



Cynulliad
Cenedlaethol
Cymru

National
Assembly for
Wales

Cofnod y Trafodion The Record of Proceedings

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[The Public Accounts Committee](#)

11/02/2016

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Motion under Standing Order 17.42 to Resolve to Exclude the Public
from the Meeting

Cofnodir y trafodion yn yr iaith y llefarwyd hwy ynnddi yn y pwyllgor. Yn
ogystal, cynhwysir trawsgrifiad o'r cyfieithu ar y pryd.

The proceedings are reported in the language in which they were spoken in
the committee. In addition, a transcription of the simultaneous interpretation
is included.

Aelodau'r pwyllgor yn bresennol
Committee members in attendance

Mohammad Asghar Bywgraffiad Biography	Ceidwadwyr Cymreig Welsh Conservatives
Jocelyn Davies Bywgraffiad Biography	Plaid Cymru The Party of Wales
Mike Hedges Bywgraffiad Biography	Llafur Labour
Darren Millar Bywgraffiad Biography	Ceidwadwyr Cymreig (Cadeirydd y Pwyllgor) Welsh Conservatives (Committee Chair)
Julie Morgan Bywgraffiad Biography	Llafur Labour
Jenny Rathbone Bywgraffiad Biography	Llafur Labour

Eraill yn bresennol
Others in attendance

Chris Cain	Cyfarwyddwr a Phennaeth Ymchwil, Northpoint Aviation Director and Head of Research, Northpoint Aviation
Yr Athro / Professor Stuart Cole CBE	Athro Emeritws Economeg a Pholisi Trafnidiaeth, Prifysgol De Cymru Emeritus Professor of Transport Economics and Policy, University of South Wales
Andrew Miller	Cadeirydd Maes Awyr Glasgow Prestwick Chair of Glasgow Prestwick Airport
Matthew Mortlock	Swyddfa Archwilio Cymru Wales Audit Office
John Nicholls	Cyfarwyddwr, Teithiau Awyrennau a Llongau, Camlesi a Chludo Nwyddau, Transport Scotland

Director, Aviation, Maritime, Freight and Canals
Transport Scotland

James Price Dirprwy Ysgrifennydd Parhaol, Grŵp yr Economi,
Sgiliau a Chyfoeth Naturiol, Llywodraeth Cymru
Deputy Permanent Secretary, Economy, Skills and
Natural Resources Group, Welsh Government

Huw Vaughan Thomas Archwilydd Cyffredinol Cymru
Auditor General for Wales

Swyddogion Cynulliad Cenedlaethol Cymru yn bresennol
National Assembly for Wales officials in attendance

Fay Buckle Clerc
Clerk

Claire Griffiths Ail Glerc
Second Clerk

Joanest Varney-
Jackson Uwch-gynghorydd Cyfreithiol
Senior Legal Adviser

Dechreuodd y cyfarfod am 09:08.
The meeting began at 09:08.

Cyflwyniadau, Ymddiheuriadau a Dirprwyon
Introductions, Apologies and Substitutions

[1] **Darren Millar:** Good morning, everybody. Welcome to today's meeting of the Public Accounts Committee. Just the usual housekeeping notices before we start the meeting proper. I just remind everybody that the National Assembly for Wales is a bilingual institution and that Members and our witnesses today should feel free to contribute to the proceedings through either English or Welsh as they see fit. If I could encourage everyone to switch off their mobile phones, or pop them on to 'silent' mode so that they don't interfere with the broadcasting equipment. And, obviously, in the event of a fire alarm, we should all follow the directions of the ushers.

[2] We've received a number of apologies this morning. We've had apologies from Sandy Mewies and Aled Roberts, and Mohammad Asghar will

be joining the meeting a little later on. We've taken oral declarations of interest at the start of this inquiry, so I won't ask Members to repeat those, but if anything does crop up during the course of the meeting, if Members could disclose at that time, I would be very grateful.

09:09

Papurau i'w Nodi Papers to Note

[3] **Darren Millar:** We've got a number of papers to note. We've got an update letter from Simon Jones in relation to the intra-Wales Cardiff to Anglesey air service. I'll take it that that paper is noted. It just provides a little bit more information in relation to opening times and the ongoing review of the marketing strategy, and a bit of a background to the suspension of the contract. I'll take it that that's noted.

[4] We've also had a letter from Matthew Quinn in the Welsh Government in relation to our follow-up work on the Glastir inquiry. It particularly touches on actions that have been taken by Natural Resources Wales to tackle some of the water framework directive failures, and I'll take it that that paper is noted. Is everyone content?

Maes Awyr Caerdydd: Sesiwn Dystiolaeth 3 Cardiff Airport: Evidence Session 3

[5] **Darren Millar:** We'll move on, then, to item 3, which is continuing our inquiry into Cardiff Airport. This is our third evidence session. I'm very pleased to be able to welcome James Price, the deputy Permanent Secretary in the economy, skills and natural resources group in the Welsh Government. Welcome to you, James.

[6] Obviously, the Auditor General for Wales published his report into Cardiff Airport's acquisition and ownership, and the performance of the airport, on 27 January. We received an oral briefing on that report. As you can imagine, Members have a number of questions that they want to ask you. I'll start with this, Mr Price: one of the things that the auditor general's report describes is the period in the run-up to the acquisition and some of the work that the Welsh Government had done to support the airport. Clearly, the Welsh Government, in the evidence that we've received so far, felt that the

airport was of strategic importance to Wales, yet it wasn't identified as an anchor company. Is there any reason for that?

[7] **Mr Price:** Actually, I think that's a very fair point, Chair. The anchor company programme is still an evolving programme of the Welsh Government. Typically, we are working with companies that we see, as you quite rightly say, as being of strategic importance to Wales. On that basis, I guess the airport could well be defined as one of those. Whether that would be quite so applicable under public ownership or not, I don't immediately know the answer to that. It may well be, and I think that's a fair challenge. There's quite a rigorous process to go through to become an anchor company. So, it wouldn't simply be that a very small company that was of strategic importance would immediately become an anchor company, but it probably at least ought to be a regionally important company. So, I think that's probably a fair point. But, at the time, that policy was just in its infancy and emerging. It's much more fully thought through and used now—this is the anchor company policy.

[8] **Darren Millar:** So, looking back now, and at the current arrangements to identify anchor companies, would Cardiff Airport have been allocated that sort of label—?

[9] **Mr Price:** I'm not immediately convinced that it would have done, and that would be because of its size rather than its strategic importance. But it certainly now would be looked at, as part of that. But I need to emphasise that the anchor company policy at that time was a very new policy. I think we went from having six or seven anchor companies for the whole of Wales to—and I'm quoting off the top of my head—about 30 now. So, I don't think it was necessarily an oversight at the time, but I think you're making a very fair point, and one that I ought to take away and have a look at now.

[10] **Darren Millar:** Just in terms of the other interaction that happened around the airport, obviously the Welsh Government was expressing concern about the decline in passenger numbers and the longer term viability of the airport. That prompted some discussions with the airport about possible support—marketing support and the establishment of a taskforce. Do you think that that level of engagement was sufficient, or, with hindsight, could there have been more?

[11] **James Price:** Okay, so, on this, I can speak quite personally in terms of the engagement with the local management team at the airport because, at

the time, I was director of transport, so I was involved quite closely with them—the previous chief exec, bar one, and, actually, Deb Barber, who is still there and was there at that time, but not in that chief executive officer role. From a transport perspective, we were doing all we could to try and cement Cardiff Airport into Wales and encourage additional links. So, in terms of what we were doing with local management, I think we did an awful lot. I would say that's evidenced by the fact that we took state aid approval through to the European Union. It took a long time—I think that was the EU end rather than our end—and we had a number of different discussions with them about landing charges, and maybe if they could bring those down, they might be able to increase demand. I think that period, probably from about 2007 all the way through to when the taskforce started, was characterised by an increasing lack of wish to engage on behalf of the local management team. I think they were probably—though not in any improper way—instructed, really, not to engage because they had a business model that was based upon maximising income in the same way that you max income on car park charging, which is to maximise landing charges.

09:15

[12] This was at a time when other airports across the UK were minimising landing charges and making money on other things—ironically, such as car parking and retail space. So, at a local management level, I think we did quite a lot, and then, latterly—I wasn't personally involved in any of the meetings, but there were a significant number of meetings at a pretty senior level involving Abertis a couple of times over here, a number of senior-level telephone conversations, and a number of trips to Spain to visit them to stress the importance of this, as well. So, I'm sure Government can always—everyone, frankly, can always do a bit more. I don't think anything more we could have done would have made any difference.

[13] **Darren Millar:** We were told by the airport chief exec last week that there was quite a tightening of the belt in terms of the investment in the capital infrastructure, and that that's partly why this support via some state aid was being looked at, and you were trying to get the approval from the EU. Clearly, with those sorts of things, where you can see the belt being tightened further and further, the speed of getting some support in to match fund any contributions from the company that then owned the airport would have been pretty important. Why did it take so long to get the approval?

[14] **Mr Price:** Well, I think, two things there—we were running at this as

quickly as we could. I remember being put under significant pressure from Ministers—this is back in 2007–08—to get this work through. But getting a scheme approved at the EU does take quite a long period of time. You have to put a significant amount of evidence in, it has to be submitted through the UK Government, it's tested, and I think the entire period took about two years to get it through, which is, I agree, a long time, but it's certainly not unheard of.

[15] But the point I would stress is, throughout that whole period, we were trying to work with the airport anyway to do other things, and I remember having a particularly frustrating conversation—I think it was frustrating for the manager concerned, as well, at the airport—where we had a potential airline that would happily go in there, and they weren't prepared to drop their landing charges at all, even though he was agreeing with me that it would improve the profitability of the airport. That is because he was—or his performance metrics were around the amount of aeronautical revenue brought in, not the profitability of the unit, which comes back to my car-parking-charge mentality.

[16] **Darren Millar:** And there was a very low take-up as well of this route development fund, wasn't there, Mr Price? Can you tell us about what the arrangements for that route development fund were, and why there was no take-up?

[17] **Mr Price:** Well, I think it's partly to do with the economics at the time. I think it was a lot to do, though, with the airport, and maybe partially to do with the scheme as well. So, in the past, if you look a long way back, the rules around state aid and route development funds were quite—I say 'lax', they were more lax than they were in the period 2007–11, and since then they've actually become a bit laxer again for smaller airports. So, compare a relatively challenging economic condition, with an airport management team that didn't seem to be incentivised to bring in flights, with a scheme that had had its rules tightened as a result of EU policy—I think put all of those three together and maybe it wasn't that surprising, the outcome that we got. I think if any one of those three had altered, we could have got a better—a marginally better, I would have suggested—outcome.

[18] **Darren Millar:** You seem to be presenting the EU approval stuff as being quite a negative here, in terms of the ability to be able to support the airport and provide rapid decisions on the sort of support that could have been available. Is that a reasonable conclusion?

[19] **Mr Price:** I think there are two different things I'm talking about here, and I need to just be careful that I don't conflate the two. So, getting the EU approval to support the project, you can do that—and I'm sure everyone around the table will be aware of this—and you can have a go at doing that for almost anything. So, you can notify a scheme to do anything, and then you have to get it approved by the EU. I think that's right and proper that that's a tested approach, and I think the EU is not renowned, at official level, for moving things very quickly. But we knew that and we expected that to take a while. The company knew that as well. Frankly, in terms of planning investment of, I think, just shy of £25 million in infrastructure, a two-year running time would have been okay. The other piece I was talking about, I don't think that was anything to do with the EU being slow. That was EU rules that you have to work within.

[20] **Darren Millar:** On the route development fund?

[21] **Mr Price:** Yes.

[22] **Darren Millar:** Okay, and just to shed a little bit more light on the arrangements for the taskforce now—obviously, the taskforce was set up, I think, back in 2012. That comprised officials and other people who wanted to engage with the airport and try to give a bit of support. You were directly involved in that taskforce.

[23] **Mr Price:** I didn't attend, actually. But I know quite a bit about it; so, I can talk to it.

[24] **Darren Millar:** Okay. What was the rationale behind the establishment of that? How frequently did it meet? How did it engage?

[25] **Mr Price:** The rationale was actually very similar to the rationale that we have got now for the current Tata taskforce, albeit that it was brought in place before anything particularly bad had actually occurred. The attempt was to try and bring local management, Government, stakeholders, and any other business that had an interest together to try and (a) understand if there really was a problem (b) understand what people's objectives were and (c) try and understand what could be done about that. I think if you speak to people who were on the taskforce, they certainly would agree that it was effective in terms of identifying what the problem was and what the objectives ought to be. I think that they, like us previously, ran into difficulties in the sense of

‘What are you going to do about it?’, because, with a head office that—. I’m sure for very good reasons for them, Cardiff Airport was not part of their strategic plan for growth. You can’t force someone to do something in a market economy that they don’t want to do.

[26] **Darren Millar:** There was this unusual step as well, wasn’t there, of seconding a Welsh Government official to the airport. Is there any other situation where somebody’s been seconded to work in a private company?

[27] **Mr Price:** Okay. So, much as—

[28] **Darren Millar:** I mean, that suggests a willingness on the part of the airport to work with Government—

[29] **Mr Price:** Yes, and I think local management—

[30] **Darren Millar:** The picture you’ve painted is that they weren’t really interested. But they clearly accepted somebody working with them and being placed there.

[31] **Mr Price:** And, again—maybe I’m explaining this a bit unclearly. I think local management had a will to want to work with us, and that was a local management decision to take the secondee. But local management work within the framework of the major company. If I go back to when I had that kind of frustrating conversation with a senior manager of the airport when I was director of transport, both he and I were equally frustrated. He couldn’t allow this airline to come in because he wasn’t allowed to reduce aeronautical revenue per passenger, even though he knew it would increase his profitability.

[32] Just coming back, though, to the question on the secondee—sorry, I don’t mean not to answer that—quite a lot has been written about it. But the one thing that hasn’t been written, and I think is important and fair to say this, is that the individual was looking for a secondment anyway. It just so happened that that was one of the opportunities to place him. So, it’s quite unusual, yes. I’d like to see it happening a lot more, and not just in those circumstances. I think I’d like to get to a position where we’ve got much more interchange between different parts of the public sector, and certainly the public sector and the private sector, to gain a better understanding. France has got a long history of doing that. Since then, we have actually done it with one of the senior members of the rail team who spent a year and a

half in the Rail Delivery Group in London in a senior post and then came back to the Welsh Government.

[33] **Darren Millar:** Okay, thanks for that. Mike Hedges and then Julie.

[34] **Mike Hedges:** Coming back to anchor companies, you've said the airport wasn't—. I don't know the 30; I don't know who the seven were, so, if I should know it, I apologise. But what I'm asking is: are Associated British Ports and are freight companies part of it? Are the anchor companies basically manufacturing companies or do they include people who are involved in activities not dissimilar to the airport?

[35] **Mr Price:** So, I haven't got the full list in front of me. As we stand here, I do not believe ABP is an anchor company.

[36] **Darren Millar:** You'll send us a note, will you?

[37] **Mr Price:** I'll certainly send you a note, and I'll send you a note on the criteria. I think this is an interesting question that's being raised here about whether, basically, something that forms a core part of the infrastructure for Wales, but which is a private company, ought to be included in that programme. We would certainly work with them in a strategic way anyway, and we do work very closely with ABP, and we were working very closely with Cardiff Airport. But I think it's a fair question, and one for us to look at.

[38] **Mike Hedges:** The other question I've got—you keep on mentioning that their fees and charges were not competitive compared with other airports. You may not want to or won't be able to answer this, but how can an airport be successful if it's charging substantially more than its competitors?

[39] **Mr Price:** I don't think it can be, and I think that was one of the reasons why it wasn't. But it's very difficult. So, if you think of it from the position of a business, they know they are guaranteed landing fees if they charge landing fees and if there are planes landing. So, for the core business that they'd dropped down to—about 1 million—I think they thought, for the time being, that 1 million was probably relatively safe. Some of the fees they were charging at the time I think were up to about £30 per person. Now that would compare with other, bigger airports that certainly, for some of the low-cost flyers, will charge nothing or up to maybe £3 a person. So, you're of a magnitude out, but there's a gap, if you like, so they can reduce that,

they take less revenue immediately, and what they're doing is they're gambling on trying to get more people flying to charge more on car parking and to be able to get more for their retail outlets. I think that was the issue, and it was described to me by the management at the time that they're running it like a car park—and that wasn't a negative comment; they own lots of car parks, the company—or running it like a road concession, where you're charging for the use, but you're not maximising the alternative uses around the sides, like a service station or whatever else it might be.

[40] **Mike Hedges:** Can I do the 'what if'? What if it had continued along those lines? There's no guarantee you're going to hold 1 million air passengers. There's no reason why people would want to pay £30 per passenger more to land in Wales than they would—. For most of us in south Wales, Bristol is less than an hour away from here, Birmingham's an hour and a half away from here, and Cardiff Airport's about 20 minutes away from here. So you're not talking huge differences in time of travel for most—possibly for Julie, because she lives very close to it. But for the rest of us in south Wales, you're not talking about huge differences in time considering how long you spend in the air to get somewhere. Was there not a danger that that 1 million passengers could drop down considerably? We do have airports running on a few hundred thousand.

[41] **Mr Price:** I think that indeed was the danger, and that's what the taskforce was very worried about, yes. If you graph the trajectory of (a) growth, which is really interesting, from 2002, really, when it started picking up, I think, 2005 particularly and 2006, it grew massively, and then it dropped off just as quickly. When you talk to management, they took an aggressive growth stance, they were offering incentive deals to airlines, and then they stopped doing that and people started to leave. So, I think you're quite right—the fear was, and the indication was, that would continue, and indeed they did lose significant flights. BMI et cetera did pull out.

[42] **Mike Hedges:** Just finally, can I take you back before 2002, back to when it was run by the three Glamorgans? Then there was substantial growth as well, wasn't there? Perhaps—again, I don't think it's in your paper—if it is, I apologise for not remembering it—but have we got a graph of number of flights from it over a 20 or 25-year period to give us some sort of understanding of how it has grown, dropped and grown?

[43] **Mr Price:** Yes, I've seen that, and that was one of the things I was referring to when I was just talking about that. But it's a massive increase

and then an equally quick decrease.

[44] **Mike Hedges:** Have we got it going back to the 1990s as opposed to just the 2000s?

[45] **Mr Price:** In terms of the approach for the airport?

[46] **Mike Hedges:** No, in terms of passenger numbers.

[47] **Mr Price:** Well, the passenger numbers peaked in 2005–06.

[48] **Darren Millar:** In terms of that historic data, we can probably pull that through—

[49] **Mr Price:** Yes, from the note. It was just over 2 million, wasn't it? That was the peak.

[50] 09:30

[51] **Mike Hedges:** Yes, but it was running at well in excess of a million back in 1990.

[52] **Mr Price:** For quite a long time, yes. I think it's in the auditor general's report, but we can provide a note on that, certainly.

[53] **Mike Hedges:** I don't think the auditor general's report goes back to the 1990s—

[54] **Mr Price:** Not that far.

[55] **Mr Thomas:** 1997.

[56] **Darren Millar:** 1997 it goes back to.

[57] **Mike Hedges:** It doesn't go back—

[58] **Mr Price:** If you'd like a note on that, we can—

[59] **Darren Millar:** We'll have that from you. Can I just check something with you? In terms of the relative performance of Cardiff versus other airports, because it's an important point that Mike's picked up on, the

performance was similar to other smaller airports that were alongside bigger regional competitors, wasn't it? So, the other airports were doing similar stuff with their landing fees, were they?

[60] **Mr Price:** No. I don't think they were. I think Cardiff's approach was quite unusual for the UK.

[61] **Darren Millar:** But, in spite of those landing fees, it seems to have held its own compared to other competitors within similar proximity to airports like Bristol.

[62] **Mr Price:** I cannot honestly comment on the technical detail of that, but I can comment on what people in the industry have told me. Their view is that Cardiff performed, given where it came from—and it wasn't a Plymouth or a Southend, it was actually a significant airport in its own right; it had plans to grow to 3 million or 4 million passengers. Whilst Bristol more than doubled in size, it halved. So, I think it underperformed, given its potential.

[63] **Mike Hedges:** I can't remember the figures, but I think Cardiff and Bristol were running at roughly the same number for a long period of time. Tell me if you think I'm wrong, but these were the second-ranking airports. You had the big ranking airports—the Manchesters, the Heathrows, the Gatwicks, et cetera.

[64] **Mr Price:** Yes, and then you had a tier 2.

[65] **Mike Hedges:** A tier 2. Bristol and Cardiff were roughly the same sort of tier 2 airports, with tier 3, then, the sort of Plymouths, Bournemouths and Norwich—those very much local airports. Then you have tier 4, things like Swansea, which, effectively, are flying clubs.

[66] **Mr Price:** Yes.

[67] **Julie Morgan:** You shared with us your frustration that you said was shared with the local managers at the airport itself about the lack of progress. How much contact was made with the actual owners during this period?

[68] **Mr Price:** Okay. So, in the very early period, back when I was talking about 2007, I doubt very much was being made with the owners, because we were dealing with what we thought were locally empowered people. That

fairly quickly became clear that they weren't massively empowered. So, by 2009, I think we would've been engaging with the head office. But, back when I started talking about 2007–08, we were engaging with the local management team.

[69] **Julie Morgan:** Right. So, did you have any engagement with the overall management team?

[70] **Mr Price:** Personally, no, but that engagement was held at a senior level, so it was Jeff Collins, who was a director who worked for me and various other directors within the wider Welsh Government, and the Minister for Economy, Science and Transport. I believe the First Minister had some conversations as well.

[71] **Julie Morgan:** So, there were efforts to engage—

[72] **Mr Price:** Most certainly, yes.

[73] **Julie Morgan:** —with the owners of the company.

[74] **Mr Price:** Yes. I remember this vividly, because Jeff Collins, actually, phoned me up as he was going to get back on the plane complaining he had a bad back, because he was carrying so many books and files—mainly books. I think Abertis had given us loads of books with pictures in them, rather than anything about how they could improve the airport.

[75] **Julie Morgan:** So, at what date did you identify that, really, they weren't interested in the airport?

[76] **Mr Price:** In retrospect, I think it was apparent as early as 2008. I think we probably had concluded that by 2010 or 2011.

[77] **Julie Morgan:** Right, thank you.

[78] **Darren Millar:** Okay. Jocelyn.

[79] **Jocelyn Davies:** Yes, thank you. Obviously, the airport is strategically important for Wales, but it seemed, obviously not for the owners of the airport, and, of course, we were in deep recession. So, passenger numbers are affected by that on top of everything else, and you mentioned the other factors. Something that I wanted to raise with you—first of all, can you tell us

what we got for £52 million? I know we talk of the airport and you've been mentioning the car park. Can you describe to us what that package includes?

[80] **Mr Price:** Okay, yes, and we can also send a note with a plan, et cetera on this as well, which might be quite helpful.

[81] **Jocelyn Davies:** Thank you.

[82] **Mr Price:** We acquired the whole—. I'll go beyond what I'm about to say, because it will just seem like I'm not answering the question otherwise. We acquired the whole of the shareholding of what was TBI through Abertis group for a price as you've quoted, and that included quite a lot of land that you're not really aware of that the airport owned—and that's typical for airports, they own quite a bit of land around them—all of the car parking—the car parking is not out on a concession, which it is in many airports, which means that the airport is able to do what they want with it, redevelop it, maximise the income from it—the terminal building, the runway, the aprons, the ownership of the firefighting equipment, and all equipment on site, actually, the avionics, air traffic control, and all ancillary work.

[83] **Jocelyn Davies:** Okay, thanks for that.

[84] **Mr Price:** So, everything within the fence and beyond.

[85] **Jocelyn Davies:** Right. But you'll send us a map—

[86] **Mr Price:** Yes.

[87] **Jocelyn Davies:** —so we can see that. Now, I know that—

[88] **Mr Price:** And an inventory, if you want.

[89] **Jocelyn Davies:** Okay. I know that airports must be very difficult to value. They're not like other things, and, earlier this week, when we took evidence from Simon Jones, he mentioned the EBITDA, earnings before interest, taxes, depreciation and amortization, which, I have to say, I've been swotting up on, Chair, because I'd never heard of it before. He said that it was somewhat discredited in terms of using that as your valuation tool, and I can see why from the stuff that I've been reading since, but he said that—

[90] **Mr Price:** But it's frequently used.

[91] **Jocelyn Davies:** Well, he did say, and he is a Welsh Government official, that it's somewhat discredited—

[92] **Mr Price:** Yes, I agree, but—

[93] **Jocelyn Davies:** Perhaps you'd explain that, but he did say that, had you used that, or had that been used, the result would have been modest, but I think he told us he couldn't remember what it would've come out at. Are you able to tell us, or would you like to explain why you think that it's perhaps not a credible benchmark for working out the value of an airport?

[94] **Mr Price:** So, do you want me to talk about the valuation methodology when we bought the airport originally, or—?

[95] **Jocelyn Davies:** Well, he was the one that mentioned this EBITDA—

[96] **Mr Price:** Okay, that's fine. So—

[97] **Jocelyn Davies:** —which we didn't know anything about, and he said—. I don't even remember why, really, he told us, but he did say, had that been used—

[98] **Darren Millar:** I think, to put a bit of context on this, we were—

[99] **Mr Price:** I've read his evidence, so—

[100] **Darren Millar:** We were enquiring just about the value at some future date, and the suggestion was—

[101] **Mr Price:** Well, it probably would be a help to—

[102] **Darren Millar:** —that if the numbers got up to about 2 million again it would be worth—

[103] **Mr Price:** There may be a significant value in it. Okay.

[104] **Darren Millar:** —£150 million-ish, based on an EBITDA valuation.

[105] **Mr Price:** So, it probably would be worth just exploring what we did when we purchased it, and then rolling it forward, maybe, just for full

disclosure and the fact that I've spent quite a lot of time making sure I understood it, so—. From what I can see, and we looked at all of these as well, there are three different ways of valuing a business or an airport. One of them would be an asset valuation, so, if it wasn't trading, what are the assets worth. One of them would be an EBITDA multiple, which is, basically, how much money does the airport make, and then you multiply it by a certain factor. The certain factor is market driven, in the same way that house prices are market driven. So, you look at similar purchases and what multiple they have applied, and the multiples that were being applied to airport purchases were anything from about 14 to 22—Bristol was at the top end, whereas some of the other airports were lower down. And then there's something called the discounted free cash-flow analysis, which is actually very similar to the EBITDA method, in the sense that what you're looking at is free cash in each period in the future—maybe 25 years—and free cash is a bit like profit, and EBITDA is, basically, profit, and then you discount it back using inflation, and you also apply a cost of capital that a reasonable business person would apply. So, any of those three methods could be used. We didn't use the asset valuation, apart from to support our opening offer to Abertis, which was done in-house, because it's very easy to get asset valuations off existing databases and just look at the size of land and multiply things up.

[106] We did use both a discounted cash-flow and an EBITDA multiple approach, albeit that, in the end, the Arup valuation was based on a discounted cash-flow rather than an EBITDA. However, I went through the figures myself with some of the team yesterday, and, if you had used an EBITDA—and I don't think Simon had done this at the time. If you'd used an EBITDA on the basis of an average EBITDA, which is what a DCF is doing, because it's looking at it over a number of years, rather than at a point-in-time profit, which, by definition, will vary—so you could have a very high profit, because you had a good year but you had no investment, or you could have a very low profit even if you had a good year, because you had massively high investment. So, if you look at that over an average period of time, the DCF and the EBITDA supported in the mid-fifties millions, basically.

[107] Now, I think the comment Simon was making is that, if you assume that the airport returned to just over 2 million passengers, and if you look back at the EBITDA that was being achieved by the airport at that time, which was somewhere between £7 million and £9 million—so, £8 million—multiply that by between 15 and 20 or 14 and 22 and you get something north of £150 million, which is three times more than we paid for it. Now, that's arithmetically correct, but the proof of the pudding would be in the eating,

obviously, and you've not only got to get the passenger numbers up, as I talked about earlier, you've got to make sure that you make the money on the passengers that are coming through the door through car parking, retail and other revenue. But it's not an unreasonable assumption, and we have had discussions with a number—I say 'a number'; I don't want to sort of overdo it—with three potential investors since we've owned it, who have been discussing with us whether they wish to invest on the terms that we invested.

[108] **Jocelyn Davies:** Right. Okay. Because I guess that, you know, when the Government comes to dispose of the airport, if it disposes of it for a considerable value, there'll be less criticism about what was paid for it, I assume—

[109] **Mr Price:** I guess that would undoubtedly be true, yes.

[110] **Jocelyn Davies:** But that depends on the future, doesn't it, and it looks like this recession is going to take a bit longer to get out of than we'd thought.

[111] The other thing that I wanted to ask you about was how you translate into value, then, the strategic importance of the airport for BA, that facility that's over there, because I notice from the recent report that we've had circulated to us—

[112] **Mr Price:** The Public Policy Institute for Wales one, yes?

[113] **Jocelyn Davies:** The PPIW one, where it says that the—on page 26 it says that that industry, the aerospace industry, is of very considerable significance to Wales. So, there are 23,000 people relying on it, and a combined turnover of £5 billion. This issue of British Airways Maintenance Cardiff, which we haven't heard a lot about yet—would that carry on without the airport?

[114] **Mr Price:** It's a hypothetical question.

[115] **Jocelyn Davies:** Well, not if the airport was going to close.

[116] **Mr Price:** No, I mean I've got to guess what would happen, and I don't know, but one thing is for certain: even if the runway was still there, if the airport closed the costs of being at that site would significantly increase for BAMC, because they'd have to maintain and run the runway themselves, and

that has a significant running cost—several millions of pounds a year—and a significant capital cost to keep resurfacing and keep equipment up together. So, my guess would be that, fairly quickly, BAMC would run their plant down and leave if the airport wasn't there, because the costs of operating would simply go through the roof.

[117] **Jocelyn Davies:** And they've got opportunities—. Because this is, in terms of the world, one of the biggest of those facilities.

[118] **Mr Price:** Absolutely, and they're looking at bringing in Dreamliner and various other things into there to maintain as well.

[119] **Jocelyn Davies:** Okay, so they could—. Did that figure in the case that you were putting together? Did that figure—not just what the airport could do, but the wider context in terms of the aerospace industry for Wales?

[120] **Mr Price:** I think there are two things here. 'Yes, it did', is the answer, but it didn't figure in our commercial valuation of the airport. So, we did two things. We looked at a public valuation of the airport as an asset, and that's the £472 million—I think; it might be £476 million—figure that was, again, quoted by Arup, and that took into account wider economic impacts, including BAMC, time savings in terms of road transport and various other things.

09:45

[121] **Jocelyn Davies:** BAMC is the British airways maintenance—?

[122] **Mr Price:** Yes, sorry. So, that was taken into account in that bigger figure, but we were very clear at the time that, even though that bigger figure would have suggested a much higher price than we paid, we were operating within a state-aid framework, and, regardless of that, we were operating in a way that we wanted to only spend the minimum necessary, so we only paid a commercial price.

[123] **Jocelyn Davies:** Okay. The other thing that I wanted—and I'll finish on this, Chair, if you don't mind—is the urgency. What was the urgency? Because I know that the Government used—I think it's the only time it's been used; I may be wrong—a section 128 in order to draw that money from reserves in order to pay. What was the urgency? Otherwise you would have had to bring a supplementary budget. So, why use that mechanism and why was the end

of our financial year the deadline for this?

[124] **Mr Price:** I remember now—you've reminded me of this—there being a very good technical reason, but I honestly can't remember exactly what it was. I haven't gone through it in preparing for this. I think we had opened negotiations and Abertis wanted to close it within a certain time window. We'd—

[125] **Jocelyn Davies:** So, this was pressure from the owners.

[126] **Mr Price:** Yes. We'd been given exclusivity for a certain time period, which is normal in negotiations and then the agreement to buy was held open for a certain period of time—the same way, if you bought a house, you'd exchange and then you complete within 30 days. I don't know what the number of days was on this—we could find out and put it in a note to you—but, from memory, that was the reason why we had to do this very quickly. I remember it raising quite a lot of eyebrows within the organisation because we hadn't done it before and it was tested—'Did we have to?'—and, if we didn't have to, we wouldn't have done it. But I think it's probably best if I get a note on it to make sure—

[127] **Jocelyn Davies:** Okay, so this was because of the sellers and not because of an end-of-year complication for Government.

[128] **Mr Price:** No, it wasn't anything to do with end-of-year budgeting, or anything like that, for us. It would have been well within our year-end flexibility anyway, this figure, but my understanding was, or—my recollection is that we had to close within a certain time period.

[129] **Jocelyn Davies:** Okay, thank you.

[130] **Darren Millar:** So, you had to close within a certain time period. That's your recollection.

[131] **Mr Price:** Yes, and I will check and provide a note.

[132] **Darren Millar:** Okay.

[133] **Mr Price:** I know we had to close within a certain time period and my recollection is that that's what drove the particular requirement—

[134] **Darren Millar:** That was the previous owners driving that rather than the Welsh Government—

[135] **Mr Price:** Yes, but that would be completely normal for purchasing anything. If you purchase a house, you exchange and you agree a timetable and you have to hit that timetable, otherwise there's interest and penalties and all sorts of other things.

[136] **Darren Millar:** Yes. Only here, you're not purchasing a house, you're purchasing an airport—

[137] **Mr Price:** Agreed.

[138] **Darren Millar:** —for multiple millions of pounds.

[139] **Jocelyn Davies:** Well, yes, and it's not your money.

[140] **Mike Hedges:** Can I just say that exactly the same thing happens when you purchase a football club: you have the exclusivity and then you have to either complete or it goes back out again. So, it seems—

[141] **Mr Price:** It's not unusual in a commercial—

[142] **Darren Millar:** Now we've kicked that ball around.

[143] **Jocelyn Davies:** But the thing I don't understand is why the Government didn't know this and didn't prepare for that before the end of our financial year. That's the bit that I don't understand. Obviously, I know the reason why the deadline was there now, but why not prepare for it in advance, because you must have known that that was the case?

[144] **Mr Price:** Can I take that away and provide a note quickly on it? Because I do remember at official level this being quite a big deal and, quite rightly, finance officials saying, 'Are you sure?', sort of 'We don't really want to do this.'

[145] **Darren Millar:** So, there was internal challenge to the timescale that you were pressing for.

[146] **Mr Price:** Yes, a lot of internal challenge on all of this, which is quite right, I think.

[147] **Darren Millar:** Okay. Can I just have a chat about these valuations again, these different methods of valuation, because this is something that a lot of people will be interested in? So, in terms of the three methods you've outlined, which are also, of course, detailed in the auditor general's report, there was an initial offer, which was made to Abertis, which was much lower, wasn't there—about £35 million?

[148] **Mr Price:** Yes.

[149] **Darren Millar:** Where did that figure come from?

[150] **Mr Price:** That figure came from a very quick desk-based analysis of the asset valuation of the airport, based on published data sources.

[151] **Darren Millar:** So that was an asset valuation that was done in-house.

[152] **Mr Price:** Yes.

[153] **Darren Millar:** Why go for that asset valuation, when quite clearly the other two are the more normally used—

[154] **Mr Price:** Okay, so I think—and, again, I haven't got the full detail of this; I could get it for you—. But, in all honesty, a conversation was being held in Spain, I believe, by a group of senior officials and, at the time, I had been quite interested in whether we could do any kind of joint venture. That was being raised with them and I think they shot back, 'We're not interested in a joint venture with you, but we'll sell it.' And there was a conversation on what figures we might want to open with. So, a quick, but proper, asset valuation was done—none of this would be binding, so there's nothing wrong with doing this—and the figure of £35 million was quoted.

[155] **Darren Millar:** But the problem in suggesting a figure is that the purchaser then knows roughly what you're prepared to pay up to.

[156] **Mr Price:** No. I can understand you making that comment, absolutely, but I don't think that's necessarily the case. So, again, I'd like to use the analogy of buying a business or buying a house. Typically, to get people to the table, you will agree a price, and, quite frequently now, in buying houses, people will come in and they'll offer the full price, subject to contract, subject to valuation and subject to survey, and they'll come back, kick the

tyres, and try and get the price down by 20 per cent. So, in all honesty, I do not believe that we damaged our negotiating position by quoting prices, and, when we were quoting £35 million, they were quoting £200 million. So, we were miles out. Our best guess of what they paid for the airport was between £120 million and £150 million. It's very difficult to work it out because they bought it in a group, as part of a wider group. They had it written down in their books as £200 million.

[157] **Darren Millar:** In terms of the Welsh Government's knowledge of the different ways of valuing airports at that time, were you not able to get some rough estimates using, again, a desk-based exercise, not a formal valuation by somebody independent, just to come up with some figures in terms of the other possible values? Because there was a big range, wasn't there, in the formal valuations that were done?

[158] **Mr Price:** Yes, and there would be if you did it again today, I think. So, I think that the safest valuation that we could have done in-house was an asset-based valuation, because it doesn't require as much commercial expertise and it would tend normally to offer the lower range rather than the higher range because you're not taking into account what profits might be made. You're not really taking into account the good will of the business either; it's simply the assets.

[159] **Jocelyn Davies:** But you're indicating the whole pathway—where they're saying £200 million, you're saying £35 million, so you're saying no way are we going up the—

[160] **Mr Price:** Yes. I think, we, probably, at that stage, told—you know, both sides told the other to get lost, really. But—.

[161] **Darren Millar:** Just to go through this, because it is important: when the formal valuations were done by KPMG, they came out with a range of between £6 million and £7 million right over to the £55-ish million that, eventually, was paid. That's a wide spectrum, isn't it, and you're negotiating position started off roughly in the middle. You'd had sight of some valuation information from KPMG before making this other offer of up to £55 million, subject to due diligence. Can you explain a little bit more about why you went in at the top of the range rather than somewhere in the middle?

[162] **Mr Price:** Yes. Absolutely. There was an awful lot of challenge provided. Again, I need to state—and this isn't me ducking anything—that

my position in this was as the person who was accountable for it and as the person who was challenging the team that was doing it—I wasn't doing it. But that's quite helpful in a way, so, all the way through the process, I was challenging the team and it got quite heated on occasions: 'I don't believe—', if I didn't at the time, '—that you can evidence what you're doing; I don't believe that's a fair price; I don't think we should be doing that.' And, at all times, those comments I made were taken into account.

[163] So, the challenge that you're giving me: was £55 million—up to £55 million; I think we said non-binding, open negotiations up to £55 million—was that a reasonable and a fair thing to do? That was exactly the question I asked the team in, frankly, quite a heated meeting and the conclusion was it was a reasonable and a fair thing to do on the basis that Abertis wouldn't come to the table to even discuss it without doing that. But that wasn't binding us to anything, because this was before formal valuations, it was before any due diligence had been done, and we could have walked away from the table anyway. So, I'd go back to the house analogy—and I'm guessing it's driving increasing numbers of people mad—where people come along, offer a price, and then try and negotiate it down afterwards.

[164] **Darren Millar:** Okay. And, just finally, on shared ownership, clearly Abertis were not interested in any kind of public-private partnership. Were there discussions with any other potential third parties to go into the same sort of arrangement with them?

[165] **Mr Price:** There were actually, yes—all subject to a non-disclosure agreement, so I can't quote any of the names, but, yes, there were. I met with a couple of airport owners, one of them very big, and talked about doing this. There was real potential for doing it. But with one of them—well, really, with both of them—the timescales that they wanted to work to didn't align with the timescales that we were looking at. So, they were talking about timescales of years rather than timescales of months.

[166] **Darren Millar:** And what was their rationale for talking in timescales of years?

[167] **Mr Price:** Simply because large companies tend to work in that way. This was non-core business for them, this was peripheral business, and we were talking about some of the bigger groups in the world, frankly, in this area. They weren't going to make a lot of money on it, but they were peripherally interested as part of a kind of risk-mitigation fact around the

edge. So, the conclusions of all of that were that we didn't take that forward, but that we could go back to them after we had made a purchase and potentially negotiate shared ownership at that point. Some of those people were the people I referenced earlier that we've discussed since—

[168] **Darren Millar:** Who you're still having discussions with.

[169] **Mr Price:** Yes. But it's got to be on terms that work for Wales. There's no point in doing it just to get some shared investment.

[170] **Darren Millar:** Just as a matter of interest, I presume that one of the questions that any of those other potential partners would have been asking would have been around, 'Well, what sort of price? What sort of investment are you looking for?'

[171] **Mr Price:** Yes. Absolutely.

[172] **Darren Millar:** Was that an issue for them—the fact that you'd made this offer of up to—

[173] **Mr Price:** No, and that's what's quite interesting. So, none of the people who we have talked to have walked away and all of them were aware, at the beginning of the meeting, even without me saying it, that we would expect, even at this stage, a 50 per cent equity stake, for example, to equal 50 per cent of what we paid for it. Their interest is all in what might happen in the future. It's a speculative interest in what growth and what profits might be.

[174] **Darren Millar:** Okay. Mike.

[175] **Mike Hedges:** Two questions: you said that they were holding a book value of it at £200 million, so they're actually showing a loss on book value in their accounts, which has probably done them a certain amount of damage. The question I really have is on asset value. You talked about asset value and valuing an asset. Were you valuing it as an airport asset or were you taking a residual land value? It's a bit like the regeneration investment fund for Wales situation that we looked at previously. Its residual land value where every part of it that is currently built on would be able to have houses built on it because the Vale of Glamorgan council, even if it wanted to, could not defend against house building on a site that currently has buildings on it: did you take into account the residual land value of it or were you just

valuing it as an airport? Because airports are not massively valuable unless they happen to be the very busy ones, but land in the Rhoose area of the Vale of Glamorgan is exceptionally valuable for house building.

[176] **Mr Price:** My recollection, and this is only a recollection—I can check and put it in a note for you—was that the original valuation was done on the basis of airport use, because that’s what the publicly available sources of information would include. Through the process, we also looked at what the value might be if it all went wrong, basically. What if it all went wrong and what you had to do was try and develop houses on it? Interestingly, the valuation wasn’t much different from the asset valuation.

[177] **Mike Hedges:** You surprise me. Rhoose is a very sought-after area, like Lisvane. I would guess that the ability to raise £1 million an acre on building land there would not be difficult. So, you’re telling me, on an initial thing, that you’ve only got 35 acres there on which houses could be built.

10:00

[178] **Mr Price:** I think that’s a very good challenge. That is the challenge I gave the valuers who looked at it for us and they came back saying, ‘You’ve got to work out what you might get planning on. And you’ve also got to take account of the cost of roads, the cost of infrastructure and the cost of cleaning up contamination, which is undoubtedly there, given the fact that the airport’s been there since 1945.’ But, this was a backstop; this wasn’t what we bought the airport for and we’ve got no intention of doing that, so—

[179] **Mike Hedges:** But it does give you, if anything else goes wrong: ‘This is what we’ve got.’

[180] **Mr Price:** Yes.

[181] **Mike Hedges:** You’re talking about road infrastructure—. You’ve got the main road infrastructure there; you’ve got the place where the planes land—the landing strip’s there—which could be turned into a road quite easily. You know that you could not fail to get planning permission on the sites that are currently built on. Where there are buildings, no local authority could ever defend ‘You can’t build on this’, when there’s a building already there.

[182] **Darren Millar:** In fairness, Mr Price has made it clear that it’s not the

Welsh Government's intention to develop. I appreciate the point that you're making, Mike, but I think we need to move on.

[183] **Mike Hedges:** You're stopping me, are you?

[184] **Darren Millar:** No, I'm just saying—

[185] **Mike Hedges:** Can I just finish the point, then?

[186] **Darren Millar:** Please be quick, then.

[187] **Mike Hedges:** Are the calculations on residual land value available?

[188] **Mr Price:** I would need to check. I know they were done.

[189] **Mike Hedges:** Because, without being unkind, the Welsh Government has not got a good record on valuing things.

[190] **Mr Price:** I could see that coming, yes. [*Laughter.*]

[191] **Darren Millar:** I'm glad I let you finish now, Mike. Julie.

[192] **Julie Morgan:** You mentioned earlier that there were three potential investors, who were interested, and they were the same ones who were interested early on. I'm aware that you may not be able to say much about this, but are you able to say what sort of model you'd be discussing with them?

[193] **Mr Price:** We've discussed a whole variety of different models with different people and, in fact, different models with the same people as well. So, some people have been interested in a simple concession with a profit share, but also putting a bit of an equity stake in there and you can have a hybrid with that. Some people have been interested in a simple equity play and some people have been interested in buying the whole thing.

[194] **Julie Morgan:** That's what I was wondering.

[195] **Mr Price:** Yes, but we're in no rush to do something—that's not in the strategic interest of Wales, having purchased the airport. The numbers seem to be going in the right direction at the minute; in fact, very well in the right direction. We've got a new management team in place, including a very keen

and energetic chair and he's got significant ambitions for the airport and I think that our view at the minute is that we need to give him time to try and deliver on that rather than assuming that we immediately need the money and the help of someone else.

[196] That's not disregarding the private sector; we think the private sector is very important, and I think Roger was here talking about the potential of maybe doing something different in three years' time. I would say that that's his personal opinion and that is an opinion he's entirely entitled to have, and he's probably better placed to have an opinion on it than I am. What will then need to be applied to that, though, is a kind of Welsh Government policy take, namely what's the best value for the taxpayer?

[197] **Julie Morgan:** So, does the Welsh Government have any forward plan at the moment?

[198] **Mr Price:** In terms of whether we want to divest or not?

[199] **Julie Morgan:** Yes.

[200] **Mr Price:** No. The publicly stated position, I believe, of the First Minister, which is the policy position that we're adopting, is that we'd be very interested in private sector investment in the airport, but we don't want to get into a position where Welsh Government would not have a significant stake in the airport, as in we don't want to have to buy it again.

[201] **Julie Morgan:** Right. What are the disadvantages of it being publicly owned?

[202] **Mr Price:** I think that critics might be better placed to answer that than I am. I guess the biggest issue currently is that any borrowing that it takes scores against the Welsh Government borrowing. That isn't an explicit disadvantage of being publicly owned; that's a potential disadvantage of being publicly owned in the current devolution settlement, where we've got limited borrowing capability. So, the Manchester Airports Group plc, for example, is, partly and quite significantly, public-owned, but because of the structure of that public ownership, they don't have that same constraint. The board of the airport believe—and I think it's fair to say that Welsh Government accountants don't currently share that belief—that there's a way of structuring the airport in a way that may get some of their borrowings off the Welsh Government balance sheets. So, I think that this is an evolving

picture.

[203] **Julie Morgan:** So, they think that can be overcome—the board.

[204] **Mr Price:** Yes. Whether it can is another matter, but they're looking at ways in which they think that that might be able to be structured and, of course, if the deal with the Treasury and the Welsh Government changes, which is evolving anyway, that would also change this.

[205] **Julie Morgan:** So, what would you estimate would be the current value of the airport?

[206] **Mr Price:** Okay, so I think—. It's a fair question, but it would probably be unfair for me to try and answer, really, in the sense of we don't know—. Well, it's incorrect to say that we don't know because we did a valuation as part of the accounts of Holdco last year and the valuation was, I think, at the high end of £55 million—it was £55-point-something million. So, we did have a valuation, but I would go back to what Roger would say: the airport's worth what someone's prepared to pay for it at any point in time.

[207] In terms of maximising the value of the asset that we have, I don't think now would be the high point in selling it because we're clearly on an upward trajectory. The Flybe deal and others need to mature. The profitable part of that deal comes in a couple of years' time and that is when EBITDA—earnings before interest, taxes, depreciation, and amortisation—and other things will start to grow significantly and the airport would look more attractive.

[208] **Julie Morgan:** So, it's a long-term strategy.

[209] **Mr Price:** Yes, or medium-term, certainly, yes.

[210] **Darren Millar:** Can I just ask about that before I bring in Jenny Rathbone? You said you had another valuation done last year on the airport.

[211] **Mr Price:** Yes.

[212] **Darren Millar:** When was that done?

[213] **Mr Price:** That was done at the closing of accounts for Holdco, so that would have been—well, I say last year; yes, it would have been last year: April

or May time last year, I believe.

[214] **Darren Millar:** And the valuation was about £55-ish million.

[215] **Mr Price:** Yes, £55-point-something million.

[216] **Darren Millar:** Even though things had moved on—

[217] **Mr Price:** It's published in the accounts.

[218] **Darren Millar:** But, obviously, there had been some passenger growth by then, so that implies that it was worth less than £55 million at point of purchase, doesn't it?

[219] **Mr Price:** I don't think it does because—

[220] **Darren Millar:** What was the basis of the valuation that was recently done?

[221] **Mr Price:** I'm not qualified to get into that. We can provide a note on it.

[222] **Darren Millar:** Which method was used to value?

[223] **Mr Price:** I think probably discounted cash flow again.

[224] **Darren Millar:** Okay, so the same methodology, better prospects, potentially, for growth than—

[225] **Mr Price:** No, I don't think better prospects because when we bought the airport, there was an assumed business case of growth. Actually, as I think the auditor general himself has pointed out, performance is slightly behind profile, albeit very good—we are about six months behind where we would want to be. So—

[226] **Darren Millar:** Three years behind I think the auditor general said.

[227] **Mr Price:** That's a fair point. Roger was trying to convince me the other day that he's got figures to suggest it was six months behind profile, but we are slightly behind profile, but when you run the figures through, I think the profile kicks higher up on the latest estimates and you end up with roughly the same figure. But I think it is—. When you look at the way it's done, it's

much more of an art than it is a science. We're using—. Well, we don't do the valuation, but equations are used: massive spreadsheets are created, but they're based upon assumptions about growth and weighted cost of capital and various things and a very slight change in the weighted cost of capital has a huge impact on the value of the airport. For example, the weighted cost of capital of 14 per cent at purchase price would see a value of about £40 million; at 12 per cent at about £56 million; and at 10 per cent, about 80 million.

[228] **Darren Millar:** And just in terms of those assumptions that you made, and going back to the valuations that were done immediately prior to purchase, there were a couple of key assumptions that were made, weren't there, about the continuity of the Welsh Government's marketing income, which clearly then changed in terms of the more recent decisions on marketing? That would have had quite a significant impact on the EBITDA—

[229] **Mr Price:** Would and does.

[230] **Darren Millar:** —from a valuation point of view. So, why would you have included that, if you knew it was going to reduce?

[231] **Mr Price:** Okay. So, at the time I don't think we did know it was going to reduce and I'm not sure that that's the entire picture of it either. Airports around the world, and many other assets—increasingly roads as well, if you drive into London—are selling advertising space, and advertising space, to a certain extent, is a commodity product; it's got a wrap value placed upon it and it's quite easy to value that space.

[232] Welsh Government, before we bought the airport, decided that we wanted to use the opportunity of people coming into Wales to advertise Wales as both a tourist destination and a business destination. That's not unusual—regional development agencies and Governments all around the world do that. Before the purchase, we had agreed a rate; since the purchase, we've still got the same rate, roughly speaking, so we're not paying less pro rata, but we're buying less than we did before. Why did we include the marketing income? Because, quite rightly, Abertis was saying, 'It's not just Welsh Government that can buy the advertising—anyone can buy the advertising.' Our view currently is that the airport will be able to sell advertising to other people, other than Welsh Government.

[233] Is it odd that Welsh Government would have reduced its advertising

spend on the airport since it purchased the airport? At one level, it is, and I think it ought to give the Public Accounts Committee satisfaction that the Welsh Government isn't 'up to anything' here, because what you would expect was for us to have maxed out the marketing spend after we bought it and maxed out grants after we bought it, but we've not given the airport one grant since we bought it. Before we bought it, there were significant grants that went in and there was an offer of £5 million against a £25 million investment. Interestingly, I went back and looked at this, albeit I can't quite pull the records, but when Bmibaby first came in, that was subject to a Welsh Government support package, which was grant as well.

[234] So, since we've owned the airport, it's been fully commercial. That's not to say that we shouldn't grant anything as we would with any other business, but I think we've acted in a way that sort of demonstrates, actually, that we can't be accused of trying to get money into the airport.

[235] **Darren Millar:** Just one final question on this whole valuation issue: the public valuation, which took into account these wider economic benefits that Jocelyn Davies referred to earlier on and the strategic importance of the airport, was commissioned quite late on, wasn't it? It was just literally a few weeks before the actual acquisition of the airport. Why was that left until so late, given that that was the whole business case, effectively, that was being made for the purchase of the airport?

[236] **Mr Price:** Okay. So, we had some indicative figures before that in-house. We had other reports. Mark Barry did some earlier.

[237] **Darren Millar:** Sorry, Mark Barry. Who—?

[238] **Mr Price:** M&G Barry Consulting. It's referenced in the work. I think the honest answer of that is: I was signing this off and I remember, again, quite a heated conversation—and I don't think there's anything wrong with having a heated conversation—with the team who was doing it, who were absolutely convinced that what they were doing was okay and was supported by evidence, and I think it was. But my position was, 'I don't think your evidence is good enough; you're not completely convincing me—try better.'

[239] **Darren Millar:** So, it was your final testing of the valuation.

[240] **Mr Price:** Yes, and in addition—and I think this, again, was a good thing to have done—the Permanent Secretary had a challenge group

established that met at least twice—it might have met three times; I tried to pull the papers this morning, but I couldn't get on to the IT—. So, not only did I challenge the team, the Permanent Secretary then challenged me and reviewed all of these papers.

[241] **Darren Millar:** Okay, so it was that final test. Is it on this, Jocelyn?

10:15

[242] **Jocelyn Davies:** Just on the business case. Obviously, we haven't seen the business case. We've had interpretations of it. It just seemed to me that, from what you've said today, that's where perhaps the Welsh Government was lacking in terms of articulating properly, and having a proper paper trail, in terms of the argument for, in the business case. Surely, the strategic importance is where you start, not where you finish. That's like: 'Oh well, is there anything else that would be an advantage? I know, we'll add in strategic importance.' Surely, that's where you start.

[243] **Mr Price:** I think that's a very fair point you're making. The strategic rationale was always public value. That was the reason we were doing it. We are not in this as a commercial entity. Clearly, we want to protect the airport for the benefit of Wales. So, if you like, where we finished was where we started. The auditor general quite rightly said that the business case didn't fully set that out, but other documentation did. Ministers, the permanent secretary, I and the senior team were clearly aware all the way through of why we were doing it, but I would accept the criticism that that wasn't articulated as well as it should have been in the business case. But, I think, importantly, for the team that was doing this, to act as though they were doing it on a commercial basis was the right thing to do anyway, (a) to drive the best possible price; and (b) to ensure that we were compliant with state aid. But I take the point, and we've agreed with the auditor general that the initial business case, in terms of the public rationale for purchasing the airport, could have been clearer.

[244] **Darren Millar:** Jenny Rathbone.

[245] **Jenny Rathbone:** I wanted to look at the connectivity of the airport and the importance of that for driving up numbers and making it a hub of economic activity. We've owned the airport since 2013, and there seems to have been not much progress on making the essential air-rail links that, if you want international passengers, are essential. I wonder why Rhoose

Cardiff International Airport station is such a modest affair still. What is the Government doing on providing the light rail that most successful airports have?

[246] **James Price:** Okay. So, again, that is a really fair and challenging question. But, if I might try and turn it around: yes, you would imagine that we would want to do that; and, from a strategic perspective, yes we would. But what we are not in the business of doing is spending other budgets within the Welsh Government to try and, in any way, benefit the airport. So, rail interventions, including light rail, have to stack up on their own basis. So, we wouldn't make an investment simply because we own the airport and we want the airport to benefit.

[247] **Jenny Rathbone:** No, I quite understand that you would want it to—

[248] **James Price:** And the cost-benefit ratios for many of the schemes that we are talking about at this stage don't look as good as they should do, particularly with—if you are talking about rail—the costs that we currently have with the Network Rail settlement that we have. So, for example, moving the line—. Again, I was trying to get hold of the figures. I couldn't get the exact figures, but we are well north of £100 million to do anything on moving the line.

[249] **Jenny Rathbone:** Closer to the current terminal?

[250] **James Price:** Yes. So, in terms of any reasonable cost-benefit, I think that's out. If we were doing rail in a different way, you know, looking forward to the metro, when we have got much lower unit costs, then that might well change that significantly. If the passenger numbers at the airport were significantly higher, I think that would also change that. In terms of how people get from Rhoose to the airport, I think that has to be looked at a bit smarter. I know there's a comment in the report saying we should evaluate the shuttle service. I think I'd go a bit wider than talk about evaluating the shuttle service. We need to work out the most effective way of getting people from the rail service into the airport. There is no point having an airport rail station—which is why it was built—that you can't get to the airport from. But, is the shuttle the most effective way? Might a light rail link be more effective? Might a bus rapid transit fully segregated route be more effective? All of those things will be—

[251] **Jenny Rathbone:** Yes, but you've owned it since 2013 and yet you

haven't made any progress on this.

[252] **Mr Price:** Well, on the rail side, that is because we're still trying to get powers over the next rail franchise. There are very limited things that we can do anyway, currently. We want more powers over rail infrastructure and anything that we did there would be part of the metro project in terms of upgrading the Valleys and associated lines. So, I think there's a very good reason for that, but I think it's a fair challenge and we need to think quite laterally in terms of what we do there.

[253] **Jenny Rathbone:** Okay. So, £100 million to move the line. What about moving the terminal?

[254] **Mr Price:** We did look at that as well when we first purchased and, on the face of it—you know, what do I know about these things? Nothing, really. But, on the face of it, building a terminal building would not cost very much at all. You could probably build a terminal building for under £20 million quite easily, I would say. I'm sure there are people watching this going, 'No, we can't do that', but I reckon you could—just the kind of crinkly shed, modern, nice-looking terminal building. The problem is, and this is where the costs came in, you have to move the fuel farms, you have to move the—

[255] **Jenny Rathbone:** Why do you have to move the fuel farms, because surely the planes need to fuel up somewhere away from the building?

[256] **Mr Price:** Well, this is what we were told, when we looked at it, by the experts. You've got to move the apron, certainly—well, you don't move the apron; you build a new apron—

[257] **Darren Millar:** The apron is? Just to help people.

[258] **Mr Price:** Where the planes park up on outside. That's very expensive. There are some safety aspects and there are also issues with locating it maybe too close to housing. So, you add all of that up and you're talking about north of £50 million again. So, our conclusion was that that wasn't a value-for-money thing to be doing, and it would actually be a matter for the airport board rather than a matter for us anyway. But this was one of the things, when we first purchased it, that we threw at the airport board and said, 'Would you have a look at this for us?'

[259] **Jenny Rathbone:** Okay. I thank you for those figures. Just in terms of

the shuttle bus—the once-an-hour shuttle bus that goes from the station to the terminal building—you have all these relationships with the Vale of Glamorgan and their local bus services. Why has it not been possible to incorporate the station into the normal bus routes?

[260] **Mr Price:** I think you're seeing—. This is not—. Can you explain that a bit more, just in terms of are you talking about—

[261] **Jenny Rathbone:** Well, at the moment, you've got a dedicated shuttle bus service. I'm not talking about the express bus going from Cardiff—that's a separate thing. Just getting people from the railway station is obviously costing £4.50 per journey, the Wales Audit Office report says. That's quite a lot. But, you know, there are local people who need to go around the area. Why is not possible for you to incorporate that?

[262] **Mr Price:** So, we did look at that. At the time, it wasn't possible. I think, in terms of thinking laterally, we ought to look at that again and see if it is possible. There would be ups and downsides to that. It might bring the costs down, but it might mean you've got a much lower quality service and its reliability deteriorates somewhat. But I do think we probably need to look at it. And this isn't by way of sort of pushing this on to someone else, but I know Stuart Cole's coming in later, and I think he would be better placed, in a way, than I am, to comment on the best way of doing that.

[263] **Jenny Rathbone:** Okay. And why is it not feasible for the express bus service to make its final stop at the station to pick up passengers there?

[264] **Mr Price:** Again, we did look at that, and it was affecting the times that we wanted to run it on. But, again, it's something, I'm sure, that could be looked at. Stuart did a review of the express bus service for us just over a year ago now, and recommended some changes, and I'm sure he'd be able to comment on that. If he's listening, he can probably prepare for that now.

[265] **Jenny Rathbone:** I'm sure he will.

[266] **Darren Millar:** He's in the gallery—

[267] **Mr Price:** Sorry. [*Laughter.*]

[268] **Darren Millar:** —paying close attention to every word.

[269] **Jenny Rathbone:** Just looking at the wider potential benefits of this large estate, which you described earlier, why has it not been possible to have some sort of economic benefits plan? I'm interested in other things that you might want to put that are compatible with an airport—for example, solar arrays or things like that. Why is—? What has been done so far on that sort of thing?

[270] **Mr Price:** Okay. So, in terms of the pure airport land, the airport is clearly incentivised to do that activity themselves, because, really, the three things we have been asking the airport to do are to increase the number of passengers, increase the number of routes, and increase profitability. So, anything that the airport could do in terms of raising additional revenue, they would want to do and they would be exploring. I think now that we've got a kind of settled-down management structure, and we've gone through the pains of purchasing the airport—there was a whole number of different things that needed to be settled afterwards, like some issues around the pension fund that need to be sorted out; all of that has been sorted, we can now go forward, and I believe that the airport board has got a plan for some solar arrays, and, equally, there is the potential for doing more with wind generation as a result of some changes in technology that mean they won't interfere so much with aircraft radar.

[271] In terms of taking that wider again—why don't we have a proper benefits plan for the purchase of the airport—which the auditor general raised, that's something that we're working on more widely. I think we've got all the elements; they're just not in one place. So, the enterprise zone has got a key plan, there's a key plan for St Athan—what we now need to do is to pull it all together into one.

[272] **Jenny Rathbone:** Okay. But, just to challenge you, I would've thought that things like solar arrays, those are quick wins—it's not complicated; it's just a piece of land and shove it on there. What's the problem?

[273] **Mr Price:** In theory, I think that's correct, and, in reality, those are the type of questions that we ask the airport board, and I am confident that they will deliver at pace anything that makes sense and anything that they can do.

[274] **Jenny Rathbone:** Okay. Thank you.

[275] **Darren Millar:** Just two more questions before we finish, if that's okay. One of the things that was in the original business plan was the possibility of

doing something jointly with St Athan in order to reduce the operational costs—to share the operational costs, effectively. There's been very limited progress with that. What's the Welsh Government doing in order to make some progress on it and to move that forward?

[276] **Mr Price:** Okay. So, we've been quite frustrated, actually, in terms of the amount of progress we've been able to make, and there were discussions about synergies—I think that's what we described them as—and those would be things like sharing key aspects of fire service, bird-scaring, security, grass-cutting, and air traffic control between the two. Air traffic control: there's been progress made, so some services are shared across the two there. But, with the other aspects, mainly because it's been quite difficult to move the military as quickly we thought it would be, we've not made the progress that we want. So, the way that the military structure is set up, it is the base commander at St Athan who has to sign off what happens, basically, and there's a kind of safety card that they can play if they're not happy with anything. We're trying to move it towards a CAA—Civil Aviation Authority—rather a military aviation method of operating, and we've struggled to get people to move as quickly as we want to on that.

[277] As I said, we've made progress on air traffic control, and the plans that we've got see significant progress being made next year, which is down to contract breaks and things like that, when we start to make real progress.

[278] **Darren Millar:** So, you still think you're going to realise these benefits that were outlined in the original business plan?

[279] **Mr Price:** Yes, and there may also be other synergies with other things that Welsh Government operates that we can pull into the mix. But, at all times, the test is going to be: is it value for money? What we're not attempting to do is cross-subsidise the airport. That's a key point that I want to make: had we wanted to, we could have had Cardiff Airport in a much stronger financial position than it currently is, but that would've been as a result of cross-subsidising, and that, explicitly, we haven't done. We're expecting Cardiff Airport to operate on a commercial basis. So, any agreements that Cardiff Airport enters into with any other parts of Welsh Government will be strictly on a commercial basis.

[280] **Darren Millar:** And, just in terms of the governance arrangements—we haven't touched on this a great deal—we heard lots earlier this week on the existing governance arrangements and the reporting back to Welsh

Government officials by those who sit on the Holdco board. So, can you describe for us how regularly you receive updates from Holdco, and what information comes back in terms of the activities of the Cardiff Airport board as well to you?

10:30

[281] **Mr Price:** Okay, so, yes—. I think we need to evolve this further. So, Simon Jones, who chairs the Holdco board, reports to me anyway as part of his position within the Welsh Government. Simon and I meet regularly, as you might expect, on a whole variety of topics, one of which being the airport. The performance of the airport is reported monthly to my management team meetings where we're looking at basically whether they are on track or whether they are not on track against the business plan. What I think we might want to do to evolve that further is for Simon, as Holdco, to produce a formal report—not a big-deal administration piece, but a formal report to me in terms of setting out whether he believes they're on track and whether there are any issues and exceptions. That is being done, and it is formal because it is written down, but it's not formalised on an annual basis, and I think Simon and I have concluded, partly as a result of this PAC inquiry, actually, that that would be a sensible thing to do.

[282] **Darren Millar:** Okay. So, that's effectively what Simon told us, I think, earlier this week, and he clearly has an observer role as well on the Cardiff international airport. That observer role seems to be different than other observer roles, which have been described to this committee in recent inquiries. He clearly participates in discussion, but doesn't vote on matters. Is that consistent now with all observers that attend as observers—do they participate in those discussions, or do they just sit and listen?

[283] **Mr Price:** So, the guidance from the Welsh Government, in terms of observers, states that—. Well, the individual has to have guidance from the Welsh Government, and then the company needs to be very clear what the individual is there for, and, furthermore, that they're representing the interest, if you like, of the shareholder. Beyond that the guidance is a bit flexible, and I think that's right. So, you've got very different reasons why people are sat on things. The rationale for Simon being there is clearly set out in the management arrangement. I have been present at one board meeting when Simon has been there, and I wouldn't characterise his attendance as contributing massively to discussions at all, actually. I think he is, really, from what I could see, much more in an observing position but

contributing if there's a question around whether they are off performance in terms of where the Welsh Government would want them.

[284] **Darren Millar:** So, it's more of a challenging sort of—

[285] **Mr Price:** Yes.

[286] **Darren Millar:** Okay. Thank you. Are there any other questions from Members? That brings us to the end of this session. Thank you very much, Mr Price, for your attendance today. You'll receive a note from the clerks, just in terms of additional information.

[287] **Mr Price:** I offered a few things, so, yes.

[288] **Darren Millar:** We'd appreciate it if you could send them on.

[289] We're going to take a five-minute comfort break before we bring in our next witnesses.

*Gohiriwyd y cyfarfod rhwng 10:33 a 10:42.
The meeting adjourned between 10:33 and 10:42.*

Maes Awyr Caerdydd: Sesiwn Dystiolaeth 4 Cardiff Airport: Evidence Session 4

[290] **Darren Millar:** We're now back in session and we're moving on to item 4 on our agenda, which is continuing with our inquiry into the acquisition and performance of Cardiff Airport—evidence session 4. I'm very pleased to be able to welcome our witnesses, Professor Stuart Cole, emeritus professor of transport economics and policy at the University of South Wales. Welcome to you—

[291] **Professor Cole:** Thank you, Cadeirydd.

[292] **Darren Millar:** I'm glad you've made it down from the public gallery up the top there.

[293] **Professor Cole:** Safely.

[294] **Darren Millar:** And Chris Cain, director and head of research at Northpoint Aviation. Welcome to you, Chris. We really appreciate the papers

that you've submitted to the committee, which Members have had the opportunity to take a read of.

[295] You've no doubt been paying attention to some of the evidence that has been coming into the committee already, and you've obviously read the Wales Audit Office report. One of the things that witnesses have pointed us to is obviously the decline in the performance of Cardiff Airport between 2007 and 2012, and how that compared with other airports of a similar size elsewhere in the UK. What was your view on what was going on in Cardiff versus elsewhere, and the prospects that it had should there have been no Government intervention? Professor Cole, if we start with you, and then come to you, Chris.

[296] **Professor Cole:** Thank you, Chair. Clearly there was—. Cardiff was a very expansive airport for a long time. It had some very clear objectives for itself, and also the airlines that were there. We had Cambrian Airways many years ago, which had a whole range of destinations. We then had a company that became Eastern Airways, and Manx Airlines, who were also very successful. They were taken over and left Cardiff. Cardiff was therefore left for a while with just charter operations. People like Bmibaby came and went, and that, of course, didn't help the fortunes of the airport in terms of numbers.

[297] So, the pattern has been a rise-and-fall pattern over the years, and back in 2012 the company wasn't—well, it had gone down again to just over 1 million passengers, and is now seemingly creeping up, with a couple of little hitches when Flybe pulled out, but Vueling and Flybe have come back.

10:45

[298] **Darren Millar:** But in terms of that performance versus other airports, was Cardiff performing better, about average, sort of middle of the pack? Obviously, there is another airport that is relatively strong just down the road in Bristol. I mean, should we have been really concerned about its fortunes? It's been there a long time, operating for a long time, as you just indicated. Was it really on the brink of closure, as some have suggested?

[299] **Professor Cole:** I don't know that, because I don't know enough about the inside positions of either Abertis or the owners at the time, or, indeed, TBI prior to them, and the Welsh Government. But as Mr Hedges raised earlier in speaking to James Price, the way in which the airport had competed with

places like Bristol—Bristol and Cardiff were pretty much the same in terms of numbers, and then Bristol basically got EasyJet and Ryanair. And once they'd got EasyJet, they weren't going to lose EasyJet. So, the opportunity for Cardiff to get even a taste of EasyJet—there's a small presence for Ryanair—but to get EasyJet to move, Cardiff would have to offer a very significant discount in terms of a whole series of charges, or free operations, to compete with Bristol. And Bristol, therefore, has risen as a result of the scheduled operation, whereas Cardiff is now very much a charter operation with a growing business operation, which I'm happy to talk about later when we come to talk about the landside links.

[300] **Darren Millar:** Thank you. Chris Cain.

[301] **Mr Cain:** I think what the industry saw over that period, where clearly we also went into a big economic recession—there was a major downturn, and that affected different types of airports on a differential basis. So, even through the worst part of that decline in economic activity, places like Heathrow and Gatwick were still basically at a steady state or growing very, very marginally. What you would call the 'larger regional airports' declined, but maybe by 10, 15 per cent at most, and the greatest volatility was seen in airports under 3 million, and some of those performed very, very badly. I mean, for example, Durham Tees Valley Airport was at 900,000, and it's now down at 200,000, and Cornwall Airport Newquay declined significantly, from over 350,000 down to about 175,000.

[302] I think Cardiff was probably in the range of the, sort of, nought to 3 million airports—it was slightly below the middle point—but it's very much dependent on carrier decisions. And, as Professor Cole has said, EasyJet's presence at Bristol has made it very difficult to attract a stable long-term low-cost carrier that can develop a network based on the south Wales traffic. And finding the right carrier, which initially I think they thought they'd got with Bmibaby—. But then there's been consolidation in the industry, so there's really only now three major low-cost carriers based in the UK. You have a series of small regional carriers and you have the charter carriers, because network carriers are unlikely—. Certainly, British Airways wouldn't come out of a regional airport; what you've got is KLM coming in from their hub, so you have hub network carriers.

[303] I think the challenge for the airport is to make the investment necessary to attract one of those big low-cost carriers to develop a persistent base. One of the challenges is that you've seen quite a lot of churn, where

Ryanair have closed bases, for example; they've opened them and closed them. So, it's not a straightforward thing. They basically will test the market for two to three years and, if they can't get to a certain number of aircraft, they'll close the base. And if there are some residual routes that work well, they'll fly them from other bases inbound.

[304] I think Abertis decided they weren't going to invest any more money in this airport. They bought TBI as a block. They were really interested in Luton and Belfast. Nobody knows, or nobody that I'm aware of knows exactly what was the value on the books, but it was a lot more than the Welsh Government had paid when they bought the asset. And in a very difficult economic climate where they were probably having other issues as a group, not just as Aerolíneas, but also as a construction group, they will have wanted to focus any investment that they had on the most profitable parts of the business. As the traffic declined, as Bristol created a very strong competition, it struck me that they—I mean, it was everybody in the industry—took the view that they were basically spending the minimum to keep the place going. The state of the airport when I came and looked at it with some investors three years ago was very run down. It was not what you would have expected of a national gateway airport.

[305] **Darren Millar:** Is it not surprising then that they didn't grasp every opportunity for financial support and investment from other sources that was available?

[306] **Mr Cain:** Not if it was match funded because that would have required them to—. They didn't want to spend any capital on the airport. They wanted to take any profit that they could get without making any investment other than—. I'm sure that they will have invested for safety and due diligence maintenance purposes. But, in terms of investment to develop the product and to compete against what at the time—when Bristol was a 3 million to 4 million airport—was quite a nice, new terminal offering quite a nice ambience for passengers, they weren't willing to do that because it would have required an investment of £20 million to really turn the terminal into something modern and efficient.

[307] What you've got to bear in mind is that the market from when that terminal was built has changed completely. We now have low-cost carriers that don't want gates. They want minimum spec, gates and stands. But the business model for airports of this size is that you get passengers processed and checked through as fast as possible—no landside dwelling. You want

them airside, spending money. A lot of the revenue that the airport gets is being generated by car parking and airside revenue—airside shopping spend—and a range of other things. It's not really kitted up to do that properly at the moment. The layout upstairs is not fantastic. There have been some improvements made. But when I first brought an investor down, they took one look at it and said, 'Why are you bringing us to this?'

[308] **Darren Millar:** So, this was a potential purchaser of the airport.

[309] **Mr Cain:** It was a potential purchaser.

[310] **Darren Millar:** So, they were obviously interested in selling the airport at that time, were they?

[311] **Mr Cain:** Yes. I kind of put my professional reputation on the line saying, 'This is an opportunity and nobody realises the scale of the opportunity'. I believe that, and I continue to believe that there is a real opportunity. But it does require an investment, and the price that Abertis were willing to sell for was simply not a market price.

[312] **Darren Millar:** So, they were playing bluff with the Welsh Government—

[313] **Mr Cain:** Yes, and I think the report by the audit commission tells a very interesting story, which rings a lot of bells with me in terms of how the whole thing played out over that two-year period.

[314] **Darren Millar:** You will have read in the report about the strategy for supporting the airport that the Welsh Government had, prior to its decision to make some offers to purchase the airport. There was a route development fund that was set aside, although it wasn't taken up by Abertis; there was some cash, which took a long time to get an EU sign-off, that was available for investment against some match funding, which I think is the point that you're making, Mr Cain—they weren't prepared to put their hands in their own pocket and put some of their own cash on the table—and then there was this taskforce, wasn't there, that was established.

[315] **Mr Cain:** There was, yes.

[316] **Darren Millar:** You've seen taskforces set up and operate in Wales before, Professor Cole. Do you think that the way that this taskforce was established was the right way? Was it an appropriate move? Were the other

steps appropriate in terms of the sort of support you would expect to see being made available to what is a pretty important airport, from a strategic point of view, for Wales?

[317] **Professor Cole:** I can't tell you about this particular taskforce because I wasn't involved in it. But a taskforce taking over any kind of business, whether it's in the private sector as the purchaser or in the public sector as the purchaser, has to have those necessary skills that can identify the benefits and the disbenefits of the operation and whether the cost is a reasonable cost. So, there are financial people to be involved, operational people to be involved. Certainly in the transport business any takeover would involve that kind of team to perform the due diligence, and that's really what the taskforce would have been doing.

[318] **Darren Millar:** Because this taskforce was one that was set up simply to support the airport, if you like, and its development, not necessarily to acquire the airport at that time. That came a little bit later, didn't it?

[319] **Professor Cole:** I see what you mean. Yes. In order to develop any business—again, we're back to the same skills—there need to be skills in that taskforce, which takes a business and says, 'These are the things that are wrong with it. These are the things that are good about it. Now, how do we eliminate as many of the bad things as we can and push the performance of the business forward? What's the market like? Is there a market for what we're offering, or is our product out of date or our service out of date, or are there aspects of our service that people will take up on?'

[320] If you ask me questions about TrawsCymru later, that was the same kind of business. It had a team. The Government decided to go ahead with it—generally in Wales not just the airport service—and to make that work we had to create a brand; we had to create a quality of service that was guaranteed. That's what the customer wanted from the market research. So, once you've done the market research, you know what the customer wants. Is it something that can be done, either profitably entirely or with subsidy, if that's what the particular service requires, and what level of subsidy? So, you have, really, to take a business and make sure that that business has got the elements in it that will make it succeed, and the airport will have needed the same kind of taskforce.

[321] **Darren Millar:** Are there any other things that you think the Welsh Government could have done prior to a decision to purchase that it didn't? I

mean, they had the route development fund, they had this potential capital investment or contribution towards capital investment in the estate, they then set up the taskforce: is there anything else you think would have been appropriate?

[322] **Professor Cole:** Well, those would have been the headline elements. I don't know how much detail they went into in terms of how the route development fund would work—sorry, how effective it would be; we know what the mechanics were, but how effective it would be—which markets were being pointed at, which markets were being specifically aimed at, were they the right markets. Because I wasn't involved, I can't actually tell you what that taskforce did in detail, but that's what any other business that I've been involved in developing, whether for private sector or public sector—. I mentioned TrawsCymru; that's exactly what you have to do before you set out—before a Government sets out, or a private takeover company sets out to purchase an operation or deciding to try and invest in that operation to develop it.

[323] **Darren Millar:** Okay. Chris Cain, do you think there was anything else that could have been done? Then, if you can just tell us about these other expressions of interest in the airport.

[324] **Mr Cain:** Yes, I think the route development fund was an interesting initiative. It just came at probably the wrong time, when the market was extremely flat. Route development funds, and the one in Scotland worked extremely effectively, work very well when there is—. There has to be an underlying market interest. You can't create interest in flying routes where big airlines aren't willing to fly them, because the route development fund is about sharing elements of risk that are marginal but important for the bottom line of the airline, but, if the underlying case is poor in terms of demand, it doesn't matter how much money you throw at it, it won't work. So, I think there was a risk aversion period in the late 2000s where it was going to be very difficult to get a return on that investment. Probably, in the current market conditions, you'd get a much better response, and, by the looks of things from Flybe, that kind of thing has happened. You've got to have willing partners to work on these kinds of taskforces. You can identify projects and build business cases if there's a willing partner. If there isn't a willing partner, I don't think there's a lot a Government can do, unless it owns an asset, to make people invest.

11:00

[325] Obviously, not being party to them, it's very difficult to say whether all the options were looked at, but I know that, certainly, the Welsh Government appears to have entered into that in the right spirit to actually try and find opportunities in a very difficult market. I think probably it was a case of timing and that it might work better now.

[326] I think what practically happened in terms of when Abertis—. There are certain ways that airport investors signal to the market, without the rest of world realising, that there are opportunities, and when an airport is underperforming, that's a good signal that they might be looking to sell. There was interest, I'm aware, from a number of parties that looked at it, and my intelligence is that they all came to the same kind of numbers that have been quoted in the report. So, that all seems to me perfectly coherent. The issue was that that wasn't a price that Abertis were willing to sell it at. Without being privy to how they were valuing the airport on the books, as part of the TBI deal, I suspect they put a value to it that was very high, probably £80 million to £100 million. They may have said £200 million—. I mean, they were buying Luton, which is worth £300 million, Belfast, which was bought originally for over £100 million, and they paid £570 million, or something like that, for the group. There was a big chunk—. It was a lot more. To be offered, at a push, £35 million for the asset would crystallise a huge loss on their books, and I think at that stage—we don't know what the internal politics of Abertis is—that might have signalled to the market, for all we know, that there's a real problem with this company more generally.

[327] So, it was a case of—there was a negotiation to achieve a price between a party that was ultimately willing to sell that came to the right kind of number that allowed them to dispose and to cover any losses off, to explain that disposal in positive terms to their investors, and the Welsh Government got itself an asset that is very important for the economy of Wales and which, with a very long-term perspective—and you have to keep in mind the difference between private investors and public sector investors. Private investors take a much shorter timescale; they look at shorter investment horizons. So, between 2003 and 2007, there was a real boom period for infrastructure investment funds and private companies buying smaller and medium-sized airports because they could see that these airports were growing fast and they could get a very quick return on their investment. As the market slowed in 2008–09, that mechanism, that business model, fell apart, and it was very difficult to find buyers for small airports between 2008–09 and 2013–14. It's still difficult to find buyers. The

investment market is now in the 3 million to 60 million range. They're really not interested in the smaller airports. But if you can take a longer horizon and make good strategic investments, then you can still get a very good return on your asset. But you look at it as a 10-year proposition or a 15-year proposition as opposed to a three- or five-year proposition. It becomes a completely different ball game. By making the investment that they have, that's what the Welsh Government have allowed themselves the chance to do.

[328] **Darren Millar:** It's quite clear from your evidence there that you think that this was a reasonable price to pay for the asset.

[329] **Mr Cain:** Yes. I think it was the market price, because that was the price that the seller was willing to sell at.

[330] **Darren Millar:** Do you think anybody else would have been interested in buying it for that sort of price?

[331] **Mr Cain:** No. I've looked at it with some North American investors, and looking at a particular type of model, which may be a long-term possibility, the facility needs to be put back on a profitable footing before it would work, with a non-profit-type model that works very well in certain countries. But they would have priced it as is in the report—the external, private sector investment—and they would have looked to the Welsh Government to invest £20 million alongside money they would have invested.

[332] **Darren Millar:** So, around the £35 million figure.

[333] **Mr Cain:** Yes, £35 million, plus they wanted £20 million of Welsh Government investment. So, when you put that together it's the same price.

[334] **Darren Millar:** Okay, and is that your view as well, Professor Cole?

[335] **Professor Cole:** From what I read at the time, these various figures were being put about of somewhere between £30 million and £60 million. And, from the information that's come out since the purchase was made, that seems to be, as Mr Cain was saying, the reasonable price for it that would have been acceptable to both sides. I can't remember who it was now who made the comment that an airport is only worth what a purchaser is prepared to pay for it, and, of course, what the seller is prepared to sell it for. Otherwise, they would have hung on and waited until another potential purchaser came along who might be prepared to offer the figure that Abertis

wanted.

[336] **Darren Millar:** And just before I bring Julie Morgan in, in terms of the ability to acquire in a different way through partnership, Mr Cain, you've indicated that other people were sniffing around the airport, as it were, really, and paying a bit of attention to it, realising that it was beginning to struggle and that there might be an opportunity to acquire. Would it have been easy for the Welsh Government to find a willing partner to do a deal with in order to acquire the airport? Because the suggestion we had just earlier on from James Price, who's in charge of the Welsh Government department dealing with this, is that there were people who were happy to have a discussion and were engaged in a discussion, but they didn't want to rush into a purchase—they wanted to take, you know, perhaps 12 months, two years, to make a longer term decision to undertake their due diligence. Is that a typical sort of turnaround time for a decision to purchase an airport? It seems a long time to me.

[337] **Mr Cain:** Airports tend to get sold in two ways; they're done through a public process, as you're seeing with London City Airport at the moment, where Global Infrastructure Partners have put it explicitly on the market and invited bids for it. The other type of purchase is off-market, where there is an approach. And I think what the Welsh Government did quite effectively was basically a soft marketing exercise to see if there was anybody out there that could buy it direct, and the basis of preference would have been that the Welsh Government didn't necessarily have to get involved in buying the asset itself.

[338] If the scenario arose that each purchaser would have needed significant grant support from the Welsh Government, I guess somebody takes the view that, rather than hand that to a private investor and have the same problem that we had before, maybe it's better just to acquire the asset ourselves.

[339] **Darren Millar:** But as a joint venture.

[340] **Mr Cain:** As a joint venture, that would complicate matters because you're going to have to agree the joint venture between yourselves.

[341] **Darren Millar:** So, that's why it would take a longer time.

[342] **Mr Cain:** It would take a longer time, and, to be fair to James, one of

the people who would have taken 12 months was the investor I brought. It's a complicated—. Any due diligence process for that kind of thing, you can rush it through in four months if you literally throw money at it, and, instead of the £1 million I noticed that was for due diligence, double, triple that, because the lawyers price it up. And there's a danger that you'll miss something. So, six months is probably the minimum, and, when your investor has some of the share capital but needs to syndicate the debt or find another partner to go with it, that's what takes the extra time. So, off-market tends to be a bit more of a slower process.

[343] **Darren Millar:** Okay, fair enough; thank you. Julie Morgan.

[344] **Julie Morgan:** James Price also told us that there'd been three companies that were interested before the Government bought the airport, and that the three were still interested now and that the Government is looking—I think he described it as a medium-term strategy in terms of the future for the airport—and were discussing different sorts of models. I wondered what comment you had on that.

[345] **Mr Cain:** That sounds like a reasonable approach to me; 'medium term' sounds like a very good civil service term to me. [*Laughter.*]

[346] **Julie Morgan:** Yes. I'm not sure what 'medium term' actually is.

[347] **Mr Cain:** Sorry, I'm an ex-civil servant myself, so I know how you use certain words. And that gives you a certain amount of—. Because the market conditions have got to be right. If the Welsh Government wants to sell some of its share capital in the airport, it wants to do it at the right price; it doesn't want to sell it at the bottom of the market. So, you need to give yourself some manoeuvring room. I think, once they've turned it around and they've got it to where the airport is seen to have a growth trajectory, that they have a clear plan for how the rest of the asset is developed. Because what you will find with small airports these days is that it's just as important to make non-passenger related investments. You need to diversify your income streams away from purely passenger charges—not only to things like car parking or retail, but also to other kinds of aeronautical charges: cargo, business aircraft, military aircraft, emergency services. And you need to develop the property portfolio. That gives you a much stronger and more reliable future income stream, which will be attractive to investors and allow you to look at bringing in a partner to take forward further development on a more sensible basis. So, from what James has said, I think I would agree with exactly what

he said.

[348] **Julie Morgan:** What about you, Stuart?

[349] **Professor Cole:** As Chris says, in order to try and find a way of developing an airport, for example, there has to be a market. There has to be a market that can be developed over a period of time. It depends how long it's going to take to develop that market. We've seen that attracting new airlines or bringing an old airline back, as in the case of Flybe, is no easy task. Therefore, to try and develop the market for the airport when that airport is in competition with a next-door neighbour at Bristol, as a largely low-cost airport—. What James was saying, I think, and what he's going to supply you with in terms of more information is probably, as Chris says, about right. It's almost impossible to say what will happen—'what if'. As an economist, my life is based on, 'What if the following assumptions come to fruition?', and you can make your assumptions. But it's not a science; it's more of an art in terms of what could happen if certain circumstances come to pass. I think James is probably—well, James and his team, are—probably in the right ball park.

[350] **Julie Morgan:** Obviously the passenger numbers appear to be rising at the moment, which seems to be optimistic. Have you any comments on those rising numbers and what they mean for the future?

[351] **Mr Cain:** I think the deal with Flybe, hopefully, will deliver consistent growth over a period. Passenger numbers are very heavily dependent upon the economic climate, because it's people's confidence to spend money on going on holiday and it's businesses' to develop new markets. And they tend to be what—. That's the market for air services. If everybody's pulling in their horns, then it's very difficult to make things work.

[352] In addition, I think there are other opportunities that can be developed in terms of trying to serve more of the outbound-leisure market from south Wales from Cardiff. I think further initiatives will need to be made to attract maybe external low-cost carriers. Maybe there are other low-cost carriers that you could get to the airport to do some kind of network. Ultimately, there is a need to make a convincing case, as a number of regional airports have done, to attract a long-haul direct service into a hub. That is not one I think is going to be turned around in a few months. It may take a number of—. I'm aware, in Scotland, to get some of the routes, it took them three years' work to convert an initial interest into the route actually coming on

stream. Newcastle certainly worked on it for three to four years, and Newcastle's quite a good benchmark of where Cardiff should try to be in five to 10 years—well, 10 years' time. The big advantage Cardiff has is the length of its runway relative to Bristol's—in that it's suitable for long haul, whereas Bristol's is a bit too short.

11:15

[353] **Professor Cole:** I'm pleased to say that the demand for Cardiff Airport services has increased, partly because of new airlines coming in more recently. I was looking at their projections for the financial year ending April of this year. It's almost a 20 per cent increase in demand. From the point of view of the Cardiff Airport Express, I'm also pleased to say that we're picking up those kinds of numbers of passengers. Demand for the airport—. There was the world cup, as a massive bonus during October of this year, with a lot more aircraft coming in, with aircraft also paying to park on the apron in exchange for—[*Inaudible.*—]—for it, and the numbers of people passing through, both going out—and, therefore, hopefully, spending money on souvenirs and so on—and also coming in. The increase in demand for the Cardiff Airport Express matched that increase.

[354] **Julie Morgan:** There was a 20 per cent increase in the use of the express.

[355] **Professor Cole:** Well, I took three dates, just to exclude the world cup impact. If we took April to August 2014 and the same period in 2015, our demand went up by 14.7 per cent and the airport's went up by 7.8 per cent. In September to December, because it had the world cup in it, our demand went up by 42.8 per cent, nearly 43 per cent. We had four vehicles on some trips rather than just one; we had vehicles standing by. The airport demand increase was 37.8 per cent. Taking the much more recent period of November to December, which were the latest figures I had in preparing for today—2014 compared with 2015, our demand was up by 30 per cent over that period. We're now carrying—. Whereas we were carrying on the airport express 98,000 passengers in 2014, the figure for 2015, which I've extended to April of this year, will be 130,000. Now, that has got to be part of the consequence of the airport's success in getting more business travellers in, and more scheduled airlines, because it's undoubtedly true that a large part of the Cardiff Airport Express market, compared with the airport market, is that—. The airport express market is very much business. There is a sizeable task to try and get the charter market. It is a usually once-a-year market,

maybe twice a year, people going on holiday, originating in a whole range of places in south Wales, which is the bulk of the catchment area, and driving to the airport because that's what they've always done. Persuading people to change from that into thinking about getting the bus—the airport express, comfortable—hopefully, you'll find that this afternoon when you go on the visit—though it is, and it is—I know I say it myself—a very efficient service, it does what it says on the tin: it's fast and frequent. That service has increased its patronage, partly because of the success of the airport in getting in these new airlines. Breaking into the charter market is going to be a difficult task, but that is the next big sort of golden opportunity for the airport express. The airport, on the other hand, depends very heavily on charter traffic. I think their leisure traffic—my figures may be last year's figures—was 86 per cent for leisure and 14 per cent for business. That may have changed slightly with the introduction of the new services. But it is predominantly, as somebody unkindly once said, a bucket-and-spade and ice cream airport as opposed to a business airport, which is perhaps what Bristol has more of, although it could still, through companies like EasyJet and the charter operators, have a holidaymaking market as well.

[356] **Julie Morgan:** But you obviously—and I think, Chris, you were saying that it should diversify more and get more business.

[357] **Mr Cain:** Yes. There is an opportunity—. As you've probably been told, there's a lot of traffic leaking out of Wales; Welsh-originating traffic that isn't using Cardiff Airport, and is either using Bristol or London, and a little bit going up to Birmingham. The term we use in the industry is 'clawing back' that traffic, because basically passengers would always prefer to fly from their local airport if the local airport can provide the services they want. Yes, they will want to compare prices, and yes there may be some routes that are not available from their local airport and then they will go to others. But that's their first choice, and getting people in south Wales to think as their first thought, 'Can I fly to where I want to go from Cardiff?', is a really important aspect of developing the airport. The work that we did when I was running Newquay—we spent quite a bit of marketing money in our own market trying to change that perception, because we found people didn't know that you could fly and where you could fly to. So, I think that's important.

[358] I think developing business routes and really tailoring those business routes to the kind of sectors that are growing in south Wales, so that you're able to meet both the international destinations and the domestic

destinations that not only they currently use, but they want to develop, is important, and understanding what those are. And then trying to diversify away from purely passenger business—I can't emphasise enough how important this is—to actually become less reliant in what will always be a slightly volatile market gives you a lot sounder basis for long-term development and investment. So, I'm not sure what the numbers are, but normally now most airports under 3 million want to get to a position where 50 per cent of their revenue is not dependent on passenger volume. That's a good, sound target. The smaller you are, the bigger you want your non-passenger component to be. The bigger you are, the bigger the passenger component should be.

[359] **Darren Millar:** I've got a couple of Members who want to come in now, if that's okay. Jocelyn first, and then Mike.

[360] **Jocelyn Davies:** Yes, I wanted to, after looking at your report and listening to James earlier, take you back a little bit to the time of the decision to make the purchase. Because I notice in your report you've got a bit here about the Welsh aerospace sector, so you can see why it's strategically important for the country and for the Welsh Government, but obviously not for the owners of the airport at the time. They didn't care about that.

[361] **Mr Cain:** No. They want to capture purely financial benefits as opposed to economic benefits.

[362] **Jocelyn Davies:** Economic benefit. So, I asked James earlier on: was there any prospect at all, do you think, that the airport would have closed, because you were saying, 'Well, they'll just run it down until a buyer comes along'? Well, they couldn't be certain that that would happen, that the buyer would have ever—. So, was there any prospect at all? Because we did hear last week that it was known, among certainly the staff at the airport, that it was something that was being considered, that it might close. Was that, you know, or was that just bluff? What would happen to the aerospace sector if that airport was not functioning? Because James Price—I asked him about the BA facility there specifically and he said that he would suspect that they would have to fund the runway themselves, and after a limited period of time they would just move somewhere else.

[363] **Mr Cain:** And I think he's right, because they wouldn't want to take on that cost, and it would mean that any further investment that they might be planning, they would look elsewhere to do it, and eventually there would

come some critical point in terms of the life of the building where major investments were required, and they would probably regard it as simpler to make that elsewhere.

[364] Whether the airport would have closed, I'll answer that, if I may, tangentially. There was a view back in the early 2000s that it's impossible to close airports. There are an awful lot of airports either closed or had to be—basically, the public sector's had to step in. That would have happened with Newquay, when the military pulled out. It's happened to Manston airport and Plymouth airport. These airports have actually closed. Blackpool closed and was reopened as a general aviation airport; there are no passenger services out of it. Filton, which is actually, funnily, one of the best placed strategic airports, has been redeveloped for other purposes.

[365] Airports do close, and with private investors—especially, I would say, overseas private investors—they're not going to continue to put money into keeping open an asset unless they see an opportunity in the long term to realise that investment. So, nobody can ever tell you for certain whether it would have happened, but I don't think you could have ruled it out, and therefore if the staff are talking about it, the staff know how bad things are getting, and that's a good indication—that they're worried—that you should be worried.

[366] **Jocelyn Davies:** I think what we were told was that it was said in the boardroom, but that that had filtered out to the staff, but you—

[367] **Mr Cain:** I wouldn't know about that, but it doesn't surprise me that—. What the staff see are the passenger volumes and the number of airlines and how many times they're on the ramp. And they know that the more passengers, the more aircrafts they turn round and the more they refuel, the better the business is doing. If it's dropping off, they will inevitably get worried. And then when they know it's a foreign owner, you add that extra level of uncertainty, because they understand it's part of a big international group that own other airports, and there will be priorities. So, I suspect they would probably very intelligently have put a number of things together, come to the conclusion that their jobs were at risk and have got worried, and I suspect that's what you've got some feedback on.

[368] **Jocelyn Davies:** I asked last week if airports reopen; you've mentioned Blackpool. Is it unusual for airports to reopen after they're closed?

[369] **Mr Cain:** Not if that's the plan at the outset. You can mothball airports and as long as the key infrastructure is not affected and obstacles are not put in the way so that—provided you can then go back to the Civil Aviation Authority and get the licence. At the moment, Plymouth, for example, has not been operating for three years, but it's still possible to reopen Plymouth; it would need some investment to do it and the same with Manston. Filton is completely shut; they're redeveloping it. You can do it, but you've got to have mothballed it in the right way. So, if you strip out or you build a block of flats at the end of the runway, that's it, done. And sometimes that's what developers deliberately do; they'll deliberately try and do something so you can't go back and reopen it, because airports are seen as very attractive brownfield sites for other kinds of development.

[370] **Jocelyn Davies:** You've pleased Mr Hedges.

[371] **Mike Hedges:** I've been trying to convince other people of that for some time during these discussions without any success, so thank you for that. Also, Mr Cain, thank you for your statement about aiming to be Newcastle. Newcastle is running at about 4.5 million passengers. Professor Cole, do you believe that's where we should be aiming for?

[372] **Professor Cole:** Oh, indeed. If you think back, Cardiff had 3 million passengers at one point, so there is clearly a market there, although, as I mentioned earlier, EasyJet has taken a sizeable chunk of—certainly anything from Cardiff to the east, where if you're coming down, say, from Cwmbran and your choice at the M4 is to go left or right, it's about the same journey time to Bristol Airport as it is to Cardiff Airport. Access by road to Cardiff Airport is okay; Bristol is dreadful by comparison, having been to both airports. Cardiff does need a significant improvement in access by car. But Bristol is the big competitor. There is no reason, though, why, given the right circumstances, alternatives to EasyJet can't be attracted, but we have to keep in mind that EasyJet is, as I mentioned a moment ago, pretty well lost to Bristol; Bristol are not going to let go of it very easily. If there's an attempt by Cardiff to offer some very attractive deal, then Bristol will look very seriously to see what they can offer EasyJet to make them stay. But, of course, EasyJet isn't the be-all and end-all of aircraft operations. There are other companies, as we've seen with Vueling and Flybe, to be attracted. KLM, as Chris mentioned earlier, doesn't base itself at Cardiff, but we have a very good service four times a day into a major alternative airport to Heathrow in Amsterdam Schiphol.

[373] **Mike Hedges:** Thank you for that. I'll just quickly say that I flew from Bristol once. The plane took off late because the pilot got lost on his way to the airport. [*Laughter.*]

11:30

[374] But the question I was going to ask is—we know that Gatwick and Heathrow are full, we know they want to put additional runways there and we know a lot of people don't want them to, including, probably, some members of this committee. I think that what I'm saying is: do you see opportunities for long-haul flights? We've got the advantage, haven't we, in Cardiff of a very good runway that can take almost any current size of aircraft. Isn't there an opportunity to start looking? If we are, where should we be looking to? I know that I asked this question last week, and I didn't get very far, but I'll try again. Should we be looking to North America, South America, Africa or Asia? Where should we be looking—all four of them?

[375] **Mr Cain:** I just want to comment on previously: the actual market or, indeed, traffic out of south Wales is 3.3 million passengers at the moment. So, that is your underlying market, and that's not taking anything from across the Severn. And, of course, at the moment, coming back the other way, you've got a £6.60 toll to pay, which is going to be added onto the passengers' perception of the price. Long haul, the two destinations that airports—let's call them medium-sized regional airports—can do will be a North American eastern seaboard gateway and a middle-eastern hub, and there are four of those, so: Emirates into Dubai, Etihad into Abu Dhabi, Qatar and Turkish into Istanbul.

[376] I think Turkish is a very interesting one because, I believe, in 20 years' time, Istanbul will be the biggest hub in the world. It's in the best geographical position globally and they are building a huge new airport that will have 160 million capacity. Basically, its value is it's further north, so, you don't have the hour-and-a-half, two-hour sector that you need to go down to get to the UAE. So, there are four opportunities. There are other, smaller gulf carriers. I am sure that the airport management team have got well-developed propositions. They understand where businesses and people from south Wales want to get to and what are the most effective hubs.

[377] It's unlikely that it will be purely point-to-point traffic. They will need to be connecting onwards across America, let's say, from an eastern—. So, if you flew into Newark, you could get to 80 destinations across America out of

Newark. You could fly into Toronto. You could fly into Atlanta. Typically, you want to go for the airport that's got the biggest underlying point-to-point traffic, which would tend to be New York.

[378] So, the difficulty with this is—I suspect the airlines have almost like a pecking order of places that they will gradually get to. You've seen it with the two London airports, Manchester, Birmingham, Edinburgh and Glasgow. Now they're down at Newcastle. They're gradually coming down and they're looking for market opportunities. The south-west and Wales is a big gap in that network. They may argue, 'Ah, well, everybody can travel down the M4 to go to Heathrow' with that. But you quite rightly say, over the next 10 years, there's no more capacity at Heathrow, and Gatwick's getting pretty full. Is this an opportune time to say, 'Well, actually, there is a very strong market out of the south-west and Wales, which Cardiff is uniquely able to satisfy'?

[379] **Mike Hedges:** Thank you.

[380] **Darren Millar:** Stuart Cole, you've already referred to some of the inadequacies, perhaps, of the road links—or certainly the improvements, perhaps, that are needed on the road links. What about rail links?

[381] **Professor Cole:** At the moment, there is an hourly service to Rhoose international airport station. That's not a frequency that is going to attract very many customers, and, in fact, doesn't. I'm sceptical about whether that link should continue between Rhoose station and the airport. I always have been. One might say that I'm biased, but before the airport express came along that was pretty well the only form of public transport, other than local bus services that called in at the airport. Since the development of the airport express—I haven't got the exact figures, but the numbers of people making a choice to go on the hourly service is low, simply because people are very cautious when they're going to pick up an aircraft—that you leave yourself plenty of time; first, to go through the check-in and security facility, but also to make sure that you've got there on time. So, if you have a 20-minute service, then you might allow yourself 40 minutes, or maybe even 20 minutes. You know there's another bus coming and you know it's within the timescale that you have to achieve in order to get on the plane. When you have an hourly service and you're having to make a connection, then you will worry about, 'Can I actually make that connection? So, I will take the precaution of travelling an hour earlier than I need to. I might get there in plenty of time, but on the other hand I might not'. It's one of the reasons

why the non-business market drives to the airport, primarily.

[382] As mentioned earlier, to persuade that part of the market to go on the airport express to the airport, rather than drive, is based on what public transport facility is there once you get to the city terminal at the railway station—well, eventually the railway station—and that doesn't really kick off in the mornings until about half past six or seven o'clock. The buses and the trains don't start in any real numbers. Similarly, in the evening, the bus services start to become less frequent after about half past six or seven o'clock. So, the only market that's available, really, to the airport express on the charter side is between departures around about midday to, say, six or seven o'clock and conversely coming back between, say, nine o'clock arrivals and four o'clock in the afternoon; because then people know that they can make their onward journeys or their forward journeys by local public transport. No-one is going to get a taxi, for example, to the railway station and then get a bus in. Certainly, those are the people, currently using cars, who would need to be attracted; but it's really only that chunk in the middle. The six o'clock charter departures, of which there are several from Cardiff Airport, are not something that people would use this airport express for. Businesspeople, on the other hand, who are staying in Cardiff overnight, would find—. Well, that's who the bulk of the customer base is currently for the airport express.

[383] **Darren Millar:** Okay.

[384] **Mr Cain:** Can I just add—? If you take a good example—and one of the best examples I've seen of bus-based public transport access was at Edinburgh, where they were achieving 27 per cent mode split. It's helped in their mix in that there are a lot of tourists using it, who tend to be willing to use the public transport. I think what Professor Cole is flagging here is that buses can deliver an awful lot in terms of public transport access that rail links, typically, unless you have the railway literally running 50 yards away from the terminal—as you do at Prestwick and Southampton—it's difficult to make a rail link work with less than 10 million passengers. So, I think developing the bus network and optimising it so that you have almost guaranteed times between the city centre and other parts of wider south Wales is a very effective way of delivering that kind of service.

[385] **Darren Millar:** Okay. Can I just ask—? You mentioned the revenue models for airports, and you don't want all the cash coming in through the passenger bums on seats, effectively, and you've got to diversify. The car

parking revenue is pretty critical to the airport as well, isn't it?

[386] **Mr Cain:** It is.

[387] **Darren Millar:** Would I be wrong in saying that there's a disincentive to get more people onto buses for the airport?

[388] **Mr Cain:** It's one of the industry dilemmas.

[389] **Darren Millar:** There's a balance to be struck, isn't there, so you're still generating the revenue from the car park.

[390] **Mr Cain:** There is.

[391] **Darren Millar:** Jenny, you wanted to come in.

[392] **Jenny Rathbone:** The more successful you are, surely, in attracting more passengers, the more you need to have people moving onto public transport, or you'll have huge congestion and unreliability in arrival—

[393] **Mr Cain:** When you get to a very large scale of airport, yes. Really, what you're trying to target with your public transport is those who don't have access to the car. So, inbound passengers, typically, will not have access to a car and therefore will want good public transport routes. Or it may be that somebody's going away for a long trip and doesn't want to park the car, or is going from their office environment for the day. There are a number of markets where there isn't car dependency. But if you think about it—let's say you manage to get to 10 per cent or 15 per cent of the traffic going on public transport—for every 100 additional passengers, that's still another 85 who'll want to park at the airport.

[394] **Jenny Rathbone:** Okay, but going back to your earlier suggestion that what we need to do is ensure that Cardiff is the first choice for people to travel, if it's available, surely one of the things that needs to happen is to have those secure links, and in the longer term, is it not essential to have decent light rail links, just like many other European airports? It's just that the United Kingdom has such poor infrastructure. You don't expect that—

[395] **Mr Cain:** I'll let Professor Cole in—he's much more of a surface transport expert. All I can say from other airports, and I know pretty much every regional airport in the UK, and most of them in Europe, is that really

good-quality bus environments people will be willing to use. You tend to go to light rail when you've got longer distances that you need to cover faster, or you need to have a completely independent corridor to get you out there. That's why they've done it in Edinburgh—because basically they were getting to the point where there were six to eight buses parked outside the terminal literally every minute, and the volumes were just becoming too big, so that they couldn't handle them purely through buses. But they diversified the bus network so that other places now are being served rather than purely the city centre. So, it's all about hitting the right type of volumes. Now, where you may get a need for something like a light rail line is if you develop all the area around the airport so that it becomes a major business district. This is one of the things that I flagged in the report. Plus, you're also developing St Athan as a major aerospace cluster. The combination of the two things—a growing airport and a big new business district—may generate the kind of traffic that would attract that kind of route.

[396] **Professor Cole:** If I take the road link first and then the potential rail link, the road link that was proposed by the Welsh Government was from junction 34 down through Pendoylan and then just bypassing Bonvilston and coming down what's been called Five Mile Lane: two sections of route pretty well in a straight line coming down from junction 34, almost to the airport. When the Government proposed this, to say there were a lot of objections from the residents of Pendoylan—and a very well-organised collection of residents—is putting it mildly. They had a whole string of expertise there and I think the Government eventually gave up on trying to take them on at that point and retreated back. The Five Mile Lane section, however, is progressing. That's now going through the compulsory purchase order stage. Certainly, there wasn't the anti feeling at the time as there was in the area around Pendoylan and, as I understand it, the building should begin in February 2017 and be completed soon thereafter. So, the process of land purchase, and so on, is going on, and it's largely an agricultural strip along that section of the route. So, that will be built, and that will then require an improvement of the A48 between Culverhouse Cross and just east of Bonvilston to get down Five Mile Lane. That will be the designated route for the moment.

[397] **Jenny Rathbone:** Okay. And would that link be sufficiently wide to accommodate light rail once we've had our electrification and all that?

[398] **Professor Cole:** I think, to look at light rail, we aren't necessarily looking at the same route. There is the possibility of an interim bus service

along that route, were the whole route to junction 34 to be built. The width of the road is a standard single carriageway. It's a one-lane, single carriageway road. So, it's a wide road, and if you happen to be in that area, there is a section of the road dropping southwards from the A48 that shows you how wide it would be. It is a good-quality road, and that would be suitable for either a busway or a guided busway, even, to drop down from the railway, which is also at junction 34. As it happens, by coincidence, there's a four-track section of railway at junction 34 that enables you to get inter-cities going past with a local train stopping. So, you know, it's possible to run something along those lines. Going back to the rail connection—

11:45

[399] **Darren Millar:** I'm terribly sorry to interrupt, professor; we're pretty limited for time now, so if you could be as concise as possible.

[400] **Professor Cole:** There was a proposal two years ago to build a railway link into the airport directly from the Vale of Glamorgan line, partly financed by a private company who owns a lot of land there, and partly funded by the Welsh Government. That hasn't got any further than that at the moment, and it remains to be seen whether that will be—. It would certainly be an attractive proposition for the Welsh Government to look at.

[401] **Jenny Rathbone:** So, that rail link would connect with the existing terminal, would it?

[402] **Professor Cole:** It would run into the existing terminal from the Vale of Glamorgan line just east of the viaduct—Porthkerry viaduct.

[403] **Jenny Rathbone:** Is there anything known about the cost of doing something like that?

[404] **Professor Cole:** Yes. At the time, the cost was estimated—. James mentioned a figure of £100 million, which is what Network Rail would have charged. If the railway was built separately by the Welsh Government to conditions set down by the railway inspectorate, and Network Rail only made the connection with their existing tracks and put up the signalling, that figure could be brought down to about half of £100 million, of which one of the big property developers—one of the big insurance companies—would have been prepared to pay up to £15 million of that capital cost, if they got into the local development plan.

[405] **Darren Millar:** Okay, thank you for that. Just two very brief answers from you on two questions, if I may. The first is on the governance arrangements at the airport. Do you have any particular view on the governance arrangements in terms of Holdco and the reporting back? Again, you've seen some of the evidence. Just any views, Professor Cole?

[406] **Professor Cole:** I think the way they've done it is to have an arm's-length company owned by Welsh Government holdings limited, the airport company being separate. It needs all sorts of things. Decisions could be made by the board, subject, of course, to the Minister deciding that the funding is available, or indeed the borrowing can be made within the public sector borrowing requirement. Secondly, it gives an independence to operate the airport without—dare I say it in this august body—too much interference from outside, and that they run the airport as a business. I think we're looking for the same thing with the railway company that the Minister's been talking about.

[407] **Darren Millar:** So, as far as you're concerned, it's an entirely appropriate arrangement and there's no reason to suggest it shouldn't be working well long into the future.

[408] **Professor Cole:** I think it's far better than having it perhaps much more closely integrated into Government.

[409] **Darren Millar:** And your view.

[410] **Mr Cain:** I think that Holdco probably needs some aviation expertise brought into it, and I think it needs to look—. It's probably a good vehicle for looking at a big strategic picture. It's very difficult, let's say, for the Cardiff Airport management board to be looking at that, when you're trying to look at St Athan and the enterprise zone; that's where Holdco has the opportunity to think strategically.

[411] **Darren Millar:** Right, so aviation expertise and a bit of a wider sort of—

[412] **Mr Cain:** A strategic role, yes.

[413] **Darren Millar:** And just finally—air passenger duty. We've had the view that if air passenger duty was devolved, then obviously that could realise some cash which could then be invested into the airport, or to give a

competitive advantage with the reduction in the air passenger duty. Would you advocate that?

[414] **Mr Cain:** I think HM Treasury are still going to want their money. The deal that I think is on offer in Scotland is that you have to pay—. Certainly, in Northern Ireland, the Northern Ireland Assembly has to pay the Treasury what it thinks it would have got if APD had been—. It's not a nil-sum game at all. Price elasticity in certain markets—of reducing the price—is attractive in terms of growing the market. If you look at what happened in Ireland when they reduced their APD and if you look what happened in the Netherlands when they removed their APD, there is no doubt that it stimulates growth. The issue is how you fund it. At the moment, I think one of the—. There is an opportunity to do it in a targeted way that would be very effective. And I think it probably—. I don't know what evidence was put to the Silk commission, but it needs to be carefully thought through—and I'm sure the Welsh Government officials are doing that—to find the most effective and optimum way of using any devolved powers. I don't think it necessarily needs to be a blanket removal.

[415] **Darren Millar:** Professor Cole, final word to you on this, and then we'll close this session.

[416] **Professor Cole:** It's exactly as though there's this balance between the elasticity of demand for using Cardiff Airport by the airlines—the price to the customer is reduced by a certain amount if Welsh Government decides to reduce APD. Similarly, as we've already heard, HMRC will require its pound of flesh, and depending on what figure that is—that's calculated in some way—then as long as HMRC are happy, we can take advantage of the market advantage that comes from a reduced APD. But that's the balance. I would just exclude HMRC—there's no discussion—but then they wouldn't to—
[Inaudible.]

[417] **Mike Hedges:** The Holtham committee showed about £10 million a year for APD.

[418] **Mr Cain:** Right. That's what would have to be paid to Treasury.

[419] **Darren Millar:** The clock has beaten us with this evidence session. Thank you so much for your evidence. It's been really good at giving us an insight into your expertise on these various matters, including these tiny little network exchanges on the rail lines and the bus network, and we

appreciate that. So, thank you so much for coming in. If there's any additional evidence in addition to the papers that you've provided, certainly on the bus numbers—. I think you were talking about some of the latest figures on the bus number, Professor Cole.

[420] **Professor Cole:** I can supply those.

[421] **Darren Millar:** That would be interesting, I think, for the committee in our files. And likewise, Mr Cain, if anything emerges and pops into your head about, perhaps, comparisons with some of the other airports, particularly the Newcastle sort of vision, if you like, for Cardiff, then please send it in.

[422] But that brings us to the end of our session. You'll be sent a copy of the transcript of today's proceedings. If there's anything inaccurate in there, please let us know and we'll get the Record corrected. So, Professor Cole and Chris Cain, thank you very much indeed.

[423] **Mr Cain:** Thank you very much.

[424] **Professor Cole:** Thank you.

[425] **Darren Millar:** We're going to take a two-minute break now while we get the video link up for our next witness.

*Gohiriwyd y cyfarfod rhwng 11:52 ac 11:58.
The meeting adjourned between 11:52 and 11:58.*

Maes Awyr Caerdydd—Sesiwn Dystiolaeth 5 Cardiff Airport—Evidence Session 5

[426] **Darren Millar:** Okay. Welcome back to the Public Accounts Committee. We're moving on now to item 5, which is continuing with our inquiry into the purchase and acquisition of Cardiff Airport by the Welsh Government. This is our fifth evidence session, and we're joined by video link, which we're hoping we'll maintain throughout the duration of the session, by John Nicholls, who is the director of aviation, maritime, freight and canals in Transport Scotland—welcome to you, John—and Andrew Miller, who is the chair of Glasgow Prestwick Airport. Welcome to you, Andrew.

[427] **Mr Miller:** Good morning.

[428] **Darren Millar:** We're very grateful to you for joining us today because, as you will know, there are some similarities and some dissimilarities in terms of the approach that's been taken in both Scotland and Wales with the Government stepping in to acquire what are strategic and important assets. Can you tell us in terms of the background to the situation in Scotland—? We're obviously aware that there had been a significant decline in passenger numbers at Glasgow airport, that the Government was trying to support the airport to find a new private sector buyer to come in and secure the future of that airport, which didn't work. What else was the Government doing prior to purchase in order to support activity at the airport to try and assist in different ways, other than acquisition? Who wants to start?

12:00

[429] **Mr Nicholls:** I'll take that one, Chair, if I may. I was involved with Prestwick from a Scottish Government perspective from October 2012, when we started to get closely involved with the acquisition or the marketing of the business. As you rightly say, the vendor, the owners at the time, had made a strategic decision to divest themselves of their European airport holdings, and were marketing various airports for sale, including Prestwick. Our main interest, again, as you rightly say, was in helping them to find a good investor to purchase the airport as a going concern for it to stay in business in that way.

[430] At that time, we were not proposing any sort of direct public ownership model. We were instead looking to support the vendors by means of marketing the airport by indicating what particular Government support might be available to a new owner, and essentially engaging very closely with the local stakeholders, including the local authority, to ensure that everybody around the table was assisting in that regard.

[431] We did consider some other options as the marketing process went along, and some of those, I think, were quite similar to those considered by the Welsh Government, in that we were looking at some sort of joint venture arrangement with a private sector partner, and, at the very end of the process, some sort of public sector involvement. That was very much the option at the end of the process when we could see that there was no other private sector buyer likely to come forward for the airport.

[432] **Darren Millar:** So, it was very much an option of last resort, as it were. You know, 'if all else fails, we'll consider this.'

[433] **Mr Nicholls:** That's correct. It became very clear to us that, although Infratil, the owners of the airport, had gone quite a long way down the route of negotiating with a potential purchaser from the private sector, they'd got to a point where that potential purchaser was not able to meet the conditions that the seller wanted on the sale, and the timescale for the transaction. So, it became clear to Scottish Ministers that time was running short, the owners had indicated that they were prepared to close the airport if no buyer came forward, and it was at that point that Scottish Ministers announced their intention to negotiate the acquisition.

[434] **Darren Millar:** You've made it clear that the opportunity for a potential joint venture with the private sector was also considered by the Government. Why wasn't that something that progressed?

[435] **Mr Nicholls:** We did have a close look at that possibility, but the short answer to that is that it didn't stack up commercially and practically from the analysis we were able to undertake. There were complications with it that, in the end, the professional advisers who we engaged didn't feel able to recommend it to us. So, that was something that we decided we shouldn't pursue.

[436] **Darren Millar:** The Welsh Government has asserted to us that one of the reasons why they were not able to progress with a similar option that they had on the table was just the length of time it would have taken to satisfy the private partners that they were engaged with. Is that one of the factors that was a barrier in Scotland?

[437] **Mr Nicholls:** I don't recall that being a particular barrier here. We did not, from recollection, look to engage with particular private sector partners at that time. As you've mentioned yourself, we were operating to quite a constrained timetable, in that the owner of the airport was in a hurry to extract themselves from the business.

[438] **Darren Millar:** And prior to the crisis situation that began to develop with the previous owner, what sort of support had the Scottish Government been giving to the aviation sector more generally across Scotland, and particularly in terms of Glasgow? Were there route development funds available? Were there grants available to support capital investment et cetera? I mean, what was available out there to support them?

[439] **Mr Nicholls:** As you'll be aware, we do have several airports in the central belt of Scotland: as well as Glasgow Prestwick Airport, we have Glasgow international and Edinburgh Airport, and, obviously, Inverness Airport and Aberdeen International Airport, and all the other Highlands and Islands airports, which are already in public ownership here.

[440] Our approach to route development, to take the first part of your question, is that, historically, in the early part of this century we did have a designated route development fund that we made available to provide direct financial support to airlines wanting to operate to Scotland. However, it turned out that that was not compliant with EU rules on state aid, so we had to redesign the route development support approach, and now what we do is, again, support airlines and airports to develop new services.

[441] That is usually done now via a number of methods. There is some financial support in the form of co-operative marketing, as we call it, in a way that sees Scottish Government and its agencies provide match funding to marketing investment by airlines. We also provide support to airports by negotiating or talking directly to airlines in terms of market intelligence and what the Scottish Government can offer in terms of political support and numbers demonstrating the demand for direct services. That's been very successful over recent years across our airports. We have to adopt an airport-neutral approach there. We encourage airlines to come to Scotland, and it's for them to decide which airport they wish to serve. And, clearly, the airports themselves have a role to play in that in providing commercial arrangements with airlines.

[442] In terms of grant support direct to airports, we do have an enterprise agency—Scottish Enterprise—who are able to provide some support to individual airports, generally for individual projects. And Prestwick has benefited from those in the past, and that is an option open to Prestwick now. Andrew may want to say a bit more about that later on, on how that's being taken forward.

[443] And, indeed, during the acquisition process, or the marketing process, for the airport, we made it clear that that facility was available, either to the owner at the time or, indeed, to a new owner.

[444] **Darren Millar:** Okay, thank you for that. Jenny Rathbone.

[445] **Jenny Rathbone:** I just want to ask: what was to prevent Infratil selling

the asset for another purpose, as £1 is obviously not a particularly attractive sale?

[446] **Mr Nicholls:** Clearly, you'd have to ask Infratil that question, but in our dealings with Infratil they made clear that their preference was to sell the airport as a going concern. There is a fair amount of land associated with the airport and that has a value, and I suppose it would have been open to them to look at it in that way. But I think that a strategic decision had been taken by Infratil and their parent group that they simply wanted to divest themselves of their airport assets, and do that in as quick a manner as possible, hence the need for speed on our part.

[447] **Jenny Rathbone:** Okay, so there was never any inclination on their part to explore other options for the use of this land?

[448] **Mr Nicholls:** Not that I'm aware of, as I say. But that's a question that you'd clearly have to ask Infratil.

[449] **Jenny Rathbone:** Okay.

[450] **Darren Millar:** You were also working under pressure of time, weren't you, here? I know that there was a significant cost to the Government in terms of undertaking due diligence work, et cetera—similar costs, actually, to those which were spent by the Welsh Government in terms of the due diligence work that it undertook. Do you want to just describe a little bit about the scope of that due diligence work? You had formal valuations undertaken, no doubt, on the asset.

[451] **Mr Nicholls:** Yes, we did, and you're right—. Just to say a little bit more about the timescale, we had six weeks from when the then Deputy First Minister, now the First Minister, announced our intention to negotiate the acquisition. That timescale was set by the owners. So, we didn't have a great deal of time. We were helped, to a large extent, by the fact that the previous private-sector bidder in the process had undertaken a large amount of due diligence in what turned out to be an aborted acquisition process and we took the decision to acquire the outputs from that due diligence to ensure we could meet that six-week deadline. That did indeed contain a lot of valuation information, which we simply wouldn't have been able to do in that timescale.

[452] And, as I'm sure you're also aware, our own Audit Scotland have

undertaken an inquiry into the acquisition process here and they found that we had acted reasonably in the process we adopted in the acquisition of the airport, including the due diligence that had been undertaken. So, that was reassuring to us. So, it involved financial and legal and property assessments. All the sorts of things you would expect an acquiring authority to undertake.

[453] **Darren Millar:** There was also a need, wasn't there, for significant support to the cash flow of the airport in, certainly, the short to medium term? Has that been in line with your forecasts at the point of acquisition? Certainly, as far as the Welsh Government's acquisition of Cardiff has been concerned, there's been a lot more cash required than had originally been anticipated. Has yours been broadly in line with the expectations?

[454] **Mr Nicholls:** Broadly in line so far, although, clearly, it's a dynamic market environment out there. What Ministers here committed to was to make available £25 million of loan funding to the business. So far, as I say, we're on track with that. We obviously can't predict the future with any degree of certainty, particularly in an aviation-industry context. Ministers have made clear that further funding will be available as necessary. But, so far, we're on track with that kind of level of investment.

[455] **Darren Millar:** Andrew Miller, perhaps we can just turn to the governance arrangements, if we may? One of the big differences between the governance arrangements at Glasgow Prestwick versus Cardiff appears to be the fact that you are both chair of the airport board as well as the holding company board that has been established. Do you want to tell us why you think that might be a good or a bad thing versus the model here, in which both boards are very separate and have different personnel? In fact, none of the individuals sit on either body's boards at the moment. Then, I'll bring in Julie.

[456] **Mr Miller:** With the exception of myself, yes. First of all, I would say that the appointments are commercially focused. The shareholders have been very keen to make sure that the commercial criteria, and the experience of the individuals in aviation and aviation-related areas, is significant enough to turn the business around and indeed lead the operation to a level of profitability, which we're currently undertaking.

12:15

[457] I sit on both boards, as you say. The holding board is confined to issues of strategy, long-term capital investments and making sure that the investments are aligned with the objectives that the holding company sets for the operating board. But also I sit as chairman, as you've said, Mr Chairman—I sit as chair of the operating company, which has the commercial grant, both from a non-executive point of view, but also from an executive point of view. We have four executives who are on the board, and we have four non-executive directors on the operating board, which I chair. These non-executive directors are from commercial enterprises and have background and experience in areas that I felt were necessary to turn the business around. For instance, one of the executives—a lady, Jayne Maclennan—she's the property director of the First Group in the UK, she has global responsibility for all property transactions, and Jayne sits on the board because of her property expertise. Our communications, brand and marketing individual, Gordon Arthur, was the communications director of the Commonwealth Games. He sits on the board as a non-executive director. We have Bob Goldfield, who is ex-chief executive officer of Dover ports authority and ex-chief executive officer of Shannon Airport and Newcastle airport, because of his transport and airport-operating experience. And we have Ken Dalton, who is the ex-managing director of AECOM, the big engineering company. These three non-executives, plus myself—because I have a life in aviation with Air New Zealand, British Airways, and also in a management consultancy, buying and selling airports and starting airlines up on a global basis—we all have what I consider to be the necessary commercial background and experience to give the business the necessary strategic oomph to make it succeed.

[458] So, the operations have the execs and non-exec. At the holding company, I would say, and no disrespect to John, that I'm the only person with a commercial background in aviation. And I chair that board. John sits on that board, along with two other colleagues who represent the shareholders' interests but at arm's length from the political dimension, if I could use that word.

[459] **Darren Millar:** You obviously hold great store in the fact that there's a lot of aviation expertise around the table on the airport board. Can I just ask, in terms of the holding company, does the holding company have a direct opportunity to place people on the airport board? Do they have to approve appointments to the airport board, or is that something that the airport board is independent and able to do on its own?

[460] **Mr Nicholls:** Well, I'll take that one, if I may, Chair. The appointments of the chair of the holding company and the operations company, and the appointments of the non-executive directors to those companies, those appointments that are—they are ministerial appointments, although, as Andrew has said, the appointments of the non-executive directors to the operational company, and for Andrew's own appointment himself, were done through a competitive process, applications and interviews. Then, following that process, recommendations were put to Ministers. For the executive appointments to the operational company, that's very much a matter for the board of the operational company. So, the holding company doesn't have a direct role in the appointments of the operational company, although I did play a part in the recruitment process for the non-executive directors and made recommendations to Ministers on those appointments.

[461] **Darren Millar:** Okay. Thank you. Julie Morgan.

[462] **Julie Morgan:** Yes. Thank you very much. I wondered, Mr Miller, if there was ever any conflict of interest in holding the two roles that you hold.

[463] **Mr Miller:** No, although there have been some occasions where there have been some discussions around some strategic areas that obviously could put me in a situation of conflict, but these have not arisen at this moment in time.

[464] **Julie Morgan:** Could you envisage what sort of issues would produce a conflict of interest, then? Could you tell us? Because it's a different model to what we've got?

[465] **Mr Miller:** For instance, an external investor in the organisation that, commercially, would fit the business in terms of whole or part shareholding. Obviously, through my position on the holding board, we would have to discuss that. If the operating board had made that recommendation, I may have to stand aside in that discussion if I were recommended the shareholder or the offer for the company to the holding company. That would be one good example, but it's not happened to date.

[466] **Julie Morgan:** And you feel confident in the model that is there.

[467] **Mr Miller:** Yes, I do. That model was transferred to me before I accepted the appointment, and it's worked very well to date.

[468] **Julie Morgan:** Is the plan for that model to continue? Was there any discussion in the Scottish Government about any change to the model?

[469] **Mr Nicholls:** Not at the present time. Scottish Ministers have made clear the long-term aspiration for the business: that it should be returned to the private sector and that we should get a return on our investment. Clearly, a change might be likely at that point. I should say that in opting for the governance model that we did, we did take advice from industry experts and corporate finance and legal advisers as to the best way of both undertaking the acquisition and governance thereafter. This was the model that was recommended to us. It's reassuring to note that, from the Audit Scotland report that came out last year, they have said that their assessment was that we had put good governance arrangements in place. So, we could take some comfort from that.

[470] **Julie Morgan:** Thank you. You say this is there for the—. Well, long-term—the Government hopes that the private sector will take over. How do you define 'long-term'?

[471] **Mr Nicholls:** Well, if I may, just to explain a little bit more on the background to the acquisition, we were very clear that to ensure there were no state aid issues with what was being proposed we've had to satisfy the market economy investment principle, which was that the Scottish Government had to act in a way that a commercial operator would. So, part of our due diligence was to develop a business plan or assess the business conditions to analyse whether or not we could make a long-term return on our investment in the airport. That assessment found that we could do that, and again Audit Scotland verified that in their report, but we have not put a timescale on that investment, on that long-term return. Scottish Ministers have always recognised that it's going to take a while. It is a challenging environment in which to work, but Prestwick has a lot going for it, but we know it's not going to be an overnight turnaround. As I say, we haven't put a public timescale on it. There are some numbers around when investments might—or when we might generate a return, but, obviously, you understand that those are commercially sensitive and aren't something that we would publicise at this time.

[472] **Julie Morgan:** Thank you.

[473] **Darren Millar:** Can I just explore this potential tension, Andrew Miller, between your role as chair of the holding company versus chair of the

operational side of the business? Given that the holding company has to hold to account the airport for its operations, isn't there constant conflict of interest, frankly, between both of the roles that you hold?

[474] **Mr Miller:** I don't think so in that regard. Operationally, do you mean the safety and the compliance aspects of running—

[475] **Darren Millar:** Just in terms of the performance. In terms more, really, of the general performance of the airport. I mean, the holding company is there to try and retain the Scottish Government's value, I suppose, and to maximise the value of the asset that they've acquired, and to make sure that the business plans et cetera are being delivered against, and the performance targets are being met. But at the other end of the table, when you reverse the situation and you're sat there in your capacity, isn't there an inherent tension?

[476] **Mr Miller:** Well, there's definitely no schizophrenia in my mind, that's for sure. The business has annual budgets and a corporate plan process, which are discussed with the operating company, and the key result areas and key performance indicators that are articulated in that plan are passed up to the holding company. There's some dialogue about the financing, dialogue about the commercial directions, the strategic directions, that the business is actually taking, and it works.

[477] **Darren Millar:** What are the main KPIs that you—?

[478] **Mr Miller:** There's no conflict of interest because the business is run on commercial grounds, and we perform, or try to perform, as profitably as possible. All I can say is that there's been no conflict between that sort of day-to-day running and the long-term horizons of the business with our shareholder.

[479] **Darren Millar:** Just to ask for a little bit more information in terms of how you measure the performance of the airport as a holding company, presumably you receive the KPIs on a regular basis, reported to the monthly board meetings, but in terms of those KPIs, what do you emphasise as being the most important KPIs? We've heard from the Welsh Government's holding company that they are looking at passenger numbers, profitability and route development, primarily, as measures of success. Is that similar to the prescription for success that you've got up in Scotland?

[480] **Mr Miller:** Yes, we obviously look at that. We've got a current profit trading gap, in terms of our break even, where we're actually trading. So, an analysis of that, an analysis of route development from the market data that we have in terms of our penetration. For instance, 10 years ago, Prestwick had around about 20 per cent market penetration in the central Scotland belt. Two years ago that was down to 10 per cent. So, it's passenger numbers, penetration, route development, looking at the routes that are currently not served from Prestwick, and looking at our catchment area from the Civil Aviation Authority data, working out which routes would be profitably served from Prestwick, and approaching the airlines with the right aircraft type, and the right balance sheet robustness, to see if we can develop plans together in terms of developing the market. So, profitability, KPIs in terms of how we sit vis-à-vis other airports, not only in the UK and Europe, in terms of throughput per employee, profit per employee, and indeed looking at the airlines that are currently flying in and out of Prestwick and making sure that we have robust financial data on them to know that all their current plans for capacity and future plans can be underwritten in terms of balance sheet strength. So, it's airports, airlines, benchmarking across airports of a similar size and state, and looking at the gaps and working through the plans in terms of how we fill the gaps and improve our performance.

[481] **Darren Millar:** And in terms of the business planning arrangements, the airport board has to present to the holding company a business plan on a regular basis, I assume. Does that have to be signed off, as it were, by the holding company, or is it just a requirement that one is presented?

[482] **Mr Miller:** Well, it has to be signed off by the holding company, because it can't be financing the business just now. Clearly we're a drain on public funds currently. That's not, indeed, going to be the case in the future. I have three major KRAs, key result areas, where I've got to perform. No. 1, less of an impact on the public purse; no. 2, look for possible alternative investors for the business; and no. 3, return the business to a long-term strategic platform in terms of longevity and stability on behalf of the local stakeholders that we have.

12:30

[483] **Darren Millar:** At the moment, the holding company for the airport here in Cardiff only requires two-year business plans from the airport board. Do you think that that's sufficient? What do you think is appropriate in your view?

[484] **Mr Miller:** Well, appropriate in my view, obviously, is a bit longer. Obviously, there are a lot of issues that play in aviation in terms of, you know, the price of fuel. If we were sitting here two years ago, fuel was over US\$100 a barrel and, you know, it's been below \$30. So, if you take a company such as a low-cost organisation like Ryanair or EasyJet, 40 per cent of their operating costs are consumed by fuel. So, if you halve the price of fuel, that has a massive impact on these businesses. However, with foreign exchange rates, fuel hedging et cetera, one has got to put, you know, a figure on a piece of paper and say, 'For every year for the next five years, this is where we believe the business is.' So, when it comes to airlines, their planning horizon is at five years plus and most of the big airlines already know what aircraft they're buying at a five-year plus horizon. Airports' long-term capital investments, infrastructure businesses, where a lot of the big pension companies—you know, global pension schemes—take a position, they work very much on a 20-year horizon. So, one would say that operating in a two-year horizon isn't probably best practice; a five-year horizon would be more appropriate, especially when you consider the long-term planning horizons of the airports and the competition around Cardiff and, indeed, the airlines that are flying in and out of there—the big players, I mean; some of the smaller entrepreneurial airlines with smaller aircraft, like some of the charter operators, will have a short-term planning horizon. But we're talking about long-term planning horizons for an important strategic asset, such as Cardiff Airport.

[485] **Darren Millar:** And just one final question, if I may, and then if any other Members have got questions, we'll get to them. But just on air passenger duty, how important is the fact that air passenger duty is devolved to the Scottish Government, and what opportunities does that present to Glasgow Prestwick for you? Do you want to just tell us, John?

[486] **Mr Nicholls:** Air passenger duty is not yet devolved to the Scottish Parliament; we await for that to happen. But the Scottish Government's policy, once devolution does happen, will be for a cut of 50 per cent in APD from 2018 and abolition when resources allow. We've seen over recent years very many airlines saying to us, both in conversations with Ministers and with officials, but also supported by a fair amount of analysis, that APD is a major deterrent to further route development in Scotland. Ryanair and EasyJet have both been on record as saying that, and have even put numbers on how many more passengers there might be to Scottish airports if APD were to be reduced or, in their view, preferably abolished.

[487] So, Scottish Ministers are very clear on that, and have stated their position publicly. We will obviously need to see what happens once the devolution of the powers do come to Scotland, and what will happen in the next Scottish Parliament, but there is a general acceptance amongst the Scottish aviation community that the reduction or removal of APD will lead to increased direct routes from Scotland.

[488] **Mr Miller:** I would just add one statistic to what John has actually said: APD currently is twice the profit per passenger that Ryanair makes, so double the current profit for bags. So, if you look at that business, which last year carried over 100 million passengers—the biggest airline in Europe—reducing APD or removing APD is a substantial incentive for them to invest into businesses, airports and markets where the APD has been withdrawn. You only have to look towards eastern Europe to see airports and markets where there's no equivalent of APD and what market stimulation has happened there. So, it's a very important number and a very important impasse currently in restraining passenger demand, especially in the low-cost sector.

[489] **Darren Millar:** And perhaps just finally—finally, one thing which you've obviously been seeking to do—and we've seen some of the information around your strategic vision for the airport—is to diversify what you're doing there in order to generate other revenue streams. You seem to be performing quite well in terms of developing the freight side of the business and, no doubt, some of your other plans, if they come off, will be extremely profitable as well. But, what is it, particularly about the freight side, that you've been able to grow that at a better rate than, perhaps, some of the other aspects of the business to date?

[490] **Mr Miller:** We've got a very good business development person in freight who was the ex-British Airways Scottish manager for freight. He's helped us understand and analyse what's happening in the marketplace. Freight's always been a fairly well-developed component of Prestwick's business. We hope it will continue to do so. There's a lot of things happening in the freight market—the growth of aircraft like the 787, which don't have the same belly space capacity for freight. Boeing have over 1,000 aircraft of that type on order, so there will be an undersupply on some of the secondary routes because of that new aircraft. We wish to play—because mostly all the freight that we carry is in freighter-dedicated services, i.e. the freight is not put on passenger aircraft, it's solus on freighter aircraft. Indeed, there's been some growth in that market, which we're capitalising upon. But, out of Prestwick, it's a global market; the oil and gas industry, from Scotland down

to Africa, and indeed to the west coast—sorry, to the USA—in terms of oil and gas—so, the global flows, which Prestwick are playing an important role in.

[491] **Darren Millar:** Thank you, any other questions from Members? Well, I think that draws us to the end of the evidence session. But, we're really grateful for you joining us today, John and Andrew. We'll be sending you a copy of the transcript of today's proceedings. If there are any factual inaccuracies in there, please let us know. Additionally, if there's any further information which you think may be useful to our inquiry that we haven't had the time to discuss, then please send that on as well. I'm sure it will help to inform us as we move forward. But, thank you very much indeed for your time. Thank you.

[492] **Mr Nicholls:** Thank you.

[493] **Mr Miller:** Thank you.

**Cynnig o dan Reol Sefydlog 17.42 i Benderfynu Gwahardd y Cyhoedd
o'r Cyfarfod
Motion under Standing Order 17.42 to Resolve to Exclude the Public
from the Meeting**

Cynnig:

Motion:

bod y pwyllgor yn penderfynu that the committee resolves to gwahardd y cyhoedd o weddill y exclude the public from the cyfarfod yn unol â Rheol Sefydlog remainder of the meeting in 17.42.

accordance with Standing Order 17.42.

Cynigiwyd y cynnig.

Motion moved.

[494] **Darren Millar:** Okay, item 6 then on the agenda—motion under Standing Order 17.42 to resolve to exclude the public from the remainder of our meeting. Does any Member object? There are no objections. So, we'll go into private session.

Derbyniwyd y cynnig.

Motion agreed.

Daeth rhan gyhoeddus y cyfarfod i ben am 12:38.

The public part of the meeting ended at 12:38.