

# Restructuring and the regulation of airport charges

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Dublin, 1 October 2004

- How should the Commission for Aviation Regulation respond to financial restructuring, and the related allocation of assets and liabilities to Dublin, Cork and Shannon Airport Authorities?
- We have sought to answer this question from an economic perspective

# The purpose of economic regulation

- Economic regulation where competition is (currently) ineffective should emulate outcomes that one would expect in a competitive market
  
- In competitive markets:
  - goods and services are produced at the lowest possible costs
  - goods and services are provided to anyone who is willing to pay more than production costs
  - firms invest to reduce costs, provide necessary capacity, and improved quality and new services
  
- Economic regulation should achieve the same, i.e. aim for economic efficiency

# How regulation aims at efficiency

- Provide incentives for firms to reduce costs and make appropriate investments while removing excess profits
- Price cap regulation has such incentive properties
  - Price cap limits the firm's ability to charge in excess of costs, while providing flexibility on how charges are structured, and incentives to reduce costs
  - Price cap is set with reference to efficiently incurred costs (both capital costs and operating expenditure), and how these change over time

- Financial structure has ***no direct impact*** on the cost of providing services (though it affects the division of returns between owners and creditors)
- ***Indirect effects*** due to:
  - impact on managerial incentives (and thus efficiency)
  - impact on cost of capital (weighted average cost of capital, or WACC)
- In setting a price cap:
  - inefficiencies as a result of imperfect governance are discounted
  - although a similar approach could be taken with regard to WACC, often actual WACC is used

- Restructuring:
  - does not affect the assets needed to provide services at Dublin airport
  - should not affect efficiently incurred costs
  - may affect WACC
- No adjustments to general methodology necessary or appropriate
- Factors used in setting the cap may need to be adjusted
- This is in line with what would happen in a competitive market, where prices would be determined by competition between firms, not how they finance their businesses