way to address ongoing uncertainty in passenger forecasts. A year ago, we had hoped for a more settled environment in April 2021; even when issuing the Pricing Readjustment in December we anticipated greater certainty around the future of trans-Tasman travel by now. Unfortunately this has not come to pass and the uncertainty remains.*
>
> *That uncertainty can be mitigated by washing up the difference between forecast and actual passenger numbers when calculating deferred revenue carried forward into PSE5. We also consider this is a pragmatic solution to what would otherwise be an area of ongoing*

disagreement between WIAL and airlines. By removing any contention around passenger numbers the wash up seems the best approach under the circumstances.

We have therefore decided to adopt Air NZ's suggestion and calculate the carry-forward into PSE5 based on actual passengers in the remaining years of this regulatory period. In combination with the approach to FY21 prices that we notified to airlines in March 2020, WIAL's aeronautical revenue for the period from 1 April 2020 to 31 March 2024 will be based on actual passenger numbers rather than forecast passenger numbers. This is an appropriate response to the unique challenge of setting prices in the face of the Covid-19 pandemic.

71. The Commerce Commission reviewed this risk share arrangement following PSE4 pricing disclosures, and concluded:

The Commission recognises that Wellington Airport and airlines will continue to face uncertainty regarding passenger demand for some time. The passenger demand washup mechanism as suggested by AirNZ and implemented by Wellington Airport seems appropriate in this context, to address under- or over-recovery of revenues by the airport, and share demand-related risk with airlines over the pricing period…

We find the use of the passenger demand washup mechanism, and the resulting risk allocation between Wellington Airport and its major customers, consistent with the purpose of Part 4 of the Act.

72. As it happened, actual passenger numbers for the pricing period were much lower than even WIAL's April 2021 forecast. The Trans-Tasman bubble was short-lived, and New Zealand remained beset by border closures and ongoing lockdowns until mid-2022. Recovery since then has been steady but passenger numbers are yet to return to pre-Covid levels.

73. Airlines benefited substantially during PSE4 from the relatively high forecast used to set PSE4 charges. Given actual passenger numbers, the accurate average FY24 price would have been $2.44 per passenger higher than the amount actually charged.

74. The shortfall results in a wash-up amount that is applied to PSE5 prices. As proposed in PSE4 consultation and endorsed by the Commerce Commission, this has been included as a carry-forward amount of $32.3 million into PSE5 and is therefore proposed to be distributed across charges in PSE5.

PSE4 deferred revenue

75. Additionally, during PSE4 consultation, WIAL proposed two revenue options to airline customers. The primary proposal, after resetting capital expenditure and passenger forecasts with the best available information at the time, would have increased prices from an average $12.97 to $16.63 by FY24.

76. We also proposed a concessionary price path, which limited this increase to $15.00 by FY24, with the remaining revenue deferred into PSE5.

77. Air NZ preferred the concessionary price path. BARNZ believed the deferral was "a step in the right direction, but not sufficient" and Qantas did not provide specific feedback on the proposed deferral. Following this feedback, WIAL adopted the concessionary price path, determining it a reasonable tool to mitigate price increases at the time.

78. The Commerce Commission reviewed this decision following PSE4 disclosures, finding:

In the later years of the PSE4 pricing period, it may still be appropriate for Wellington Airport to provide price relief to airlines, achieving lower revenues in the process, if travel demand has not

sufficiently recovered. We find that the deferral mechanism would be sensible under such conditions and have included the revenue deferral in our assessment of Wellington Airport's expected profitability. By including the revenue that has been deferred in our assessment of Wellington Airport's target return for PSE4, we recognise this revenue as contributing to the airport's profitability during PSE4. We expect that the deferral will be reflected in an opening carry forward adjustment for PSE5, and we will assess Wellington Airport's target return for PSE5 without double counting the impact of any deferred revenue from PSE4.

The revenue deferral into PSE5, in effect, transfers some of the risk associated with demand and price variation that would otherwise occur during PSE4. The revenue deferral also maintains an incentive for Wellington Airport to improve efficiency and reduce costs during the years of revenue deferral prior to its significant capital expenditure programme anticipated in PSE5, which would be consistent with the purpose in s 52A(1)(b) of the Act.

79. The delta between WIAL's nominal PSE4 revenue and the concessionary revenue was included as a $15.1m closing carry forward adjustment in PSE4. This amount is now proposed for recovery in PSE5.

Unspent PSE4 capex

80. We are cognisant that some planned capital expenditure for PSE4 remains unspent, due to the impacts of Covid-19 during that time, numerous lockdowns and passenger delays continuing for longer than expected. As discussed above, the return of passengers took longer than expected when prices were finalised in April 2021, with ongoing border closures and repeated lockdowns, setting back passenger recovery and consequently our capex programme.

81. As a result, given these very unusual circumstances we propose to make a one-off discretionary adjustment to our PSE5 pricing to return unspent capex to airline customers through a $9.8m opening carry forward adjustment in PSE5, though this is not required by the IMs. The carry forward balance was determined by calculating the reduction in post-tax returns that WIAL would have targeted in PSE4 had actual capex been used, with the balance being inflated to 31 March 2024 terms at WACC.

82. Attached to this paper is the Capital Expenditure Forecast Spreadsheet (Forecast Spreadsheet), at Appendix D, which details the forecast capital expenditure, individual projects and the allocation methodology applied. Attached as Appendix E is further information on each project.

Net revaluation carry forward

83. There is also a remaining net revaluation carry forward from PSE4, with $5.98 million remaining to be returned to airline customers in PSE5. This is discussed in Part I: Asset Revaluations.

PART E: COST OF CAPITAL CHALLENGES

Summary

84. For the first time since the introduction of Information Disclosure regulation, WACC estimates are increasing due to increases in the risk-free rate. This presents challenges for airports for whom costs are increasing, and airlines who bear this through increased prices; however, we note airlines have benefited from a low risk-free rate and consequent lower WACC consistently over the period the Part 4 regime has been in force, and particularly in recent years. The current increase in WACC reflects the market increase in the returns required to achieve NPV=0 over the life of assets.

85. As a general principle, we have been guided by the Commerce Commission's estimated mid-point WACC for WIAL, using the 2016 IMs as a starting point, with updates to asset beta and cost of debt based on latest data and WIAL's BBB credit rating.

86. In summary, WIAL has calculated a WACC for PSE5 of 8.55% which is comprised of:

- Cost of debt of 6.07%, slightly above the Commission's estimate due to WIAL's BBB credit rating;
- Cost of equity of 9.53%, above the Commission's mid-point under the current IMs due to higher asset beta assumptions reflecting updated data on the Commission's 2016 comparator sample.

87. The proposed WACC is consistent with the methodology underpinning the current IMs, but with updated parameters to incorporate current market conditions. The justifications for this WACC are outlined in HoustonKemp's report which is appended to this proposal. WIAL has made two further adjustments to HoustonKemp's assessment:

- Calculated asset beta over a 15-year period, rather than a 10-year period, in order to smooth the immediate impact of Covid-19 on asset beta data;
- Removed the Commission's 0.05 downward adjustment to asset beta, which is not based on any data or evidence.

This results in an asset beta of 0.745, slightly above Houston Kemp's estimate of 0.74.

WACC model and parameters

88. WIAL's starting point for calculating WACC was to apply the Commission's mid-point parameters, before making three changes: we have adjusted its cost of debt based on WIAL's BBB credit rating, and adjusted asset beta based on CEPA's analysis released by the Commerce Commission as part of the current IMs review.

Parameter	Commerce Commission benchmark WACC (2016 IMs) (1 June 23)	HoustonKemp recommended WACC (1 June 23)	Wellington Airport WACC (1 June 23)
Risk-free rate	4.29%	4.29%	4.29%
Debt premium	1.20%	1.60%	1.60%
Leverage	19%	15%	19%
Asset beta	0.60	0.74	0.745

Equity beta	0.74	0.87	0.92
Tax adjusted market risk premium	7.00%	7.00%	7.00%
Average investor tax rate	28%	28%	28%
Debt issuance costs	0.20%	0.20%	0.20%
Cost of debt	5.70%	6.09%	6.09%
Cost of equity	8.28%	9.18%	9.53%
Mid-point vanilla WACC	7.79%	8.72%	8.88%
Mid-point post-tax WACC	7.49%	8.46%	8.55%

Debt premium

89. WIAL proposes to adjust its debt premium to account for its BBB credit rating, as the IMs assume an A- rating.

90. In PSE4, we took a similar step to adjust for our BBB+ rating at the time. The Commerce Commission reviewed this and concluded:

> *In our view, the available evidence suggests the BBB+ assumption and the higher debt premium estimate of 1.60% are reasonable in Wellington Airport's specific circumstances and appear to be consistent with prudent levels of debt financing.*

91. We assume the same logic will hold for our now-lower credit rating and Houston Kemp has conducted analysis accordingly, resulting in a debt premium of 1.60%.

Asset beta

92. As noted in HoustonKemp's report, we have relied on CEPA's updated asset beta data which was provided to the Commerce Commission in the course of its IM review. CEPA's report utilises the methodology the Commission used to determine the current IMs, and so this estimate of asset beta is consistent with both the current methodology and updated market conditions.

93. However, we have departed slightly from HoustonKemp's recommended WACC inputs as noted above.

94. WIAL acknowledges the impact of updated asset beta estimates on WACC. In order to spread this impact over a longer period, we propose a 15-year estimate of asset beta rather than a 10-year estimate. We plan to continue this approach into the future. For clarity, this results in a downward adjustment to asset beta in the current period (from 0.79 to 0.745); but would be expected to have an upward impact in PSE7, when Covid-impacted data will continue influencing our asset beta estimates.

95. WIAL has elected not to adjust this downward by a further 0.05, as this approach is not based on any data or evidence.

96. This asset beta estimate reflects the real risk profile of airports as revealed by the pandemic. Covid-19 was an unprecedented shock to the global aviation industry and unquestionably influenced the systematic risk faced by regulated airport operators in New Zealand. It is therefore unsurprising that the data should reveal an increased asset beta.

97. Maintaining the NPV=0 principle that underpins airport regulation requires that the asset beta accurately reflect the systematic risk faced by airport operators. If asset beta is too low relative to actual systematic risk, airport operators will not have the opportunity to earn a normal return over time, thereby disincentivising investment.

98. Our bespoke estimate takes the Commission's tried and tested method applied through the IMs to date, while smoothing the impact of Covid-19 by adopting a 15-year estimation window. Maintaining the consistency of this approach ensures that investors will achieve a normal return over time as market conditions change; and ensures that shocks such as Covid-19 are adequately and accurately compensated for over time.

99. We acknowledge this approach is at odds with the Commission's draft 2023 IMs. The draft IMs are not determinative for the purposes of this pricing proposal, as they remain subject to consultation, and do not take effect until 2026 in any event. Our approach is consistent with the IMs that are currently in force, with updated parameters given changes in the market since 2016. We invite feedback from airlines on our proposed approach.

Earthquake risk

100. WIAL also believes it would be appropriate to make an upward adjustment to its target rate of return based on the risk of a large earthquake or tsunami event in Wellington. Given WIAL's location within the plate boundary of the Pacific and Australian tectonic plates, and its exposure to the highest seismicity in New Zealand, an uplift based on the risk of a serious earthquake is unequivocal. However, its impact on target rate of return is difficult to quantify, and therefore we are simply noting this point for now.

Forecast rate of return implied by proposed prices

101. The target rate of return for the pricing asset base is 8.55%.

PART F1: WELLINGTON AIRPORT'S CAPITAL EXPENDITURE PLANNING PROCESS

Background

102. WIAL's 130-hectare site is a small site for the provision of aviation services at the scale that operates on the site. The airport is constrained by its existing landholding, neighbouring residential properties, and by sea at both the northern and southern boundaries.

103. Even with the recent acquisitions of the former Miramar South School Site (1.8 ha), and southern half of the Miramar Golf Course (12.9 ha), WIAL is still significantly smaller in landholding than the other main airports in New Zealand, and continues to facilitate the highest number of passengers per hectare of all the main airports in Australasia.

104. As a result, we continue to seek innovative opportunities to ensure space is used as efficiently as possible, and to its full potential. Examples of projects which achieve greater efficiencies include the Northern Terminal swing gates which can facilitate both domestic and international operations, a management system for the baggage reclaim belts that allows a belt to be utilised for either international or domestic services as demand requires, and a spatially condensed turboprop apron with power-in/push-back operations, allowing intensive use of limited space when local weather conditions permit.

105. While the impacts of the Covid-19 pandemic continue to be felt across the industry, the gradual return to forecast growth and evolving operational requirements are again starting to place pressure on WIAL's existing infrastructure, and the operations of our customers.

Wellington Airport's capital expenditure planning process

106. The processes for capital expenditure planning at WIAL evolve over time to respond to changes in customer demand and passenger numbers, changes in services (or service quality) offered to passengers, and/or changes in operational regulatory requirements. Historically these processes have enabled us to respond to changes in passenger numbers while continuing to offer a high quality of service to passengers.

107. WIAL's main terminal opened in 1999, when the airport catered for 3.6 million passengers each year or an average of 9,800 passengers per day. Since that time, annual passenger numbers reached a pre-Covid peak of over 6 million, or approximately 17,500 passengers per day. Capital developments undertaken over the past 25 years have been a series of incremental changes to existing facilities to respond to short to medium term demand, or service level increases. The central premise of our planning during this 25-year period has been to achieve efficient use of (and where appropriate, expansion of) facilities within the existing airport footprint.

108. This approach has been an efficient and cost-effective way of delivering appropriate enhancements to the aeronautical assets (and our response to the pandemic to defer the 8MPPA terminal requires us to continue this approach in certain terminal areas over PSE5), but it will not suffice beyond the next few years. Long term increases in demand will outgrow the existing terminal structure, and a future expansion will be required in the near-term.

109. More recently the Covid-19 pandemic has meant our processes for capital expenditure planning have required adaptability in response to the unprecedented changes the industry has faced. This has included working with airlines to defer expenditure, and adjust plans as changes have occurred.

Consideration of capacity, demand and service quality requirements

110. The development of airport infrastructure requires long lead times in order to ensure developments reflect airline, and other airport user design and operational requirements, while also ensuring that customer expectations are met over the long term.

111. WIAL's planning process anticipates and responds to a number of planning horizons, as shown in the following table.

Planning Process	Future Demand Issues Considered
Master Planning	Master Planning seeks to ensure long term capacity is available when required. This includes: • Ensuring sufficient land is available to accommodate required levels of airport infrastructure[2] • Ensuring sufficient capacity will be available to meet aircraft stand or parking requirements, and passenger processing requirements within terminals • Reviewing airport site design and layout to ensure operational efficiency for aircraft movement • Ensuring that technical regulatory requirements are met for airport infrastructure • Ensuring that health and safety standards are met, or exceeded
Major Infrastructure Project Development	• Intended to deliver major projects in line with the Master Plan • Consultation with airlines and other parties focusses on design requirements to consider long term efficiency, service quality and cost issues • Regulatory requirements for aircraft operations or passenger processing also addressed
WIAL Business Planning/ Pricing Consultation	• Processes to address shorter term five year time horizons • Allows responses to shorter term capacity and service quality issues • Requires incremental approach to capital expenditure projects where major assets are enhanced or altered • Enables WIAL to consult on capital expenditure requirements with airlines
WIAL Annual Budgeting/ Operational Forums with Airlines and Agencies	• Shorter term capital expenditure requirements considered • Enables response to immediate capacity, efficiency or service quality issues where short term asset changes are possible

The 2040 Master Plan

112. In 2019, WIAL issued the 2040 Master Plan to establish a long-term development path. The Master Plan addresses a ~20 year planning horizon and shows the prospective development that is expected to be required to accommodate several long term traffic forecast scenarios.

113. The 2040 Master Plan was founded on a different approach from previous iterations in several key respects:

[2] This continues to be a major challenge for WIAL which has a very small land footprint compared to other airports with comparable passenger numbers. For example, WIAL's total land holding is circa 110 hectares, compared to Christchurch and Auckland Airports, which have 750 and 1,500 hectares respectively.

- It illustrates facilities that will be required to support three specific levels of demand [3];
- Changes to the land holdings needed to provide the identified airport services, at each demand level are identified, and
- The combined terminal and apron layout necessary to accommodate the increased passenger numbers and expected aircraft mix has been reconsidered.

114. WIAL undertook a formal consultation process on the 2040 Master Plan with its substantial airline customers and other affected parties. The consultation process commenced in July 2017, and included considerable engagement over a period of ~18 months. In addition to the consultation with airlines, and other affected airport agencies, the draft Master Plan was subject to public consultation.

115. Post-Covid, the 2040 Master Plan remains the foundation of our future planning. The Master Plan projects have been extensively consulted with airlines, with broad agreement on the way forward. In our view, the Master Plan continues to set out the most efficient way to eventually cater to passenger growth, protect for long-term compliance with ICAO standards, and meet evolving regulatory requirements.

116. However, Covid-19 has obviously set back forecast growth and consequently has required a pause in our infrastructure plans. Our current estimate is that passenger numbers will reach 8MPPA by 2035, previously forecast for 2028-29; a 5-6 year delay. We have consequently delayed our terminal and apron developments by approximately five years. We intend to begin planning and development work for the 8MPPA terminal within the PSE5 period, and therefore refer to it in this document and have provided detail around planned expenditure and timeframes. However, as these assets will not be commissioned until PSE6, they do not materially impact current pricing.

Capex planning for smaller development projects

117. Along with the key development projects arising from the 2040 Masterplan, other projects are considered necessary to address more imminent congestion and service quality issues, business growth or compliance requirements within a five-to-10-year time frame. These are identified by WIAL from feedback from ongoing operational forums with WIAL's customers, observation of short-term congestion points, remediation of service quality concerns or in response to impending changes in regulatory requirements by government agencies.

118. Consultation with substantial customers is undertaken in two main ways:

- Key or large projects – consultations are undertaken with substantial customers. The consultations allow the proposed design, scope, timing and costs to be reviewed and amended or refined as discussions progress.
- Smaller projects – forecasts for these projects are provided to substantial customers in pricing consultation. In addition, WIAL engages with its airline customers and keeps parties to the engagement during price consultation informed through operational meetings, such as the monthly TEAM WLG operational forum meetings which include attendees from WIAL, the airlines and Government agencies. These meetings have included discussions on recent projects such as installation of new Electric GSE charging equipment, Baggage Handling System (BHS) resilience works, and on congestion issues within the terminal.

[3] Total passenger numbers to equal 8 million, 10 million and 12 million from the actual 6.3 million in 2018.

119. The consultations assist WIAL to ensure that the projects are appropriately defined and designed, will meet business requirements and are efficient in terms of scope, cost and timing.

120. However, WIAL also acknowledges that not all projects are supported by all airlines. In these circumstances WIAL may need to form final conclusions on the projects after considering the following:

- Competing interests of different airlines - for instance some airlines may support incremental terminal projects less than others, depending on which parts of the terminal, or aircraft gates, airlines are customarily using;
- Competing interests of airlines and passengers - for instance airlines may consider a facility to be adequate while passenger feedback, such as from ASQ surveys, may indicate a lack of satisfaction with the facility;
- Medium term demand forecasts. An element of capacity should exist to accommodate a forecast increase in demand or accommodate congestion at peak periods; and
- Differences in view on the level of operational compliance required – for instance WIAL currently operates with dispensations from the New Zealand Civil Aviation Authority (NZCAA) for certain areas of non-compliance with International Civil Aviation Organisation (ICAO) requirements. WIAL considers it appropriate to reduce the level of dispensations required over time where it is efficient and practicable to do so.

Operational capex requirements

121. There is also a wide range of capital expenditure that is required to maintain the ongoing operation of the airport. For example:

- Apron, taxiway and runway infrastructure maintenance.
- Maintenance of terminal buildings and building systems, (such as fire systems, heating and ventilation systems, lifts, and escalators).
- Refinement of facilities for passengers and airport visitors.
- Vehicle replacement, and
- Information technology improvements.

122. Individually the expenditure items are not substantial and fall well below the $5 million capital expenditure threshold established for information disclosure. However, there are notable exceptions such as when a runway overlay may be required.

123. Consideration of these projects is an important part of WIAL's business processes including the completion of annual company budgets and five yearly business planning forecasts. As part of its annual budget process, WIAL completes a five year capital forecast which includes a review of longer term key projects, and input from across the business for operational capital expenditure requirements.

124. These annual forecasts for the year ended 31 March 2024 have formed the starting point for preparation of the PSE5 forecast in respect of WIAL's operational needs.

125. The current forecasts for operating capital expenditure are included in the consultation material provided to substantial customers for pricing consultation.

Historical performance of actual versus forecast expenditure

126. WIAL's actual versus forecast capital expenditure for PSE1 – PSE3 summarised below:

	PSE1 2008-12	**PSE2 2013-14**	**PSE3 2015-19**	**Total**
	$000	**$000**	**$000**	**$000**
Price setting forecast	74,288	47,970	124,864	247,122
Actual capital expenditure	83,644	19,495	139,787	242,926
Total over/(under) spend vs forecast	**9,356**	**(28,475)**	**14,923**	**($4,196)**

135. The cumulative spend over this period is within 1.7% of forecast and demonstrates WIAL's ability to deliver on its capital expenditure plans.

136. After 3 years of PSE4, WIAL has spent $77.2m versus the $109.9m forecast. This largely reflects the slower than expected recovery in passenger numbers which has both limited WIAL's funding capability and deferred the demand for growth-driven investment.

137. As stated in Part D, we propose to wash up the difference in charges relating to proposed vs actual capex for PSE4. We believe that this, along with our prior track record of accurately meeting forecast spend, should give airlines confidence in the accuracy of our forecasts and intention to only propose capex which is prudent and deliverable.

PART F2: REDUCED CAPITAL EXPENDITURE PROGRAMME – BACKGROUND AND SUMMARY

Introduction

138. This section sets out the background, approach and assumptions for WIAL's capital expenditure ("capex") forecast, as well as the value of commissioned projects, for PSE5.

139. There are a number of major projects where capital expenditure is proposed to commence in PSE5, but the projects are not completed, and do not impact pricing, until PSE6. However, because the expenditure commences in PSE5 WIAL has included comments on these projects in the IPP.

140. The capex forecast includes:

- Projects revised or deferred following the Covid-19 pandemic;
- Projects deferred from PSE4 which are now urgently required to replace outworn infrastructure and meet new regulatory standards;
- Additional projects proposed for PSE5 – interim terminal fixes, EMAS and Plexit costs.
- Operating capex - expenditure that preserves the functionality of existing facilities and/or maintains compliance with operational and statutory requirements.

141. Further comment on the main items within each group of expenditure are provided later in this section. Capital expenditure is then allocated to aeronautical activities. Allocation factors have been established where assets are shared, following consideration of the expected use of the assets and the IM requirements for asset allocation.

142. Attached to this paper is the Capital Expenditure Forecast Spreadsheet (Forecast Spreadsheet), at Appendix D, which details the forecast capital expenditure, individual projects and the allocation methodology applied. Attached as Appendix E is further information on each project.

Summary of revision and reductions

143. WIAL has previously consulted extensively on its 2040 Masterplan and associated developments. This formed the centrepiece of PSE4 pricing consultation, and airlines were broadly in agreement with the proposals for future development.

144. During PSE4 consultation, we indicated that capital expenditure of $489.9 million was expected in the years FY25-29, in order to enable construction of new terminal and apron developments, a new baggage handling system, seawall redevelopment, and ECAC Standard 3 screening. Inflated for today's costs, this would now amount to $594 million in required capital spending.

145. Obviously, Covid-19 has set back these plans and we have worked hard to revise our capital expenditure programme accordingly. Compared to the $594 million previously stated, we now propose $384.2 million in capex for the period.

146. We acknowledge this is still a significant amount; however once broken down by project, each aspect is considered to be prudent for its own reasons. Some costs are unavoidable due to regulatory or resilience requirements, and construction cost inflation continues to increase. We have deferred the commissioning of terminal and future apron assets to PSE6, so these Master Plan developments do not impact current proposed pricing.

147. Our starting point has been to defer or delay construction of the new terminal and apron due to the impact of Covid-19 and restrained passenger numbers now anticipated. The 2018 forecasts used to develop the Masterplan had WIAL reaching 8.2 million passengers per annum in FY29-30. We are

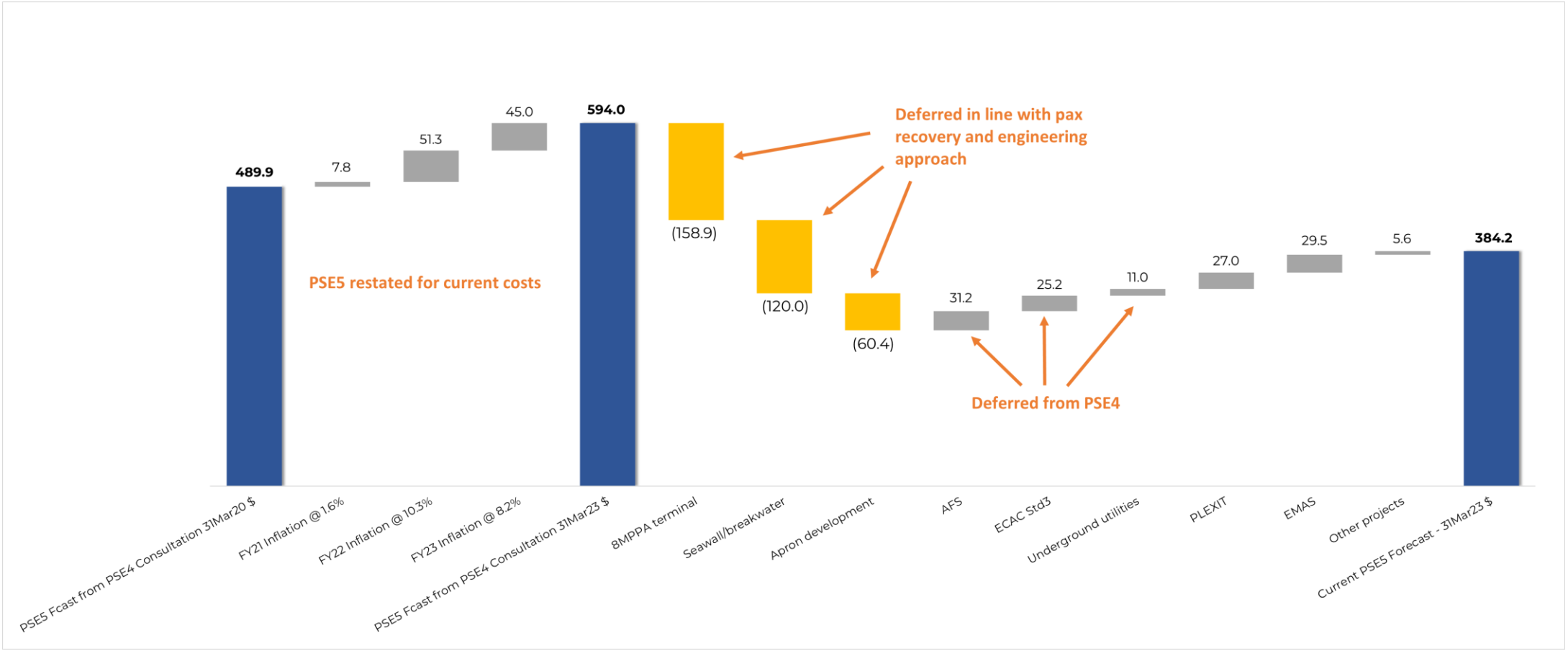
now expected to surpass 8 million passengers by 2035, indicating current forecasts are that the works identified as being required by the Master Plan have been effectively delayed by 5-6 years.

148. Accordingly, we propose to commence planning and early works for the identified Masterplan developments in PSE5, while not commissioning these assets until PSE6. This amounts to a reduction of $158.9m for the terminal, and $60.4m for apron development, compared to previous PSE5 forecasts.

149. The essential seawall resilience project remains a material item, however we have worked to mitigate short term risks to enable the staging and deferral of this investment over a longer period than previously anticipated.

150. Other projects have been deferred from PSE4 and are now underway, including the replacement Airport Fire Service building which has been planned and consulted on for many years now; ECAC Standard 3 upgrades; and improvements to underground utilities.

151. The anticipated transfer of airfield power and lighting from Airways to WIAL (PLEXIT) is contributing to capex and opex costs in the pricing proposal, however this ought to result in a corresponding decrease in Airways charges faced by airline customers.


489.9
7.8
51.3
45.0
594.0
(158.9)
(120.0)
(60.4)
31.2
25.2
11.0
27.0
29.5
5.6
384.2
PSE5 restated for current costs
Deferred in line with pax recovery and engineering approach
Deferred from PSE4
PSE5 Fcast from PSE4 Consultation 31Mar20 $
FY21 Inflation @ 1.6%
FY22 Inflation @ 10.3%
FY23 Inflation @ 8.2%
PSE5 Fcast from PSE4 Consultation 31Mar23 $
8MPPA terminal
Seawall/breakwater
Apron development
AFS
ECAC Std3
Underground utilities
PLEXIT
EMAS
Other projects
Current PSE5 Forecast - 31Mar23 $

PSE5 forecast summary

152. WIAL has prepared a detailed capital expenditure forecast which is detailed in the worksheet attached at Appendix D. The worksheet is in real 31 March 2023 dollars.

153. WIAL's aeronautical capital expenditure forecast in real dollars is summarised below for PSE5 (refer to the end of this section for detail on capex in nominal terms and for commissioned assets).

31 March 2023 Real Terms	2025	2026	2027	2028	2029	Total
	$000	$000	$000	$000	$000	$000
Infrastructure/Growth	97,428	72,665	64,295	48,712	23,100	306,200
Leasing Developments	25,000	14,000	-	-	-	39,000
Operational/Maintenance	19,064	21,032	14,109	11,895	11,941	78,041
Total Capital Expenditure	**141,492**	**107,697**	**78,404**	**60,607**	**35,041**	**423,241**

154. The forecast capex commentary and values used in this chapter reflect 31 March 2023 real dollars and are consistent with the capex schedule shown in Appendix D.

155. The real capex values are then indexed by an allowance for construction cost inflation in the building block model.

156. The cost of construction inflation assumption is based on NZIER's forecast for the non-residential building cost index (as at Q1 2023):

	2024	2025	2026	2027	2028	2029
Forecast Index	5.0%	3.9%	3.3%	2.7%	2.4%	2.4%

157. WIAL's forecast capex in nominal terms is as follows:

Nominal Terms	2025	2026	2027	2028	2029	Total
	$000	$000	$000	$000	$000	$000
Total Capital Expenditure	154,361	121,369	90,744	71,828	42,526	480,828

158. Assets are only included in the regulatory asset base when the assets are completed and in use.

159. Therefore, the amounts actually proposed to be capitalised such that they will impact the forecast regulated return for PSE5 are summarised below. Note that these figures exclude asset transfers which are covered in part J.

Capitalised Values	2025	2026	2027	2028	2029	Total
	$000	$000	$000	$000	$000	$000
Infrastructure/Growth	68,095	91,392	41,858	125,628	27,029	354,002
Leasing Developments		57,015	-	-	-	57,015
Operational/Maintenance	19,520	22,382	17,867	12,709	13,070	85,548
Total Capital Expenditure	**87,615**	**170,789**	**59,726**	**138,337**	**40,098**	**496,566**

PART F3: KEY CAPITAL EXPENDITURE PROJECTS FOR PSE5

160. This section provides a summary of the key capital expenditure projects included in the pricing forecast for PSE5, including those that may not be completed until PSE6. Further detailed comments on each of the projects, is provided at Appendix E.

161. WIAL has already undertaken discussions with airlines on the projects and this engagement will continue during PSE5.

Projects revised or deferred following Covid-19 pandemic

8MPPA terminal construction (now proposed to be commissioned in PSE6)

162. WIAL undertook extensive consultation with customers on the construction of an 8 million passenger per annum (8MPPA) terminal in developing the 2040 Masterplan, and as part of the PSE4 consultation process. An extension of the terminal to the south, and a "flip" of international and regional operations is the most efficient way to accommodate passenger growth beyond the near-term.

163. In recognition of the slight deferral in demand caused by Covid-19 and the current high-WACC environment, we have proposed to defer commissioning of this major project to PSE6.

164. The 8MPPA terminal has still been included in this proposal as a key capital project, as its deferral provides context for other key capital projects, including the proposed Bag Factory and Terminal Optimisation Programme.

Apron Development Programme (now reduced from previous PSE5 forecasts)

165. The proposed programme involves the progressive development of a flexible apron to accommodate existing demand and forecast growth in passenger numbers and aircraft movements to 8MPPA. The apron expansion scheduled for PSE5 includes construction of seven remote stands to the south, a remote stand to the north (under the existing Airport Fire Station), and reconfigurations of existing stands around the South and Southwest piers, to improve utilisation and resilience in typical wind conditions.

166. To enable existing areas of apron to be reconfigured ahead of the future relocation of international and regional operations, and to ensure delivery of new apron can be aligned with delivery of the future 8MPPA terminal, additional apron capacity is required in the near-term over and above that driven by the demand.

167. The additional capacity created during PSE5 addresses this, and is an enabler for future staged apron development in PSE6, aligning with the future 8MPPA terminal expansion, and the Master Plan.

Marine Defences Programme (now proposed to be staged over 10 years)

168. The programme consists of the ongoing maintenance and upgrade of all marine protection structures to ensure that the integrity of the airfield platform and instrument landing system is preserved and provides resilience against seismic events; future climate change; sea level rise and the increasing frequency and intensity of storms.

169. WIAL consulted with airlines on the need to renew and upgrade the marine defences ahead of PSE4, based on peer-reviewed recommendations from marine engineers BECA. Investigations at the time concluded that the structures are nearing the end of their life, are under-designed by today's standards, and their replacement is recommended.

170. During the Covid-19 reset of capex forecasts, WIAL proposed to continue planning for renewals, but defer major works until future pricing periods. BECA were subsequently further engaged to consider options for seawall replacement and maintenance strategies, and to manage risk until the existing seawalls are replaced with resilient structures that meet modern design requirements. The work to date has included early contractor involvement on constructability and a peer review of design assumptions.

171. BECA's Sea Defence Structures Inspection report May 2023 informs the proposed programme of works for PSE5 and beyond by considering the current condition and risk of the marine defences. Their recommendation states:

> *"…it is recommended that the sea defence renewals project be completed within the next approximately ten years. Preferably, the renewal project is completed within the next 5 years. However, if necessary, the life of the sea defences could be extended for up to approximately 10 years with increased inspection and maintenance effort, noting the increasing risk of storm damage…over that time as the assets continue to age and deteriorate."*

172. While we are cognisant of the current WACC environment, and have proposed to adopt the extended time frame (of 10 years to complete the seawall works) for this pricing period, we note that there is the potential that storm damage or an acceleration of seawall deterioration may require the advancement of works. In the event of this occurring, we propose a Specific Project Charge [4] will be levied to fund this.

Projects deferred from PSE4 which are now urgently required to replace aged infrastructure and meet new regulatory standards

ECAC Std3 Bag Factory

173. The existing Baggage Handling System (BHS) at WIAL was commissioned in early 1999 and since then has been expanded and altered to meet growth, additional security/screening requirements, and airline user requirements. The current BHS is severely space constrained within the existing bag hall, and does not allow for required compliance, efficient growth, or the increased requirements for modern manual handling and health and safety systems.

174. In 2018 it was confirmed that the new European Civil Aviation Conference (ECAC) Standard 3 screening machines need to be operational by the end of 2021, and at the time of PSE4 consultation, the timing of those requirements, as well as the need to expand the terminal presented a solution to incorporate the new BHS into the new terminal. Post Covid-19, the NZ CAA updated the Std 3 compliance requirement to FY24, but that target date is currently under review.

175. The effects of the pandemic on passenger forecasts (and the resulting deferral of the 8MPPA terminal extension), the deferral of Std3 Compliance dates, and Air New Zealand's surrender of the flight catering facility ground lease in 2021 has provided WIAL an opportunity to review its BHS strategy, and in particular the long-term location of the future system, and the opportunity to decouple it from the 8MPPA terminal development.

176. The proposed standalone Bag Factory will effectively address the compliance, capacity, reliability, and manual-handling issues which plague the current system. Decoupling the BHS from the terminal and moving to a Bag Factory concept has the following benefits:

[4] An SPC charge has previously been consulted upon with airlines for application to discrete capex projects, see PSE4 Revised Pricing Proposal dated 6 December 2019, para 104

- ability to cost-effectively meet regulatory compliance targets, and address existing capacity, reliability, resilience, and manual handling issues without requiring new terminal construction.

- ability to house the system in a building with significantly lower construction costs than equivalent volume/area terminal construction.

- ability to expand the baggage system vertically without being constrained by current and future terminal floor levels, allowing a reduced footprint on WIAL's constrained site.

- opportunity to refine future terminal expansion requirements, with ~5000m2 less space required for a BHS within the future terminal.

- relative ease of future expandability to meet demand and regulatory requirements, vs a system constrained by hard terminal infrastructure.

- minimised impact to existing BHS ops during construction of the new system.

Airport Fire Station (AFS) relocation

177. The existing AFS is at the end of its useful life and is no longer fit for purpose. Its location is also not consistent with the 2040 Masterplan for efficient airfield operations.

178. This project replaces the existing end-of-life, inefficient, and ill-situated building with a modern and resilient fire station, which is sited to make efficient use of available land. Upon completion, the existing fire station is planned to be demolished to allow for aircraft parking and long-term taxiway realignment in line with the 2040 Masterplan.

179. We consulted with airlines on this project for PSE4, and it was then deferred to the end of PSE4 as part of the Covid-19 capex forecast reset (also consulted with airlines). Enabling works are now underway, and commissioning is planned for FY26.

TC3 BHS and Check-in Resilience

180. This Project takes advantage of enabling and resilience enhancement works from PSE4 by extending the existing check-in and bag drop systems to the south, improving screening capacity and system reliability, and enabling connectivity to the proposed Bag Factory.

Decarbonisation Programme

181. The proposed Decarbonisation programme includes investment in infrastructure to enable WIAL and its customers to meet published emissions reduction targets, and increase efficiency.

182. The main component of the programme is the replacement of WIAL's gas boiler terminal heating and cooling systems. Major components of the terminal space heating and cooling infrastructure are at or approaching the end of their economic lives. The renewal and replacement of these components was planned to occur as part of the 8MPPA terminal extension, now deferred into PSE6. The programme includes a replacement of the terminal's end of life and at-capacity gas boiler heating system with a modern, sustainable, and energy-efficient heat-pump alternative.

183. To enable a reduction in customers' scope 1 & 2 emissions (and reduce WIAL's scope 3 emissions), the programme also includes progressive rollout of aircraft electrical ground power, pre-conditioned air (PCA), and ground service equipment (GSE) charging facilities at aircraft stands.

184. WIAL is also planning for infrastructure to support future aircraft types, including electric and hydrogen-powered aircraft. At this stage we request more information from airline customers

relating to infrastructure needs, in order to ensure we can support this and incorporate it into our forecast in our Revised Pricing Proposal. In particular, we note airlines are planning to launch electric demonstrator services, and possibly regular commercial flights, within the PSE5 period. We are eager to understand as much detail as possible regarding fleet mix and energy requirements.

Underground Utilities

185. Some of the underground utilities at WIAL are at the end of their useful lives. Many date back to the original airport construction, and their condition, location, and capacity are not considered to be at appropriate levels.

186. This project is designed to relocate and upgrade trunk services which are under (current and future) aircraft operational areas to minimise risk to aircraft operations and improve service resilience. An outage in one of the many utilities which are currently under aircraft operational areas could cause significant delays, as parts of the airfield would require closure while the service is repaired. The proposed new service corridors are outside of significant operational areas and allow for maintenance activities to occur with minimal disruption.

Flight Catering Relocation

187. The existing flight catering facility is 45 years old, is at the end of its useful life and provides a poor level of amenity. The location of the facility is not consistent with the 2040 Masterplan, and as such any further upgrades to the facility are considered to be uneconomic.

188. This project is proposed to include the construction of a new sustainable and efficient flight catering facility located at a new site to the north of the airport on the former Miramar South School site (7 Kauri St). The demolition of the existing facility would allow for the construction of the proposed ECAC std 3 Bag Factory.

Logistics Hub

189. The existing freight facilities at WIAL are split across five separate buildings. With the exception of the DHL leased warehouse all of the buildings are beyond or approaching the end of their intended design life, provide generally poor amenity, do not meet current earthquake code requirements and are not consistent with the 2040 Masterplan.

190. This project is proposed to include the construction of a purpose built, flexible freight processing facility that meets regulatory and biosecurity requirements, while also allowing airfield geometry and capacity to be improved.

New projects proposed for PSE5

Terminal Optimisation programme

191. In response to the effects of the pandemic on passenger volumes and forecasts, and in recognition of the cost pressure on customers, WIAL has proposed to defer major construction and commissioning of the 8MPPA Southern Terminal Extension to PSE6.

192. Several existing terminal processors (International arrivals, baggage reclaim, and North Pier departures), which prior to Covid-19 were at or beyond capacity, are now returning to those levels of demand, resulting in congestion, delays to passenger processing, and IATA Sub-Optimum Levels of Service.

193. WIAL has proposed relatively minor, but specifically targeted works to reconfigure existing terminal processors which are at or beyond capacity to efficiently accommodate interim demand until the 8MPPA terminal is completed.

Engineered Material Arresting System (EMAS)

194. This project aims to enhance Runway Safety at WIAL by upgrading of the existing 90m long Runway End Safety Areas (RESA) and installing an Engineered Material Arrestor System (EMAS) at both runway ends.

195. EMAS is a passive system which decelerates an aircraft, and brings it to a safe, calculated stop in the event of an overrun.

Airways Power and Lighting Divestment (PLEXIT)

196. Provision of Airfield Ground Lighting (AGL) is a Part 139 requirement. In NZ, AGL infrastructure has historically been provided at airports by Airways NZ (Airways). In 2019 Airways made changes to their services framework, which included the divestment of their power and lighting assets to airports.

197. Airways notified WIAL of their intention to divest their AGL in late 2020. Since then, WIAL has commissioned asset condition inspections and conducted due diligence on the assets. WIAL is now in negotiations with Airways on the transfer of the AGL assets from Airways to WIAL, to occur at the commencement of PSE5.

198. As well as the transfer of the value of the existing assets from Airways to WIAL, PSE5 includes a programme of works to progressively remove obsolescence, increase serviceability, and improve the resilience of this critical system.

Operating capital expenditure for PSE5

199. Operating capital expenditure typically comprises a number of items which are usually not material in their own right. Planning for this expenditure comprises identification of specific works on a long-term basis where this can be achieved, such as for airfield engineering and facilities maintenance, while providing an allowance for expenditure that is expected to be required but which typically occurs on a more ad hoc basis such as minor building works.

200. WIAL reviews its forecast operating capital expenditure on a detailed basis annually as part of its budgeting process. During this process WIAL:

- Establishes specific items where expenditure is required in the ensuing year; and
- Reviews expert advice received in respect of technical areas such as engineering works and information technology upgrade requirements.

201. WIAL also periodically reviews its longer-term forecasts to consider whether changes in timing of forecast expenditure are required in subsequent years.

202. These processes in combination seek to ensure that expenditure is efficiently incurred, operational and statutory compliance obligations are maintained, and addresses shorter term service deficiencies where identified.

203. We provide comment below on the major operating capex cost categories for PSE5. A detailed breakdown of the forecast items proposed is contained in Appendix D.

Airfield engineering - maintenance

204. Airfield engineering works are in accordance with long term asset management plans for the airfield and have been identified following consultation and advice from our external consultants Aecom.

205. The specific works vary from year to year with the projects required identified by assessment of the physical life and maintenance requirements of the relevant facilities, with an emphasis on managing risks associated with the single runway type of fleet mix.

206. Smaller specific projects included in the forecast include (a more detailed list is included in Appendix D):

- Construction of an area of pavement suitable for high-power aircraft engine run-up;
- Ongoing replacement of apron flood lighting masts, and upgrade of lights to LED;
- Installation of additional stormwater treatment capacity; and
- Other smaller projects to improve runway efficiency.

Terminal projects

207. Similarly, there are a number of smaller projects included for the terminal activity including:

- construction of a jet and turboprop bus lounges for bussing services expected to be required for aircraft boarding;
- general capital maintenance on the terminal including lifts and escalators; and
- Aerobridge upgrade and replacement works in line with asset lifecycles.

PART G: MAINTAINING LOW OPERATING EXPENDITURE PER PASSENGER

Summary

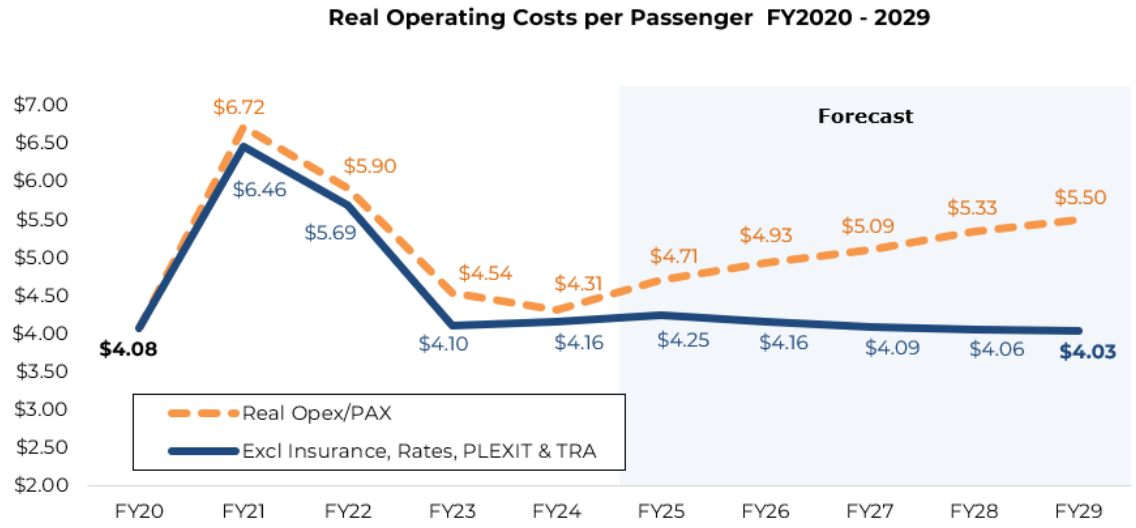
208. This section sets out WIAL's methodology and key assumptions for PSE5 proposed operating expenditure forecasts. Note that this section excludes Noise Mitigation activities which have been forecast separately and are described in Part O.

209. The PSE5 forecast approach remains consistent with PSE4 and applies the same cost allocation model WIAL uses for its annual information disclosures.

210. Comparing actual expenditure outcomes with previous forecasts demonstrates the historic reliability of our methodology and assumptions. Total operating expenditure spend for the 5 years of PSE3 was $2.0m / 2.0% above forecast and a similarly accurate outcome is projected for PSE4.

211. In responding to the impacts of Covid-19, WIAL achieved significant cost savings. Despite the challenging cost environment and recovery in passenger numbers, WIAL is committed to retaining these savings wherever possible and this is reflected in the PSE5 forecast assumptions.

212. Excluding the largely uncontrollable increases relating to Airport Fire Service (AFS) staffing, insurance, rates and PLEXIT, real operating costs per passenger are forecast to remain below pre-Covid levels ($4.03 in FY29 vs $4.08 in FY20). We aim to continue this trend over the long-term with growing passenger numbers and efficiencies of scale.



213. WIAL considers that its PSE5 forecast is reasonable and demonstrates our commitment to operational efficiency whilst maintaining a high standard of airport with commensurate high quality of service. Consistent with previous reviews, operating costs are low by comparison to other airports in both Australasia and worldwide.

214. Detailed operating expenditure forecasts are included in Appendix C.

Forecast approach and assumptions

215. WIAL's whole of company budget for FY24 has been used as the base year for the forecasts proposed. The annual budget is subject to a detailed and robust review prior to approval by the company's Executive and Board and actual year-to-date expenditure indicates the budget remains accurate.

216. The budget has been allocated to regulated and unregulated activities using a methodology consistent with the IMs. WIAL has applied the same cost allocation model used to prepare annual information disclosures and previous PSE forecasts.

217. The allocated FY24 budget was then rolled forward for five years, taking into account assumptions including CPI, service levels and changes in operational requirements. Each of these assumptions is commented on below.

Inflation

218. CPI has been assumed consistent with the rates applied for the indexed revaluations of WIAL's asset base. The rationale for this is discussed in Part I (Asset Revaluations):

Year ended	FY25	FY26	FY27	FY28	FY29
CPI %	2.62	2.27	2.19	2.05	2.02

Passenger Numbers

219. We have allowed for specific passenger related costs to increase by the growth in passenger numbers. The proposed passenger forecasts are addressed separately in Part C: Constrained Passenger Numbers.

220. The costs where this assumption has been applied include:

- Cleaning;
- Rubbish removal; and
- Toilet consumables.

Salary Inflation

221. We have forecast employee remuneration for existing staff positions to increase at our assumed inflation rates plus an allowance of 1% for real employee cost increases.

222. This is based on external advice and our assessment of a reasonable increase in remuneration levels and should enable WIAL to retain staff at market levels in what is currently an incredibly competitive and candidate driven market.

Employee Numbers

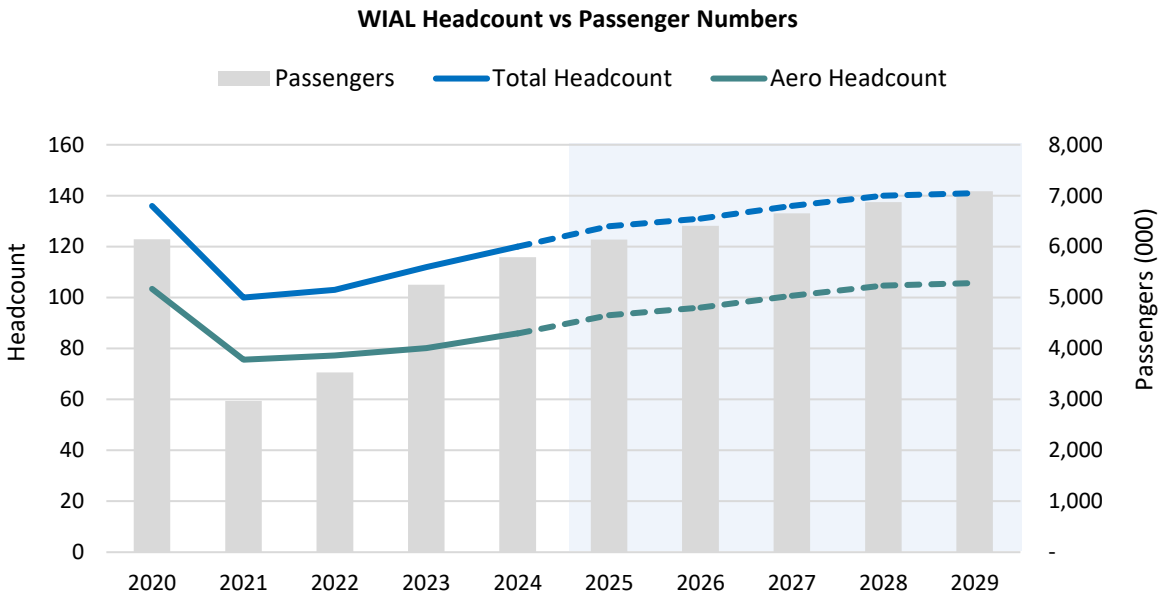
223. In response to Covid-19, WIAL resized its workforce over 2020/21 to deliver a 30% reduction in headcount.

224. Despite a strong recovery in passenger numbers and activity levels over PSE4, WIAL has continued to safely provide high-quality service with a smaller workforce through increased productivity and innovation. The FY24 budget assumes employee numbers remain 18 below pre-Covid levels (120 vs 138).

225. Additional roles are expected to be required over PSE5 with changing operational requirements and as passenger numbers recover to, then exceed, pre-Covid levels. The forecast assumes a return to 138 employees in FY28 (two years after passenger numbers are expected to fully recover) with a total of 141 employees at the end of PSE5. While we expect to retain some efficiencies gained during Covid-19, and therefore some roles are not forecast to return, other areas (such as

sustainability and Airport Fire Service) require additional resource. We consider that the WIAL workforce is efficient and streamlined compared to some other airports, and we are pleased to keep staffing forecasts at pre-Covid levels despite the forecast growth to 7MPPA and additional regulatory requirements and workload.

226. We show below our whole of company and aeronautical headcount alongside passenger numbers for FY11 to FY24, and for the FY25-FY29 forecast period:



227. The following additional roles are incorporated into the PSE5 forecast:

- Task Resource Analysis – AFS: WIAL undertook a Task and Resource Analysis (TRA) on the Airport Fire Service, following the guidance issued by the Civil Aviation Authority. The purpose of a TRA is to establish the minimum number of personnel required to deliver an effective Airport Fire Service and the analysis indicates that WIAL needs additional firefighters. After deferring implementation of these requirements from PSE4 due to the pandemic driven reduction in activity, WIAL intends to phase in additional resourcing over PSE5. The forecast includes an allowance for three new firefighters in each of the years from FY25 to FY28, plus an AFS Manager and Training Officer.

- AGL: Provision of AGL is a Part 139 requirement and necessary to facilitate the safe navigation of aircraft. In New Zealand, AGL infrastructure has historically been provided at airports by Airways. In 2019 Airways made changes to their services framework, which included the divestment of their power and lighting assets to airports. Airways notified WIAL of their intention to divest their AGL in late 2020. WIAL is in negotiations with Airways on the transfer of the AGL assets from Airways to WIAL, to occur at the commencement of PSE5. The forecast includes a WIAL AGL manager to oversee the transfer and management of this critical asset going forward.

- Baggage Handling System Support: To manage WIAL's end-of-life BHS system, WIAL's current headcount includes a Baggage Systems Engineer and three Bag Hall Officers, to respond to day-to-day clearing of bag jams, resets, and upkeep of the system. The forecast resources will provide extended shift coverage, and the additional interface and works supervision required during regular maintenance and proposed major projects.

- Operations: Additional team member is assumed in FY27, FY28 and FY29 in line with growing passenger numbers. Total operations staff at the end of PSE5 remain in line with pre-Covid levels.

- Facilities & Contract Manager: WIAL's main terminal was commissioned in 1999, and is now almost 25 years old. This new role assumed in 2025 is required to ensure WIAL's facilities continue to be maintained in line with passenger growth and appropriate asset management practices, as major assets enter the second half of their design life. This is intended to reduce reactive maintenance and improve asset life cycle costs.

- Sustainability & Data Analyst: WIAL currently has one dedicated sustainability role. An additional resource is assumed from FY25 to manage the increasing focus and regulation within this area. This is expected to be more efficient than engaging external consultants/experts.

Insurance

228. Despite difficult market conditions and Covid impacts over recent years, WIAL's insurance premiums per dollar of insured value are near flat in nominal terms over the long-term, and have reduced in real terms.

229. Three key factors have been taken into account in our forecast insurance costs for PSE5:

- Projected increases in underlying premium rates as international reinsurers continue to price in recurring natural disasters (7.5% p.a. assumed based on advice from WIAL's brokers and taking into account actual increases experienced over recent years);

- Growing asset replacement values due to capital expenditure plus the impact of cost of construction inflation on existing assets; and

- Higher business interruption insurance values consistent with revenue forecasts.

230. WIAL continues to place the majority of its insurance through the UK market and has maintained direct relationships with insurers to achieve the best terms possible.

231. WIAL has also established a wholly owned captive insurance company to provide an alternative insurance risk management solution. This provides more stable and cost-efficient outcomes over the long-term by:

- Enabling WIAL to directly access the reinsurance market thereby minimising commission costs charged in traditional insurance transactions;

- Increasing price tension by strategically competing for portions of WIAL's insurance cover; and

- Reducing exposure to price fluctuations by increasing/decreasing self-insurance in response to market conditions.

Local Authority Rates

232. Rates increases are driven by Wellington City Council and Greater Wellington Regional Council and WIAL has minimal ability to influence these costs.

233. For the 2023/24 period, Wellington City Council have announced a planned increase of 12.3%. For subsequent years WIAL has adopted the increases included in the Council's long-term plan (2021-2031).

234. The PSE5 forecast also includes an allowance for new aeronautical land and building assets, as described in Part H.

Terminal Heating Decarbonisation

235. WIAL plans to progressively transition from the existing natural gas heating system for the terminal to electric heat pumps. This is an important step in reducing the airport's own carbon emissions but will result in a net increase in energy costs.

PLEXIT

236. As noted above, Airways and WIAL are in negotiations regarding the transfer of AGL assets from Airways to WIAL, expected to occur at the commencement of PSE5. The requirements for the day-to-day inspection, operation, and maintenance of the airfield lighting system are set by the CAA, and require specialist resources, with 24 hour coverage, to ensure safety and continuity of operations.

237. WIAL has considered how best to provide this coverage, given the specialised nature of the subject, and the limited resource available in NZ, and proposes to outsource this to a third party for the duration of PSE5. The third party's proposal for provision of services has been used as the basis for the forecast operating costs.

Other costs

238. Other costs include the following items:

IT/Technology

239. WIAL has made ongoing investments and improvements in IT over recent years, in particular for common use terminal equipment, cyber security and increased automation. These have enabled reduced infrastructure spend as noted above plus increased customer service, efficiency and resilience.

240. Notwithstanding this, the change in accounting treatment of cloud-based software as a service subscriptions has also resulted in a step change in operating expenditure as costs need to be reclassified from capital to operating expenditure.

241. WIAL has assumed a 20% real increase per annum for PSE5 in line with its forecasts to enable continued investment in operating systems to improve service, efficiency and resilience.

Common Use Terminal Equipment

242. WIAL plans to continue its investment in common use equipment for passenger facilities including at boarding gates, check-in and baggage drop. Common use facilities create considerable efficiencies for customers through:

- Reducing the requirement for expansion of airport infrastructure to facilitate dedicated airline facilities;
- Improving the flexibility of the terminal check in area to accommodate airline growth and changes;
- Reducing the duplication of airline owned equipment/personnel;
- Enabling WIAL to manage check-in capacity over a larger group of passengers to improve utilisation of common use equipment; and
- Enabling airlines to improve customer service, contactless travel and reduce their own staffing levels and costs.

Airport Operations Requirements

243. The following changes in Airport Operations costs have also been included in the PSE5 forecast:

244. Passenger Tracking: WIAL is aware that, at times, queue lengths and wait times are exceeding passenger expectations and do not meet target service levels. WIAL has been working with Avsec to improve this service. Implementing passenger tracking technology in PSE5 will enable WIAL to better manage and predict passenger flows. This will also inform future operational and investment decisions to address these issues.

245. ACDM: WIAL implemented ACDM during PSE3. To further develop the benefits of ACDM, such as improving apron efficiency and reducing track miles, ACDM needs a network wide approach. Airways and Airlines have both expressed interest into re-energising this national project and WIAL considers it appropriate and beneficial to progress.

246. Virtual Training: Staff Training is a cornerstone for safe and efficient airport operations. WIAL is proposing to introduce some virtual training to compliment the current learning management toolbox. Virtual training will initially focus on airside driver training and training for our Airport Fire Service.

247. Airport Compliance & Safety Management System Replacement: Currently WIAL is operating separate systems to manage risk, compliancy, audits, investigations and emergency response. We are proposing to combine all of these aspects into one system with a view to improving our overall safety management system.

PSE5 forecast outcomes

248. WIAL's forecast cost increases for PSE5 are attributable to several discrete areas as explained above. A summary of the forecast change in costs is provided in the table below:

	Base Year	YEAR ON YEAR CHANGE IN COSTS				
	FY24	**FY25**	**FY26**	**FY27**	**FY28**	**FY29**
REAL COST INCREASES						
Insurance		911	1280	1323	1489	1,589
Rates		413	1047	404	654	447
PLEXIT		1,730	-	-	-	-
TRA - AFS staffing		350	259	367	374	13
Key Cost Increases		**3,404**	**2586**	**2093**	**2517**	**2,050**
All Other Costs		1,362	733	636	834	802
Total Cost Increases		**4,766**	**3,318**	**2,729**	**3,351**	**2,851**
Total Costs - 31 Mar 2024 Real Terms	**30,269**	**35,035**	**38,353**	**41,082**	**44,433**	**47,284**
INFLATION		102.6%	104.9%	107.2%	109.4%	111.7%
CPI Impact		918	1,898	2,978	4,197	5,512
Total Costs - Nominal Terms	**30,269**	**35,953**	**40,252**	**44,059**	**48,630**	**52,796**

249. Note: The operating costs shown above exclude WANT Limited (noise mitigation activity). Costs are split into pricing and non-pricing activities in schedules 18 and 19.

250. This breakdown shows the significant proportion of the forecast cost increases that are due to the new services and specific items. WIAL assumes that it will otherwise achieve cost efficiencies in PSE5 by accommodating increasing passenger numbers within the existing cost base.

251. WIAL considers that its PSE5 forecast is reasonable and demonstrates its commitment to operational efficiency whilst maintaining a high standard of airport facilities, with a commensurate high quality of service.

252. Excluding the largely uncontrollable growth in costs for insurance, rates, PLEXIT, and TRA, WIAL's real costs per passenger in FY29 are forecast to remain below FY20 levels.

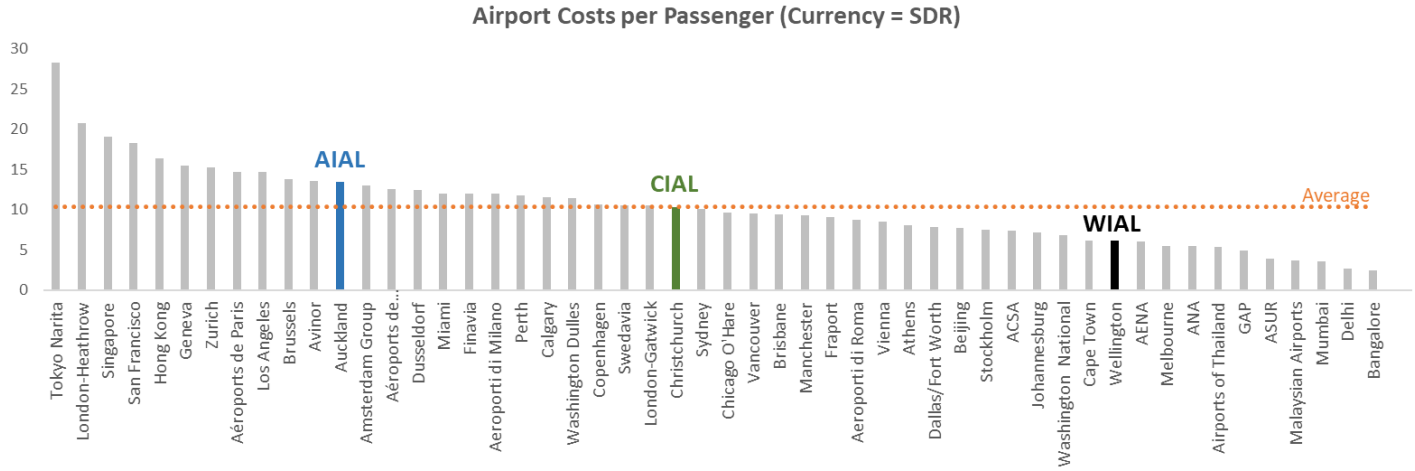
Comparison of WIAL's costs against other airports

253. Consistent with previous reviews, it is also evident that WIAL's operating costs are low by comparison to other airports in both Australasia and worldwide.

254. WIAL recognises that any analysis of charges needs to be treated with caution due to the impacts of factors, such as the differing mix of international and domestic passengers and the nature of services provided. For instance, in Australia security and baggage handling services are typically undertaken by the airports, whereas in New Zealand these are undertaken by Government agencies and the airlines respectively. By contrast, in New Zealand airports employ the fire crew, whilst in Australia this is not the case.

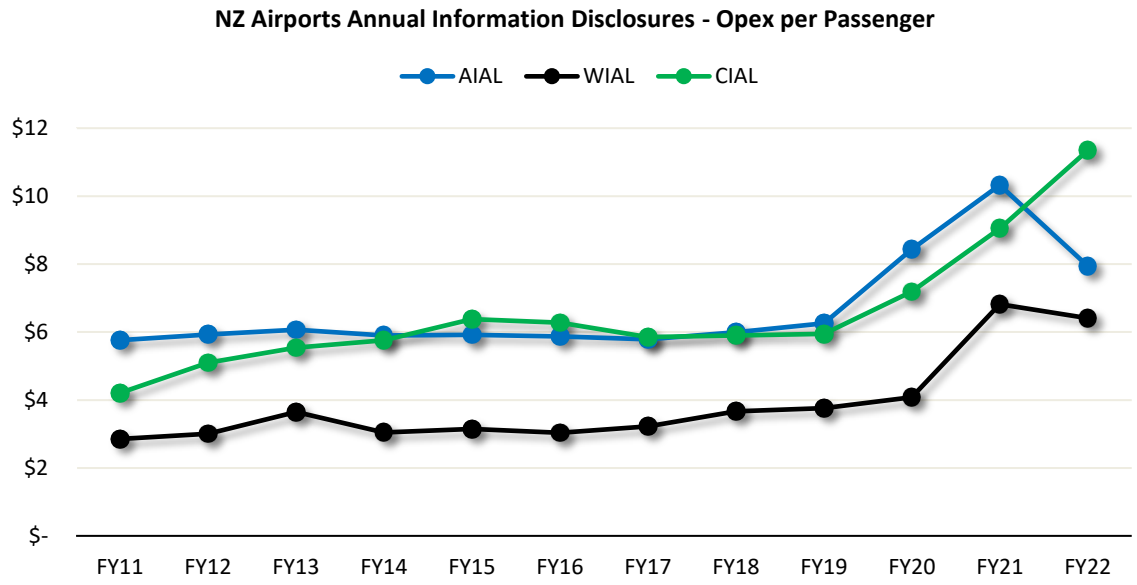
255. Notwithstanding these considerations, WIAL notes that its costs compare extremely favourably to other airports.

256. Jacobs UK (formerly Leigh Fisher) research compares total costs per passenger at a large sample of airports around the world. Consistent with prior iterations of this report, WIAL's operating costs for the 2021 financial year are amongst the lowest when compared to this sample and are the lowest in NZ:



Note: CIAL and WIAL do not participate in this survey. The outcomes for these airports have been calculated on the same basis as the calculation for AIAL.

257. The New Zealand information disclosures also show's WIAL's costs have consistently been the lowest within New Zealand where each of the airports have the same statutory responsibilities.



Expense allocation methodology

258. WIAL proposes to maintain an approach consistent with the IMs for allocating operating expenses to regulated activities. This approach is also consistent with the methodology adopted in WIAL's historical pricing consultations since commencement of the ID regime.

259. We summarise our cost allocation approach as follows:

- Forecast commences with the costs incurred for aeronautical or shared activities;
- We consider whether direct or causal allocation of costs is appropriate; and
- We allocate the remaining costs using proxy cost allocators.

260. In WIAL's financial management system, operating costs are grouped by 'cost centres' to reflect areas of accountability or asset facilities. The cost allocation approach outlined above is then applied to the costs incurred within each cost centre.

261. Set out below are the cost centres maintained by WIAL that have an aeronautical or shared purpose, an explanation of their activity and the cost allocation method proposed as the appropriate allocation methodology.

Cost centre	Cost centre activity	Cost allocation approach
Hangar #12	Property for aircraft and freight services	Aircraft and freight direct costs
Hangar #18	Property for aircraft and freight services	Aircraft and freight direct costs
Executive Jet Hangar	Property for aircraft and freight services	Aircraft and freight direct costs
Western Other	Property with mixed tenancies	Use of shared rental revenues as causal allocator
Hangar #23	Property for aircraft and freight services	Aircraft and freight direct costs
Houses	Residential properties purchased	Use of rental revenues as causal

	by WIAL	allocator
Terminal	Terminal buildings, including all passenger facilities	Use of share of terminal net book value as causal allocator
Fire Station	Building accommodating airport fire service	Airfield direct cost
AGS	Property with mixed tenancies	Use of shared rental revenues as causal allocator
Eastern Other	Properties with mixed tenancies	Use of share of rental revenues as causal allocator
Infrastructure Project Delivery	External costs to maintain WIAL's civil works infrastructure	Airfield direct cost
Airport Operations	Staff and associated facilities costs for staff administering airside safety and terminal facilitation	Estimate of time allocated to aeronautical and non-aeronautical activities as causal allocator
Airport Fire Service	Airport fire service staff and costs	Airfield direct cost
Noise Mitigation	Costs associated with managing WIAL's air noise obligations	Airfield direct cost
Maintenance	Maintenance staff and associated facilities	Share of maintenance expenditure incurred on maintaining facilities as proxy allocator
Corporate Property	Staff and associated facilities costs for staff administering property lease portfolio	Estimate of time allocated to aeronautical and non-aeronautical activities as causal allocator
Marketing	Staff, associated costs, and marketing, airline development and external relations costs	Initial identification of direct costs for each area with shared costs allocated in proportion to estimate of time allocated to aeronautical and non-aeronautical activities as causal allocator
Corporate salaries	Corporate office staff and associated costs for company management functions including HR, finance and IT	Estimate of time and costs allocated to aeronautical and non-aeronautical activities as proxy allocator
Consultation and regulation costs	Costs associated with Airport Authorities Act consultation and Commerce Act ID regime	Allocated to regulated activities based on the proportion of total regulated revenue forecast for each activity
Corporate administration costs	Corporate overheads (eg director's fees, audit fees) and administration costs.	Share of all other expenditure allocated to aeronautical and non-aeronautical activities as proxy allocator

PART H: COMMENCING ASSET BASE VALUES

Summary

262. This section sets out the approach and process applied by WIAL to establish the commencing regulatory asset base (RAB) for PSE5.

263. WIAL is proposing to adopt valuation methodologies that are consistent with the Commission's IMs for information disclosure.

264. The commencing asset values for PSE5 are based on the following:

- Land assets - a Market Value Alternative Use (MVAU) land valuation has been prepared by CBRE as at 1 April 2023. WIAL proposes rolling this valuation forward 12 months to 31 March 2024 at CPI to align with the start date of PSE5.

- Specialised (non-land) assets – WIAL proposes rolling forward the audited 31 March 2023 RAB (prepared for the annual disclosures) to 31 March 2024. Note that the IPP has been based on a roll forward of the 2022 RAB as the 2023 disclosures are not yet complete.

265. Other components that then impact the carry forward asset value are addressed in separate chapters, namely:

- Revaluations;

- Forecast capital expenditure;

- Asset allocation; and

- Depreciation.

Updated land valuation

266. An MVAU valuation as at 1 April 2023 was commissioned from CBRE and the draft report is attached at Appendix F. WIAL proposes to roll this valuation forward 12 months at forecast CPI of 4.7% to align with the start date of the PSE5 period.

267. The MVAU valuation is based on an alternative land use plan prepared by Boffa Miskell, with market demand analysis prepared by Property Economics Limited. The detailed principles and conclusions are not restated in this section as these are fully set out in the draft valuation report.

268. Note that the valuation covers WIAL's aeronautical land holding only. Land utilised directly for commercial activities is excluded.

269. WIAL maintains a detailed asset register that records land holdings based on underlying use. Each area is directly attributed to a business activity where possible, or to a shared use which is then allocated between regulated and non-regulated activities. Further detail on WIAL's asset allocation methodology is provided in Part J: Asset Allocation.

270. WIAL has a total landholding of 130 hectares. The land included in the MVAU valuation is calculated as follows:

	Hectares
Total WIAL Landholding	130.2
Less Investment Property and Commercial Land	(26.8)
Land Area Used to Provide Specified Airport Services	**103.4**
Less Allowance for Roads	(20.6)
Less Allowance for Public Spaces	(15.8)
Net Development Land Area for MVAU valuation	**67.0**

271. The value of the pricing asset base land (comprising airfield, specified terminal, and an allocation of shared land) was then calculated as follows:

MVAU Valuation	$288.5m
Total land available for MVAU valuation	103.4ha
Value of Land per Square Metre @ 1 April 2023	$279/sqm
Value of Land per Square Metre @ 31 March 2024 (4.7% CPI)	$292/sqm
Total land area in pricing asset base	81.8ha
MVAU Value of Land to Include in Pricing Asset Base	**$239.0 million**

Valuation of specialised (non-land) assets

272. The commencing RAB for PSE5 will be based on a roll forward from the RAB reported in WIAL's annual information disclosures for the year ended 31 March 2023. Note that the IPP has been based on a roll forward of the 2022 RAB as the 2023 disclosures are not yet complete.

273. The RAB includes Aircraft and Freight and other leased assets that are not included in the pricing asset base. A breakdown of the allocation of the RAB and an explanation of the allocation methodology is shown in Part J: Asset Allocation.

PART I: ASSET REVALUATIONS

Summary

274. This section sets out WIAL's approach to historic and forecast revaluation movements, including:

275. Revaluation uplift from 2023 MVAU land valuation – an uplift in WIAL's pricing land value of $37.0m arises if the updated CBRE 2023 valuation proposed by WIAL is adopted. If the valuation is adopted WIAL proposes to allocate this uplift to its customers as an opening carry forward adjustment.

276. The remaining net revaluation carry forward adjustment discussed in PSE4, previously $9.7 million, with $5.98 million remaining to be allocated in PSE5 in present value terms.

277. Forecast revaluations – WIAL proposes to index its asset base during the pricing period and to include forecast revaluations at WIAL's assumption for CPI. Forecast revaluations will be included as income, consistent with prior pricing approaches.

Valuation uplift from MVAU land valuation

278. The updated MVAU valuation has resulted in a substantial uplift in land values.

279. As advised above, WIAL proposes to apply the updated land value and in accordance with the IM, recognise the valuation uplift as a carry forward adjustment in the pricing calculations for PSE5.

280. The carry forward adjustment is calculated as follows:

Excluding Future Use Assets	**Total RAB $m**	**Pricing RAB $m**
2022 annual disclosures land valuation (actual)	189.3	181.1
2023 CPI indexation of RAB	12.6	12.0
2024 CPI indexation of RAB	9.4	9.0
2024 annual disclosures land valuation (projected)	211.3	202.1
MVAU valuation	250.0	239.1
Real uplift @ 1 April 2024 (treated as carry forward)	**38.7**	**37.0**

281. WIAL is proposing to allocate this carry forward entirely within PSE5, recognising that this will partially offset other factors driving price increases within the period.

Net revaluation carry forward

282. There is also a remaining net revaluation carry forward from PSE4, with $5.98 million remaining to be returned to airline customers in PSE5. This relates to WIAL's PSE4 MVAU revaluation, which was partially offset by a historical revaluation shortfall and then allocated to customers over two pricing periods (PSE4 and PSE5):[5]

> *The total land valuation proposed is $175.3 million, an uplift of $46.2 million as at the commencement of PSE4. This is tempered by WIAL's calculation of a historic revaluation shortfall of $36.5 million since the commencement of the Information Disclosure ("ID") regime.*

[5] Initial Pricing Proposal, WIAL PSE4 (September 2019).

WIAL proposes to allocate the net revaluation of $9.7 million as a carry forward adjustment to consumers over the next two pricing periods.

283. The history of this carry forward is further outlined in the PSE4 consultation documents, which we are able to provide again if necessary.

Forecast revaluations

284. We note that the IMs do not prescribe a specific approach for estimating CPI. It was proposed in the 2016 IM review that airports should adopt CPI forecasts in line with the Reserve Bank of New Zealand (RBNZ). However, following submissions, this was not adopted and airports retain flexibility.

285. WIAL proposes to include forecast revaluations using its PSE4 method of estimating CPI. This method was arrived at following feedback from airlines, and was accepted by the Commerce Commission as reasonable.

286. This approach takes an equally weighted average of the RBNZ forecast, NZIER market consensus forecast (which incorporates all major bank forecasts), and the breakeven rate based on indexed bond yields.

287. The RBNZ forecasts are extended beyond the forecasting period by assuming that inflation trends linearly towards the RBNZ's inflation target (2%) over the remainder of the five-year regulatory period.

288. The breakeven inflation rate is calculated by subtracting CPI-indexed bond yields from fixed coupon bond yields. The gap between nominal and indexed bond yields represents investors' expected inflation rate that, over the life of the respective bonds, would generate the same return whether one was holding indexed or nominal bonds. It therefore provides a market-based assumption of CPI.

Year ended	**FY25**	**FY26**	**FY27**	**FY28**	**FY29**
RBNZ	2.27	1.99	2.00	2.00	2.00
NZIER	2.40	2.20	-	-	-
Breakeven	3.19	2.62	2.37	2.10	2.04
Average	**2.62**	**2.27**	**2.19**	**2.05**	**2.02**

289. This CPI assumption is used throughout the IPP wherever CPI indexation is required, other than for construction cost indexing which uses NZIER construction market forecasts.

PART J: ASSET ALLOCATION

Summary

290. The allocation methodology applied by WIAL for the forecast RAB and capital expenditure is consistent with that which WIAL utilises for its annual information disclosures. As a result, the methodology complies with the Commission's IMs.

291. Assets and capital expenditure directly attributable to regulated activities is allocated 100% to either airfield, specified terminal, or aircraft & freight accordingly.

292. Indirect assets and capital expenditure are allocated to regulated and unregulated activities using an appropriate driver as set out below.

Allocation methodology

Introduction

293. This section sets out the methodology applied by WIAL to allocate assets to aeronautical activities consistent with WIAL's annual information disclosures. This methodology has been used to allocate assets to regulated activities and to establish the commencing pricing asset base. The allocation rates are also used to determine the proportion of capital expenditure that is incorporated into WIAL's forecast RAB.

Generic Approach

294. The Commission's IM for asset allocation requires WIAL to:

- Identify directly allocated assets.
- Allocate a share of common assets to specified airport activities by using causal or proxy cost allocators.

295. The approach that WIAL proposes to apply, consistent with the Commission's IMs, is as follows:

- WIAL assigns a business code to each asset to depict the activity in which that asset is used. The categories used by WIAL are:
    - Airfield
    - Terminal aeronautical
    - Terminal non-aeronautical
    - Terminal common
    - Airfield and freight
    - Commercial
    - Shared
- Directly attributable assets are identified from the asset coding above.
- Shared or terminal common assets are then allocated as follows:
    - The terminal common assets are those used to provide services to all users of the terminal. These assets are allocated between terminal aeronautical and commercial activities.

- Shared assets are those used to provide services to all users of the airport site. A share of these assets is allocated to all airport business activities.

Allocation of Shared Assets

296. The bases for the allocation of shared assets to aeronautical activities in the IPP are based on WIAL's 2022 information disclosure RAB (to be updated to 2023 for final pricing calculations):

Allocation of Terminal Common Assets		
	Basis for Allocation	**Aeronautical %**
Land	Allocated between terminal aeronautical and contestable areas based on floor areas for directly allocated assets	78.1%
Other Assets	Allocated between terminal aeronautical and contestable areas based on asset values for directly allocated assets	91.1%

Allocation of Shared Assets		
	Basis for Allocation	**Aeronautical %**
Land	Based on share of land area directly allocated to activities.	82.2%
Other Assets	Based on value of assets directly allocated to activities.	57.9%

Asset transfers

297. Where the underlying use of an asset changes between regulated and unregulated activities, the IMs require the asset to be transferred into or out of the RAB.

298. For PSE5, WIAL has forecast the transfer of assets using the following approaches in line with the IMs:

- Land assets transferred at MVEU;
- Non-land assets transferred at depreciated historic cost (using GAAP); and
- Future use assets transferred at excluded asset cost.

299. WIAL previously noted in PSE4 that where land is transferred from non aeronautical to aeronautical use, it should be transferred into the RAB at its existing use value, rather than at MVAU as required by the current IMs. This is because its most valued alternative use is literally reflected in its existing use.

300. Requiring the value of assets to be written down upon transfer to the RAB could result in perverse outcomes where airports are incentivised to keep land assets in non aeronautical use, even when it would be more efficient for that land to be incorporated to enable aeronautical growth. This is an important point of principle for WIAL given the scarcity of land in the airport precinct.

301. The forecast value of land transferred into the pricing asset base in PSE5 is $4.8m higher under MVEU compared with MVAU, and $7.0m higher for the total asset base.

302. The table below summaries the transfers included in WIAL's PSE5 forecast, which are driven by capital expenditure project requirements. A detailed breakdown of individual assets and areas is provided in Appendix H.

Relevant Project	Affected Areas	Assets Transferred	Regulated Activity	Transfer Timing	Allocated Value Transferred ($000)
AFS Relocation	Coutts St residentials & roadstop	Land	Airfield	FY26 - 27	$6,236
ECAC Std3 Bag Factory	Carpark/apron area East of MTB	Land	Specified Terminal	FY28	$3,366
Apron Development	Commercial/aero leased land,Southern apron	Land	Airfield	FY27 - 29	$6,969
TC3 Check-In	Valet area of MTB	Building, civils & services	Specified Terminal	FY25	$3,383
Southern Seawall	Miramar Golf Club	Land	Airfield	FY26 - 29	$40,039
GSE	Southern apron	Land	Aircraft & Freight	FY25 - 26	$2,251
Flight Catering	Miramar South School & bordering residential properties	Land	Aircraft & Freight	FY26	$5,185
Logistics Hub	Southern apron and shared roading	Land	Aircraft & Freight	FY26	$4,068
Bus Lounge	Carpark North of Hotel	Land	Specified Terminal	FY26	$281

PART K: DEPRECIATION

Summary

303. This section sets WIAL's approach to determining forecast asset depreciation for inclusion in the building block model.

304. As advised in Part H: Commencing Asset Base Values, WIAL is using an IM compliant approach to the valuation and roll forward of assets, and it is intended that WIAL's approach to depreciation is also consistent with IM requirements.

305. Depreciation on WIAL's existing RAB asset base is forecast using the asset values and remaining asset lives as at 31 March 2022. WIAL has calculated forecast depreciation for each year of PSE5 using the RAB file for its 2022 annual information disclosures. This will be updated to the 2023 annual information disclosures for final pricing calculations.

306. Depreciation for each asset has been calculated in the manner required by the Commission's asset valuation IM with standard depreciation assumptions for each asset consistent with those used for WIAL's annual disclosures.

307. Capital additions - depreciation assumptions have been applied for forecast capital expenditure based upon WIAL's assessment of reasonable average asset lives for each project, or category of business as usual expenditure.

Allocation

308. The depreciation expense is allocated to the pricing activities using the same methodology as is applied for the allocation of assets.

Tax depreciation

309. WIAL determines its tax depreciation in accordance with IRD requirements. WIAL's calculation of tax expense for the pricing activities recognises the timing difference between accounting and tax depreciation. That is WIAL uses tax depreciation to calculate the annual tax expense on a tax payable approach.

310. WIAL has established forecast tax depreciation from the tax asset base used for its 2022 annual information disclosures, in the same manner as accounting book depreciation has been calculated for the RAB. This will be updated to the 2023 annual information disclosures for final pricing calculations.

PART L: TAX

Tax payable approach

311. With the exception of Noise Mitigation activities, WIAL proposes to calculate its annual tax cost by applying the tax approach required by the IMs. Consequently, WIAL's calculation of tax expense for the regulated, and pricing, activities recognises the timing difference between accounting and tax depreciation. Other timing differences are also allowed for, albeit that these are immaterial.

312. Tax forecasts for Noise Mitigation activities reflect WIAL's projection of the actual tax obligation for each year, which differs from the unlevered tax calculation required by the IMs. As set out in Part O, WIAL obtained a binding ruling from the IRD relating to the treatment of house removals and this results in a non-standard tax calculation. WIAL considers this departure from the IMs to be appropriate as it more accurately reflects the costs of the programme.

PART M: TARGET REVENUE (BUILDING BLOCK MODEL)

Summary

313. WIAL has applied a building block approach to establish its proposed required revenue, and therefore pricing, requirements for PSE5.

314. WIAL's building block model produces a forecast Internal Rate of Return (IRR) for the pricing asset base and total asset base in the format required for the price setting event disclosures (schedules 18, 19 and 20).

315. WIAL is targeting a post-tax IRR of 8.55% in PSE5.

Activities in the price setting consultation and Building Block Model

316. The following activities are included in the pricing asset base and total asset base:

Total Asset Base	**Pricing Asset Base** *included in price setting consultation*
Airfield activities including airfield leases	Airfield activities excluding airfield leases
Specified terminal activities including terminal leases	Specified terminal activities excluding terminal leases
Noise mitigation activities (WANT Limited)	Noise mitigation activities (WANT Limited)
Aircraft & freight activities	

Pricing Asset Base – IRR and Revenue Outcomes

317. WIAL has calculated the pricing revenue required to achieve the target return on capital of 8.55% during PSE5, using the Commission's default cashflow timing assumptions in the price setting event schedules.

318. The IRR calculation and revenue requirement resulting from the forecast model is shown below:

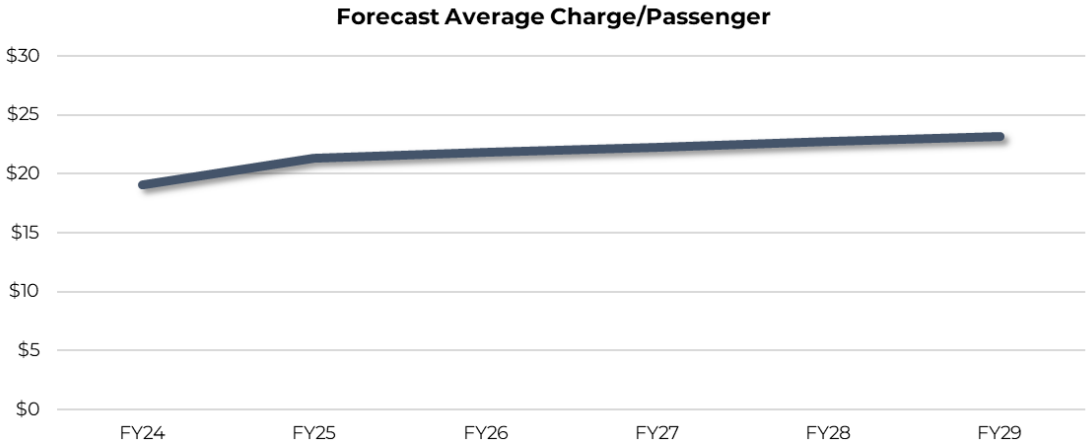
		Opening RAB $000	Opening Carry Forward $000	Revenue Requirement $000	Assets Commissioned $000	Operating Expenditure $000	Unlevered Tax $000	Closing RAB $000	Closing Carry Forward $000	Total Net Cashflows $000
	1 April 2024	**(664,352)**	**5,336**							**(659,016)**
FY25	30 September 2024				(90,998)	(34,648)	(23,506)			(149,152)
	3 November 2024			131,276						131,276
FY26	30 September 2025				(141,446)	(38,504)	(23,321)			(203,271)
	3 November 2025			139,963						139,963
FY27	30 September 2026				(62,273)	(42,200)	(23,152)			(127,625)
	3 November 2026			148,367						148,367
FY28	1 October 2027				(141,703)	(46,650)	(23,147)			(211,500)
	4 November 2027			156,311						156,311
FY29	30 September 2028				(63,405)	(50,681)	(23,186)			(137,271)
	3 November 2028			164,454						164,454
	31 March 2029							**1,118,981**	**0**	**1,118,981**

5 Year IRR	**8.55%**

Price Path

319. WIAL has based the proposed PSE5 price path off an adjusted FY24 charge per passenger of $19.07, being the charge that would have applied in the final year of PSE4 without the $15.1m revenue deferral and using actual passenger numbers for the year.

320. To avoid a large peak in charges in the final years of PSE5, WIAL has proposed a larger step up in year 1 of the price period with charges then being indexed to CPI from 2026-2029:



321. This results in a total nominal price increase of 21.7% from FY24 to FY29, or an average uplift of 4.0% per annum:

	FY24	**FY25**	**FY26**	**FY27**	**FY28**	**FY29**
Average Charge/PAX	$19.07	$21.32	$21.81	$22.38	$22.74	$23.20
Increase p.a.		11.8%	2.3%	2.2%	2.1%	2.0%

322. WIAL believes the change in expected revenue per passenger over PSE5 is reasonable, particularly when considered in conjunction with the substantial increase in WACC, challenging cost environment, and significant investment requirements facing the airport.

PART N: PRICING METHODOLOGY

Summary

324. The proposed pricing methodology is largely unchanged from that previously consulted on and adopted for the PSE4 pricing period. The pricing methodology, which was primarily designed in PSE2, sought to recover the cost of providing specified aeronautical services through charges which aimed to incentivise efficient use of, and investment in, WIAL's assets.

325. As part of the PSE4 consultation process, WIAL commissioned Sapere Research Group to analyse the seven years of operating with this price structure (PSE2-PSE3) to form a view of the effectiveness of the components of the Pricing Methodology adopted. A similar review covering PSE4 was considered, however the disruptive impacts of Covid resulted in non-standard behaviours which would have been difficult to analyse.

326. As a reminder, the Sapere report concluded the introduction of:

- Peak airfield charging had resulted in a higher utilisation of the runway with a 24% increase in the average number of passengers per movement;
- Common use check-in facilities had enabled the introduction of new carriers without the need to invest in expansion;
- Growth incentives had supported faster growth in domestic (23% versus 11% over the same period prior) and international (29% versus 22%) passengers, including three new international airlines and two new year-round routes. They concluded the higher passenger growth rate of 24% over the PSE2-PSE3 period (versus 13% the same period prior) would lower the average charge by just under 10% into PSE4.

327. In PSE4, WIAL noted the complexity of applying the PSE3 Pricing Methodology and after consultation simplified the methodology by:

- Combining the scheduled airfield MCTOW and passenger charge into a single passenger charge;
- Rolling in the check-in facility charges into the wider terminal charge to encourage airlines to move to the common user facilities;
- Presenting a charging schedule which combined the airfield and terminal charges into a single passenger charge.

328. Growth incentives have formed part of WIAL's pricing structure since PSE2, supporting higher levels of growth at the airport. These incentives were paused during PSE4, due to the negative impact of Covid on passenger numbers, and the expectation that the industry would remain in a recovery phase for an extended period of time.

Proposed PSE5 pricing methodology

329. The pricing methodology for PSE5 is proposed to be almost identical to PSE4, which in turn considered the findings of the Sapere review, previous feedback from the Commission, and views from airlines. The components of the price structure considered for or incorporated in the IPP are described below.

Price Structure Simplification

330. Previous airline feedback featured a view that a simplification of the price structure would be welcomed. PSE4 looked to introduce a simplified per passenger charge where appropriate. This principle has been retained in the IPP.

Exempt Passengers

331. The current price structure exempts infants (under 2 years old), transit passengers (those travelling on the same aircraft without leaving the lounge), positioning crew, and diverted international passengers (not processed by customs). WIAL is proposing to maintain these groups of exempt passengers for PSE5.

332. Currently exempt passengers total around 1.9% of the domestic and 1.7% of all international passengers; the PSE5 forecasts assume these proportions remain unchanged.

Transfer Passengers

333. WIAL has considered a lower charge (or exemption) for transfer passengers. Transfer passengers are passengers connecting between two flights, generally within a few hours of each other, whose main origin and destination of travel is not the airport they are passing through. Connecting flights are typically used where the numbers travelling between city pairs are not large enough for commercially viable non-stop services. Operating costs can be expensive for these smaller markets due to the additional airport charges (and government charges) incurred at the transfer airport.

334. Forecasts from InterVistas estimate that in FY24, 13.7% of passenger counts at Wellington Airport will be transferring (each transfer counts as two passengers), with 14.0% of domestic passengers and 11.5% of international passengers transferring to/from another service.

335. WIAL is interested in airline views of the merits of incorporating discounts or exemptions for transfer passengers, the definition of transfer passengers (within airline, between airlines, timeframe between connecting flights), and the ability of airlines to be able to provide accurate counts of transfer volumes for charging purposes. Transfer discounts have not been proposed in the IPP.

Peak Pricing

336. The introduction of peak pricing has supported a reduction in movements during the peak (to the shoulder) and an upgauging of aircraft, resulting in more efficient use of the runway. The Commerce Commission in their review of WIAL's pricing was notably supportive of the peak pricing mechanism.

337. WIAL proposes retaining the current definition of the peak time period, being 07:45-08:45 and 18:15-19:15 weekdays, and the shoulder time period applying 30 minutes either side of the peak.

338. WIAL proposes to continue the application of increased charges during the peak as a per movement charge. The charge is proposed to be fixed throughout PSE5 at $20/mvmt during the peak and $10/mvmt during the shoulder. With no relative increase in peak pricing proposed, the forecast assumes the current proportions of peak, shoulder and offpeak flying remain unchanged over PSE5.

339. For unscheduled movements, no change is proposed. The peak charge in PSE4 is currently equal to a MCTOW charge consistent with a scheduled aircraft of the same MCTOW (assuming 80% load factor), while general aviation (aircraft less than two tonnes) faces a higher fixed charge.

Table: Proportion of Peak Flying

Aircraft	Period	2024	2025	2026	2027	2028	2029
Domestic Jet	Peak	14%	14%	14%	14%	14%	14%

	Shoulder	12%	12%	12%	12%	12%	12%
	Offpeak	74%	74%	74%	74%	74%	74%
Domestic Prop ≥10 Tonnes	Peak	16%	16%	16%	16%	16%	16%
	Shoulder	14%	14%	14%	14%	14%	14%
	Offpeak	69%	69%	69%	69%	69%	69%
Domestic Prop <10 Tonnes	Peak	14%	14%	14%	14%	14%	14%
	Shoulder	14%	14%	14%	14%	14%	14%
	Off peak	73%	73%	73%	73%	73%	73%
International	Peak	1%	1%	1%	1%	1%	1%
	Shoulder	2%	2%	2%	2%	2%	2%
	Off peak	97%	97%	97%	97%	97%	97%

Table: Scheduled Airlines Peak Pricing Charges

Per Movement	1 April 2024	1 April 2025	1 April 2026	1 April 2027	1 April 2028
Peak	$20.00	$20.00	$20.00	$20.00	$20.00
Shoulder	$10.00	$10.00	$10.00	$10.00	$10.00

Notes:

1) Peak defined as actual landing or takeoff time 07:45-8:45 and 18:15-19:15 Monday-Friday; shoulder 30 minutes either side of peak

Airfield and Terminal Charge

340. Price structure simplification as a result of PSE4 resulted in the removal of the MCTOW airfield charge and the combination of the airfield and terminal charge into a per passenger only charge. The IPP proposes to retain the PSE4 price structure with charges differentiated by domestic jet, domestic prop ≥10 tonnes (MCTOW), domestic prop <10 tonnes (MCTOW) and international and on a per passenger basis.

Table: Scheduled Airlines Airfield and Terminal Charges

	1 April 2024	1 April 2025	1 April 2026	1 April 2027	1 April 2028
Offpeak Passenger Charge					
Domestic Jet	$22.73	$23.24	$23.72	$24.01	$24.51
Domestic Prop ≥10 Tonnes	$15.66	$16.17	$16.65	$16.94	$17.44
Domestic Prop <10 Tonnes	$14.71	$15.22	$15.70	$15.99	$16.49
International	$31.77	$32.53	$33.26	$33.80	$34.55

341. Unscheduled airfield charges are proposed to retain the same methodology as in PSE4, which are based on a MCTOW per tonne charge that is equivalent to the airfield charges for a similar weight scheduled aircraft assuming an 80% load factor. For unscheduled aircraft with MCTOW greater than 100 tonnes, it is proposed that the charge for tonnage over 100 tonnes is charged at 10% of the standard charge. This methodology was previously included in PSE3 prior to the move to the simplified per passenger structure for scheduled aircraft. The airfield charges component (71% of total charges) includes an upweight for peak/shoulder flying, and is disaggregated into an international and three domestic weight bands as outlined below. General aviation (aircraft less than two tonnes) is charged a fixed movement charge grown at CPI, with a higher charge during the peak.

Table: Unscheduled Airlines Airfield Charges

		1 April 2024	1 April 2025	1 April 2026	1 April 2027	1 April 2028
Per MCTOW Tonne Movement (Note 2)						
Domestic Prop ≥30 Tonnes	**Peak**	$31.87	$32.52	$33.14	$33.46	$34.09
	Shoulder	$31.74	$32.38	$33.01	$33.32	$33.95
	Offpeak	$31.60	$32.25	$32.87	$33.18	$33.82
Domestic Prop 2-30 Tonnes	**Peak**	$21.36	$22.08	$22.78	$23.13	$23.83
	Shoulder	$20.37	$21.09	$21.79	$22.14	$22.84
	Offpeak	$19.38	$20.10	$20.80	$21.15	$21.85
International	**Peak**	$44.67	$45.69	$46.70	$47.42	$48.43
	Shoulder	$44.54	$45.57	$46.57	$47.29	$48.30
	Offpeak	$44.41	$45.44	$46.44	$47.16	$48.17
General Aviation <2 Tonnes	**Note 3**	$12.22	$12.50	$12.77	$13.04	$13.30

Notes:

1) Peak defined as actual landing or take-off time 07:45-8:45 and 18:15-19:15 Monday-Friday; shoulder 30 minutes either side of peak

2) Aircraft with a MCTOW greater than 100 tonnes will be charged the full charge to 100 tonnes and 10% of the full charge for the incremental tonnage over 100 tonnes

3) Off peak charge per movement (not MCTOW tonne). A minimum charge of $100 in the peak and $75 in the shoulder applies. A minimum monthly charge of $55 per month (increased by CPI) applies

Aircraft Parking Charge

342. Parking charges were introduced to encourage efficient use of apron assets particularly during peak periods. For PSE3, the charge was relaxed to eliminate the inefficient towing of aircraft that was evident during PSE2. PSE5 proposes to continue the current charging regime with charges consistent with PSE4 in real terms. There would continue to be no charges for a standard turnaround during the peak, or parking during the weekday off peak, overnight or at weekends. PSE5 forecasts assume that the average parked time per aircraft will remain unchanged over the pricing period.

Table: Airlines Parking Charges

		1 April 2024	1 April 2025	1 April 2026	1 April 2027	1 April 2028
Per (part) Hour – Only applies Mon-Fri 06:00-10:00, 16:00-20:00						
Domestic Jet	After 60 mins	$61.10	$62.49	$63.86	$65.16	$66.48
Domestic Prop	After 60 mins	$48.88	$49.99	$51.08	$52.13	$53.18
International	After 120 mins	$85.53	$87.48	$89.39	$91.22	$93.07
Unscheduled	After 120 mins	$24.44	$25.00	$25.55	$26.07	$26.60

Check-in Charge

343. WIAL incorporated the previously collected check-in charge into the wider passenger charge in PSE4. The removal of the check-in charge supported the move to a fully common-user facility and transition from manual to automated passenger handling. WIAL proposes to continue including the cost of providing check-in facilities within the wider passenger charge.

344. For airlines with specific equipment installed, it is proposed that airlines can continue to use this equipment until it becomes redundant. Any new equipment installed is proposed to be non-airline specific. The retention of the current check-in counter conditions of use is also proposed.

Incentives for growth

345. Incentives are commonplace in the industry as a mechanism to promote and de-risk the introduction of new services thereby bringing forward the addition of new capacity. By accelerating the introduction of new services the costs of providing airport assets are able to be spread across more users producing lower unit costs to airlines.

346. PSE2 and PSE3 contained published growth incentives incorporated into the price structure. The cost of the incentives was included in the required revenue and the volume expected to be delivered by way of the incentives was included in the passenger forecast producing a lower cost per passenger. The incentive scheme was paused during PSE4 as traffic moved from growth to recovery.

347. WIAL proposes to reintroduce incentives for growth in PSE5. The passenger forecast includes:

- New international airline capacity on existing routes rebuilding to pre-Covid levels;
- A new Australia short-haul route;
- A fifth freedom long haul service; and
- 17% growth in domestic passenger movements over the period FY24-FY29.

Table: Scheduled Airlines Incentives for Growth

	Qualifying Capacity		Year 1	Year 2	Year 3
Domestic	All Pax Growth over Previous Year[2]		50%	25%	0%
International – Short Haul	3 per week	Additional capacity on existing route[2]	50%	25%	0%

	3 per week	New route	100%	50%	25%
International – Long Haul	All	Additional capacity on existing route[2]	50%	25%	0%
	3 per week	New route	100%	100%	100%

Notes:

1) Discounts on qualifying passengers – excludes Noise Charges

2) Capped at total market growth

Support for Next Generation Aircraft & Technologies

348. Wellington Airport's central location between the two islands results in relatively short and frequent domestic sectors, with around 60% of the airport's domestic flights within 400km (the likely feasible range for first generation electric/hybrid aircraft). The airport is expected to play a leading role in the transition from fossil fuel powered to more sustainable aircraft particularly given the initial range limitation expected of the technology.

349. WIAL recognises this role as well as the challenges airlines will face as next generation aircraft are adopted. To aid in the transition WIAL is open to exploring with stakeholders how price structure can best support the introduction of new aircraft. In particular, the airport is interested in considering reduced charges for electric/hybrid aircraft, possible higher charges for older generation aircraft, and discounts in relation to the introduction of Sustainable Aviation Fuels.

350. While carbon-friendly solutions are not expected to form a material part of the airport's operation until PSE6, the PSE5 forecasts assume electric aircraft will begin operating in FY28 and will reach around 700 movements in FY29.

351. The following tables provide a summary of the scheduled passenger and parking charges in PSE5.

Table: Scheduled Airlines Airfield and Terminal Charges

	1 April 2024	1 April 2025	1 April 2026	1 April 2027	1 April 2028
Offpeak Passenger Charge (Note 2)					
Domestic Jet	$22.73	$23.24	$23.72	$24.01	$24.51
Domestic Prop ≥10 Tonnes	$15.66	$16.17	$16.65	$16.94	$17.44
Domestic Prop <10 Tonnes	$14.71	$15.22	$15.70	$15.99	$16.49
International	$31.77	$32.53	$33.26	$33.80	$34.55
Peak Movement Charge (Note 3)					
Peak	$20.00	$20.00	$20.00	$20.00	$20.00
Shoulder	$10.00	$10.00	$10.00	$10.00	$10.00

Notes:

1) Charges are additive.

2) Per departing and arriving passenger excluding infants (under 2 years old), transit passengers, positioning crew, and diverted international passengers returned to destination (being only those diverted passengers not processed by customs).

3) Per aircraft landing and departure. Peak defined as actual landing or take-off time 07:45-8:45 and 18:15-19:15 Monday-Friday; shoulder 30 minutes either side of peak. No peak charge outside of these periods.

Table: Scheduled Airlines Parking Charges

		1 April 2024	1 April 2025	1 April 2026	1 April 2027	1 April 2028
Per (part) Hour – Only applies Mon-Fri 06:00-10:00, 16:00-20:00						
Domestic Jet	After 60 mins	$61.10	$62.49	$63.86	$65.16	$66.48
Domestic Prop	After 60 mins	$48.88	$49.99	$51.08	$52.13	$53.18
International	After 120 mins	$85.53	$87.48	$89.39	$91.22	$93.07

Notes:

1) Parking charge rates are per hour (or part thereof). Parked time is determined by subtracting the scheduled aircraft take-off time from the scheduled aircraft landing time, and then subtracting 8 minutes for taxiing time (4 minutes in each direction). Parking charges apply to any time spent on the Eastern apron; parking on the Western apron will incur the non-passenger parking charges. WIAL will consider parking charge relief for the time parked outside of the control of the operator e.g. weather disrupts.

Summary of charges per passenger by aircraft/service type

352. The following tables provide a summary of the charges per passenger for different aircraft types and services over PSE5.

Table: Average Domestic Charges per Passenger

Aircraft	Time Period	FY24 (Note 2)	FY25	FY26	FY27	FY28	FY29	FY29 vs FY24
A321	Peak	$19.39	$22.34	$22.77	$23.40	$23.74	$24.25	25%
	Shoulder	$19.33	$22.28	$22.71	$23.34	$23.68	$24.19	25%
	Offpeak	$19.27	$22.22	$22.65	$23.28	$23.62	$24.14	25%
A320	Peak	$19.42	$22.36	$22.80	$23.43	$23.76	$24.28	25%
	Shoulder	$19.35	$22.29	$22.73	$23.36	$23.69	$24.21	25%
	Offpeak	$19.27	$22.22	$22.65	$23.28	$23.62	$24.14	25%
ATR	Peak	$14.57	$15.52	$15.95	$16.58	$16.92	$17.43	20%
	Shoulder	$14.38	$15.33	$15.76	$16.40	$16.73	$17.25	20%
	Offpeak	$14.20	$15.15	$15.58	$16.21	$16.55	$17.06	20%
Q300	Peak	$14.70	$15.65	$16.08	$16.71	$17.05	$17.56	19%
	Shoulder	$14.45	$15.40	$15.83	$16.46	$16.80	$17.31	20%
	Offpeak	$14.20	$15.15	$15.58	$16.21	$16.55	$17.06	20%
C208	Peak	$15.33	$16.28	$16.71	$17.34	$17.68	$18.19	19%
	Shoulder	$14.29	$15.24	$15.67	$16.30	$16.64	$17.15	20%
	Offpeak	$13.25	$14.19	$14.63	$15.26	$15.59	$16.11	22%
PC12	Peak	$16.03	$16.97	$17.40	$18.04	$18.37	$18.89	18%
	Shoulder	$14.64	$15.58	$16.02	$16.65	$16.98	$17.50	20%
	Offpeak	$13.25	$14.19	$14.63	$15.26	$15.59	$16.11	22%

Notes:

1) Excludes parking, includes average discounts for growth, assumes 80% LF.

2) FY24 published charges prorated to adjusted FY24 revenue

Table: Average International Charges per Passenger

Aircraft	Time Period	FY24 (Note 2)	FY25	FY26	FY27	FY28	FY29	FY29 vs FY24
A321	Peak	$28.43	$31.13	$31.43	$30.06	$30.62	$30.11	6%
	Shoulder	$28.37	$31.07	$31.38	$30.00	$30.56	$30.05	6%
	Offpeak	$28.31	$31.01	$31.32	$29.94	$30.50	$29.99	6%
A320	Peak	$28.46	$31.16	$31.46	$30.09	$30.65	$30.14	6%
	Shoulder	$28.39	$31.08	$31.39	$30.02	$30.58	$30.07	6%
	Offpeak	$28.31	$31.01	$31.32	$29.94	$30.50	$29.99	6%
B738	Peak	$28.46	$31.15	$31.46	$30.09	$30.65	$30.14	6%
	Shoulder	$28.38	$31.08	$31.39	$30.02	$30.58	$30.07	6%
	Offpeak	$28.31	$31.01	$31.32	$29.94	$30.50	$29.99	6%
A359	Peak	$28.41	$31.11	$31.42	$30.04	$30.60	$30.09	6%
	Shoulder	$28.36	$31.06	$31.37	$29.99	$30.55	$30.04	6%
	Offpeak	$28.31	$31.01	$31.32	$29.94	$30.50	$29.99	6%

Notes:

1) Excludes parking, includes average discounts for growth, assumes 80% LF.

2) FY24 published charges prorated to adjusted FY24 revenue

Aeronautical revenue summary

353. The following table outlines Aeronautical Revenue by charging component over PSE5. Around 70% of revenue is airfield, consistent with the required revenue, with the scheduled per passenger component generating almost all the revenue. Unscheduled aircraft generate just over 1% of revenue, the peak runway component 0.2% and parking 0.1%. Around 30% is terminal revenue. Overall, forecast incentives are around 3.5% of total aeronautical revenue.

Table: Aeronautical Revenue by Component ($m)

Category	**FY25**	**FY26**	**FY27**	**FY28**	**FY29**	**Total**	**% of Total**
Airfield Fixed	0.323	0.330	0.333	0.327	0.323	1.636	0.2%
Airfield Pax	93.029	99.819	106.831	112.477	119.465	531.620	71.8%
Airfield Unscheduled	1.997	2.053	2.107	2.136	2.191	10.483	1.4%
Airfield Parking	0.161	0.169	0.176	0.177	0.181	0.864	0.1%
Airfield Inentives	-2.305	-2.999	-4.108	-4.140	-5.401	-18.953	-2.6%
Airfield TOTAL	93.205	99.372	105.338	110.978	116.758	525.651	71.0%
Terminal Pax	39.037	41.810	44.428	46.715	49.401	221.392	29.9%
Terminal Incentives	-0.967	-1.220	-1.400	-1.382	-1.707	-6.676	-0.9%
Terminal TOTAL	38.070	40.591	43.028	45.332	47.694	214.715	29.0%
TOTAL	131.276	139.963	148.366	156.310	164.452	740.367	100.0%

PART O: NOISE MITIGATION CHARGES

Summary

354. In PSE1 WIAL commenced discussions with its substantial customers with a view to establishing charges for airport noise mitigation activities (previously called LUMINS, or Land Use Management & Insulation for Airport Noise activities). These activities included the removal of certain noise affected properties close to the airport and the noise insulation of other specified properties.

355. As a result of prior consultations, WIAL has taken the approach of including a separate charge for noise mitigation activities.

356. The approach to noise mitigation activities is working well and supported to date by all parties. WIAL considers that the commercial arrangement has been given effect by:

- The provision of specific feedback by the consultation participants, but not objections, on the proposed charge in the PSE3 consultation.
- Management of the noise mitigation activity being undertaken by the independent Air Noise Management Committee which includes local community and airline representatives.
- WIAL's provision of updates to BARNZ, on behalf of airline customers, on the progress of the scheme, including annual accounts for WANT Limited and financial outcomes.

357. In short, airlines are overseeing financial aspects of the noise mitigation activities in the manner proposed by the commercial agreement.

Progress of Noise Mitigation Programme

358. To date, 6 properties on the airport's boundary have been acquired with the houses being removed and approximately 111 houses have received noise insulation treatment.

359. WIAL has continued to manage the rollout of the programme in line with cashflows from the current $0.32/passenger charge. This has required careful management throughout Covid-19 with limited revenue from low passenger numbers. WIAL is now completing approximately 1.5 house treatments each month.

Noise Mitigation Model

360. WIAL's separate noise mitigation model seeks to achieve an NPV = 0 over the life of the project.

361. WIAL is therefore seeking to continue to recover the costs of the activity from a separate charge levied to airlines. The charge will be discontinued when the project is concluded.

362. The key assumptions in the forecast continue to be:

- Timing & rates of uptake on offers to insulate or purchase homes;
- Average costs of insulation works per house;
- Purchase price & write-off costs of houses acquired; and

363. A copy of the forecast is attached in the PSE5 building block model file.

PSE5 Outcome

364. WIAL considers the current pace of delivery appropriately balances the need to complete works in a timely manner whilst maintaining a reasonable charge to airline customers.

365. Based on current run rates, WIAL estimates the rollout will be completed during PSE6. The timeline has been extended from PSE4 forecasts due to Covid-19 impacts and actual uptake rates being higher than estimated.

366. Forecasts show a small increase in the Noise Mitigation charge (from $0.32 to $0.34 per passenger) will be required to achieve an NPV neutral outcome by the end of PSE6. This is predominantly driven by the higher uptake rates plus inflation in costs of construction.

367. WIAL is also open to accelerating the rollout if preferred by airlines, but notes this would require a larger increase in charges.

IRD Binding Ruling

368. WIAL reminds its substantial customers that during the PSE3 consultation WIAL sought an IRD binding ruling with regard to the tax treatment of house removal and noise mitigation costs in its wholly owned subsidiary WANT Limited. An IRD ruling was received and the noise mitigation building block model is consistent with this ruling.

369. The IRD issued the ruling for a four-year period ending on 31 March 2016, which was subsequently extended. WIAL's model assumes that the IRD's ruling will have effect for the entire project and WIAL has no reason to believe that the approved tax treatment will be changed pre or post expiry of the binding ruling. Nonetheless if the IRD does change its view or ruling in the future WIAL retains the option to adjust pricing for the noise mitigation activities at that time, in accordance with the implications of any IRD change.