



# FOOD/BEVERAGE AND RETAIL CONCESSION PERFORMANCE ASSESSMENT

DALLAS/FORT WORTH INTERNATIONAL AIRPORT

*Final Presentation*

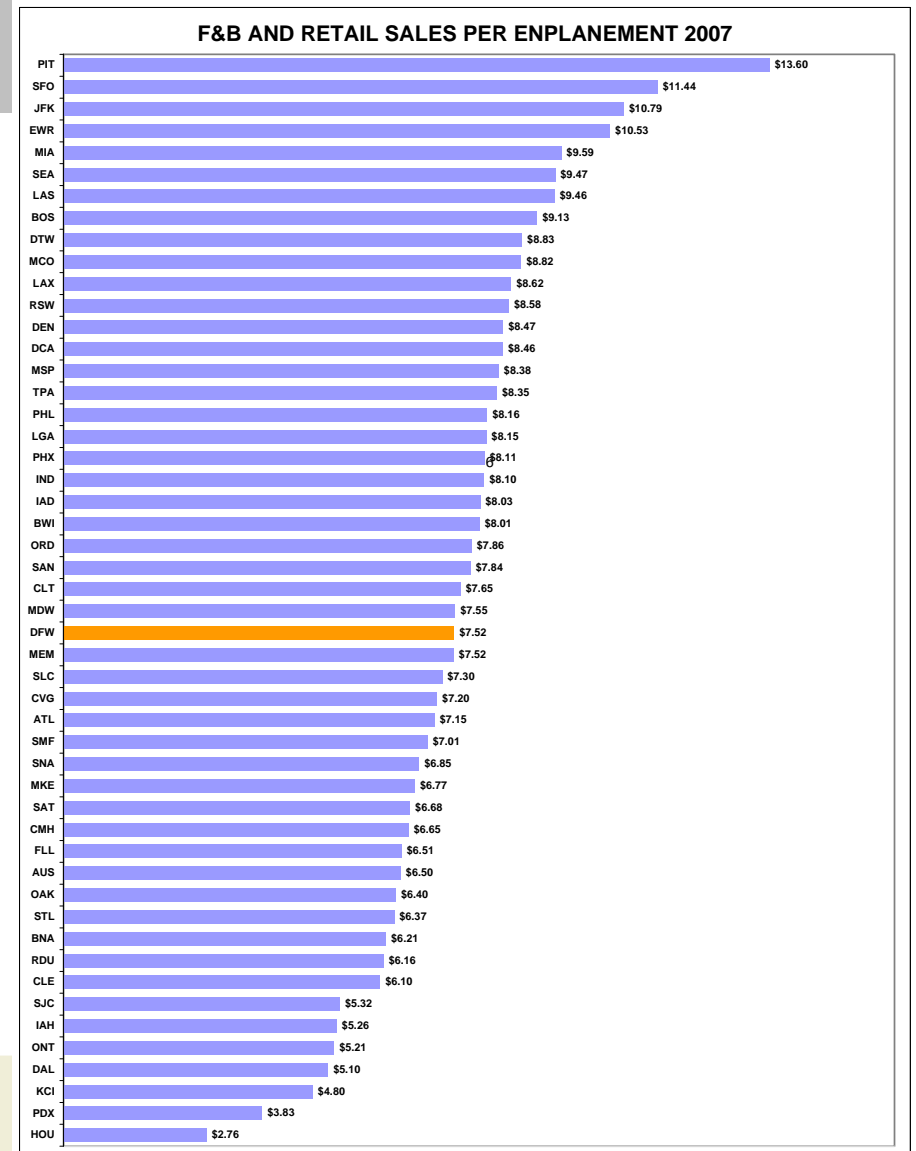
**JACOBS** Consultancy

# Purpose of Study

- Review DFW food/beverage and retail concession financial results and compare to available industry data
- Review DFW concessionaire loans
- Compare key DFW concession contract terms and conditions vs. off-airport and peer airport locations
- Discuss airport concession management structures
- Provide findings on DFW terminal concessionaire construction costs
- Identify good street pricing validation process procedures

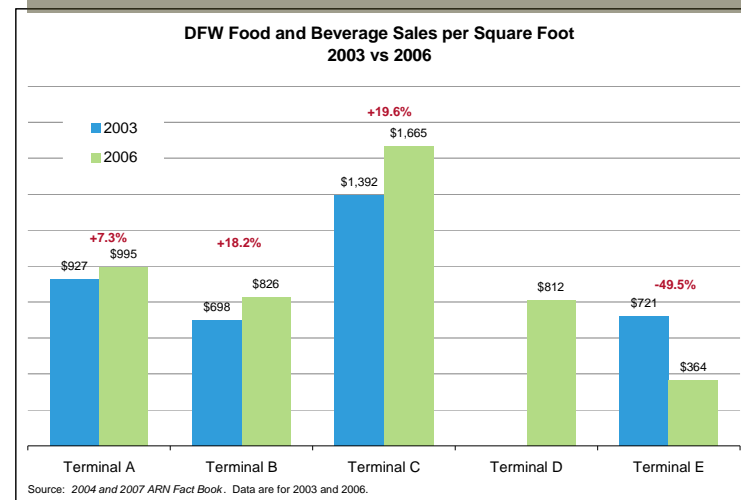
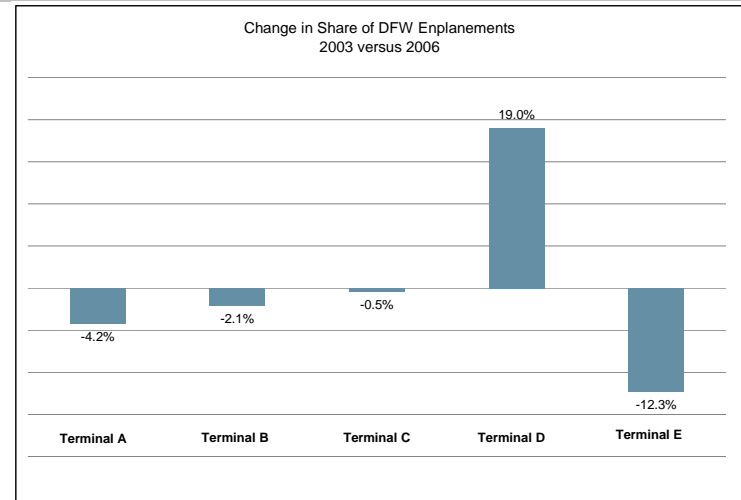
# Introduction

- In 2003, DFW ranked 45 out of the top 50 performing North American airports with sales per enplaned passenger of \$5.43
- By 2007, DFW had improved its ranking to #34 and its sales per enplaned passenger by almost 40% to \$7.52



# Sales History

- The opening of Terminal D resulted in a decrease in passengers in other terminals (see chart, top right).
- Still, between 2003 and 2007 concession sales increased in 3 of the 4 terminals:
  - Terminal A +20%
  - Terminal B +30%
  - Terminal C +12%
- Sales in Terminal E declined by 21% (but rent relief was granted)
- Sales per sq ft also increased in 3 out of 4 terminals (see chart, bottom right).

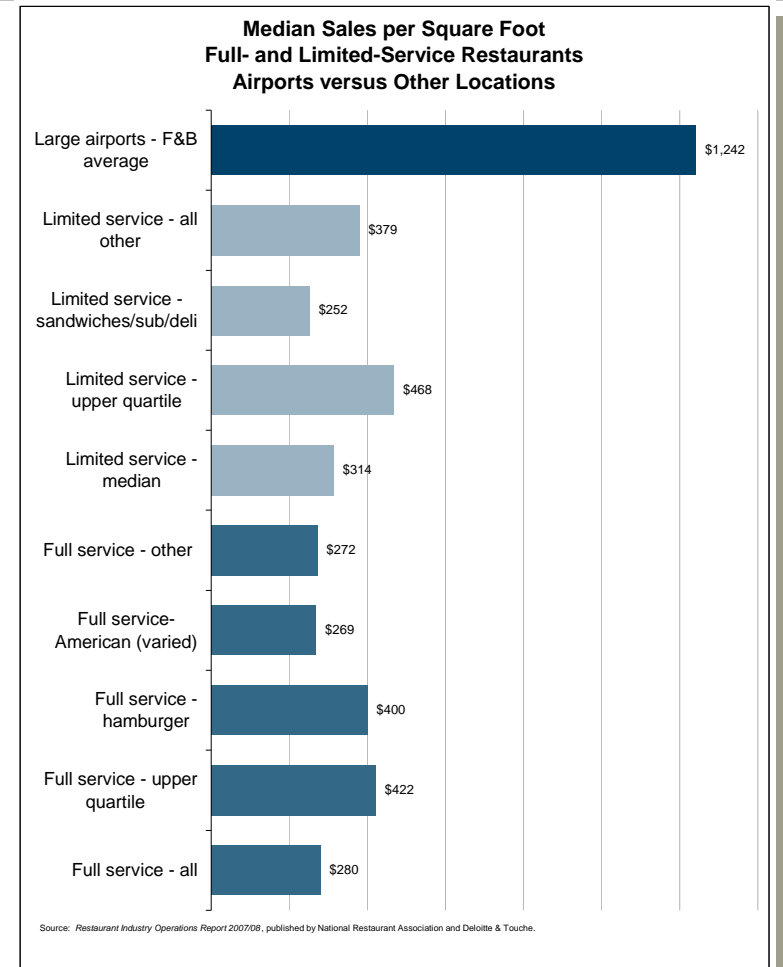


# DFW Concessionaire Survey Responses

- Financial information was received and analyzed for 111 locations
- The concessions were separated into 5 categories
  - Full Service Restaurants (6 locations)
  - Quick Service Restaurants (34 locations)
  - Bars (7 locations)
  - News/Gift (23 locations)
  - Specialty Gift (41 locations)
- Approximately 25 concessionaires (45% of stores) did not respond

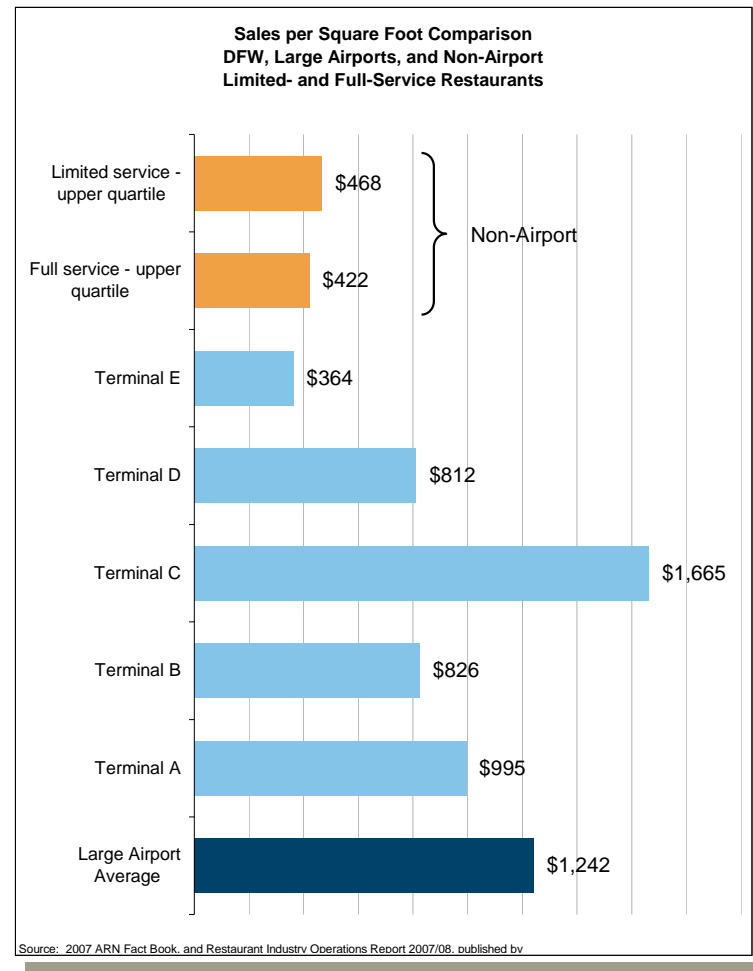
# Full Service Restaurants at DFW

- Average DFW sales per square foot of \$854 is much higher than off-airport locations (see chart, right)
- 85% average ratio of operating expenses to sales is below off-airport locations (Texas all restaurants median is 89.8%; All full service restaurants median is 95.6% )
- Large depreciation and corporate expense allocations result in to operating loss reported at 1 location



# Quick Service Restaurants at DFW

- Average sales per square foot of \$1,082 is much higher than off-airport locations. (see chart, right)
- 79.6% average ratio of operating expenses to sales is below comparable off-airport locations (Texas all restaurants median is 89.8%; Limited service restaurants (multi-unit, company operated) median is 82.0%)
- One multi-location concept reflected poor financial results regardless of location



# Bars at DFW

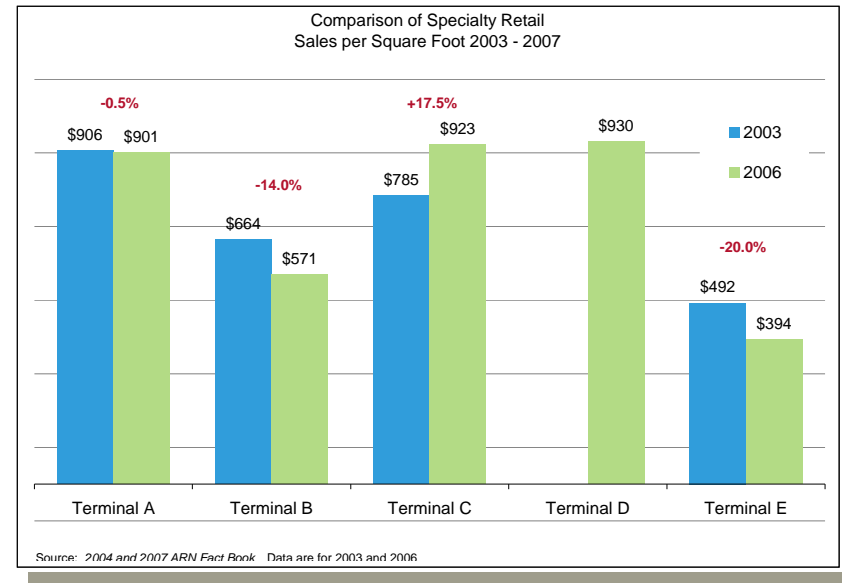
- Average sales per square foot were \$822 in the most recent year
  - Lower sales per sq ft than quick-serve restaurants, but much larger in area
- Bars have higher margins than other F&B facilities, and higher percentage rents
- No off-airport data comparison sources were available
- Sales exceeded total operating expenses at all locations

# News/Gift at DFW

- Average sales per square foot were \$1,455 in the most recent year
- This compares with large airport average of \$1,212.
- No off-airport data comparisons were identified
  - Airport news/gift shops are a unique category with a unique merchandise mix of low-margin news and high-margin gifts
- All concessionaires showed operating profits, but losses were reported for 3 individual locations

# Specialty Retail at DFW

- Average sales per square foot of \$975 is much higher than off-airport locations
  - Median for top 10% of U.S. enclosed shopping centers = \$536)
- 94.9% average ratio of operating expenses to sales is comparable to off-airport locations
  - Barnes & Noble, Body Shop, Brookstone and Fossil annual reports were reviewed
- 3 of the 13 concessionaires that reported in this category showed operating losses



# Concessionaire Financial Results Summary

- Sales per square foot at DFW significantly exceed off-airport restaurant industry medians
- Higher on-airport operating expenses (e.g., rents) are offset by the greater sales potential at airports
- Operating expenses to sales ratios at airport concessions compare favorably with off-airport restaurant and specialty retail locations
- Financial results of comparable off-airport bars and news/gift locations could not be located
- Concessionaire financial results at other airports were not available (proprietary information)

# Comments on Financial Results

- It is not uncommon for some businesses to fail in any shopping environment
- Various controllable factors may contribute to poor financial results (e.g., management, customer service, product quality)
- But, uncontrollable factors (e.g., contract terms, airline gate reassignments, passenger traffic flow) can also contribute
- It is the airport operator's job to create fair and reasonable opportunities for success—but total success cannot be guaranteed

# Loans to DFW Concessionaires

- 31 loans were disclosed by the DFW concessionaires (15 – quick service restaurants; 1 – bars; 10 – news/gift; 5 – specialty retail)
- Range of loan amounts is quite large (\$25,500 - \$1.7M)
- Some concessionaires have multiple loans
- Typical term of loans
  - Full service restaurants – none provided
  - Quick service restaurants – 7 years
  - Bars – insufficient data received
  - News/gift – 5 years
  - Specialty retail – 3 or 5 years

# Comments on Loans

- Lender's loan decision affected by:
  - Perceived risk
  - Cash flow estimates,
  - Profitability projections,
  - Economic factors,
  - Pre-existing business relationships,
  - Collateral and
  - Other factors
- Commercial loans for leasehold improvements typically run 5 – 7 years; Amortization period may be longer requiring balloon payment or renegotiation at end of term
- No difference in on-airport versus off-airport loan conditions could be discerned
- Loan payoff usually has huge result on concessionaires' cash flow
  - Usually 3% to 4% of sales (equal to 20% to 30% of net income)

# Comparisons of DFW Concession Practices to Other Locations

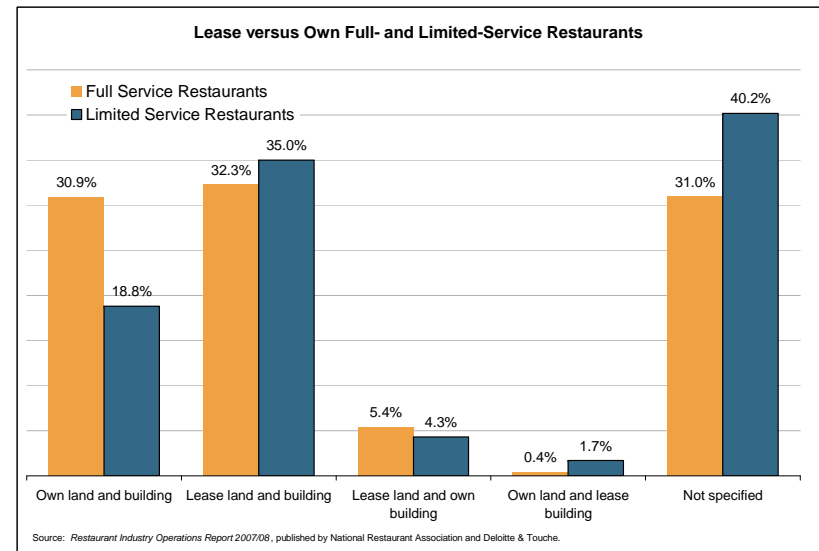
- Information was gathered to compare DFW concession business practices to those at comparable on and off airport locations in the following categories
  1. Rent
  2. Term Length
  3. Hours of Operation
  4. Pricing Policy
  5. Management Structure
  6. Construction Costs

# 1. Rent

- Off-airport percentage rents are often 5% or more below lower than on-airport
  - However, sales are often 3 or 4 times higher on-airport
- Minimum rent is typically much higher on-airport, again offset by higher sales
- Off-airport rents differ greatly based on demographics in the store vicinity
  - e.g., strip center versus super-regional mall or high-end shopping street
- Off-airport rents are typically negotiated (not publicly tendered)
- Rent ranges at DFW were reasonably within the rent ranges reported by the peer airports in all categories

## 2. Term Length Off-Airport

- Restaurants and bars typically carry terms of at least 7 years at off-airport locations
- 20-year terms are common when stand-alone facilities are constructed
- Specialty retail terms may be shorter due to lower capital investment requirements



# Typical Lengths of Term in Airport

	<u>DFW</u>	<u>PEER AIRPORTS</u>
<b>FOOD AND BEVERAGE</b>		
▪ Full Service Restaurants	10 years	7 -10 years
▪ Quick Service Restaurants	5 years	7 -10 years
▪ Bars	5 – 10 years	7 – 10 years
<b>RETAIL</b>		
▪ News/gift	5 years	5 – 7 years
▪ Specialty Retail	5 years	5 – 7 years

*Note: IAH grants 5 – 7 year base terms for quick service restaurants and bars, but also includes 3 one-year term extensions which are typically exercised.*

# 3. Hours of Operation

- DFW hours of operation policy (based on flight departures) is consistent with peer airports
- Hours are considerably shorter in most malls and other shopping centers (e.g., 10 a.m.- 9:30 p.m.)
- Only stand-alone quick service restaurants may have comparable opening times and longer hours
  - Example: McDonalds 0600-2200

## 4. Pricing Policy

- Landlords at off-airport locations do not establish pricing policies for their food/beverage or retail tenants
  - Competition results in price discipline, competitiveness
- DFW's "street + 10%" policy is consistent with many other airports
  - 10 of 23 airports surveyed indicated street pricing + 10% policy
  - 9 had street pricing without markup
  - 4 indicated no street pricing policy (or no pricing policy at all)
- In general, we believe airport industry pricing policies are inconsistently enforced, particularly airports claiming "true street pricing"
- Pricing policies are particularly important where there is limited competition, e.g., dominance by a few major concessionaires.

# 5. Airport Management Structures

- There is no single right or wrong approach – each airport solves for its own goals
- DFW employs a direct leasing program
- Peer airports use each of the following approaches:
  - Direct leasing
  - Developer
  - Multiple prime concessionaires
  - Master concessionaire
- Direct leasing is used by 13 of the top 20 large airports
- 11 airports use a combination of approaches

Concession Management Approach  
20 Large Airports

Rank	Airport	Direct	Primes	Developer	Master
1	ATL		X		
2	ORD	X	X		
3	LAX	X	X		
4	<b>DFW</b>	<b>X</b>			
5	DEN	X			
6	LAS	X	X		
7	JFK	X	X	X	
8	PHX	X	X		
9	MSP	X	X		
10	DTW	X	X		
11	EWR			X	
12	MCO	X	X	X	
13	SFO	X			
14	MIA	X	X	X	
15	PHL			X	
16	SEA		X		
17	CLT		X		
18	IAH		X	X	
19	BOS			X	
20	LGA	X	X	X	
<b>Totals</b>		<b>13</b>	<b>14</b>	<b>8</b>	<b>0</b>

**Total hybrid (two or more management approaches) = 11**

*Source: Jacobs Consultancy from ARN Fact Book 2007 and airport management interviews.*

# Management Structure Primary Pros and Cons

## Top 3 Most Used Approaches

### Direct Leasing

Pros: Most control, higher gross sales, higher revenue, more opportunity for local businesses

Cons: High administrative costs, more management time required

### Prime Operator

Pros: Fewer contracts to manage, concessionaire experienced with subcontracting (e.g., ACDBE)

Cons: Less competition, fewer operators

### Developer

Pros: High customer satisfaction, highest gross sales, wide variety of individual concepts

Cons: Developer fees reduce revenue to Airport

## 6. Construction Costs

- Airport construction costs exceed off-airport construction costs by a significant margin (as much as 50% per industry sources)
  - Delivery restrictions, security requirements, higher life-safety system requirements, other airport requirements raise costs
  - Construction costs vary greatly based on design standards and quality of finishes
- DFW construction costs are generally within or below the peer airports' range of construction costs
- Dallas was ranked 47<sup>th</sup> of 51 major cities in the RSMeans' Construction Cost Indices (CCIs), January 2008, at 84.3% of the national average
  - January 2008 CCIs showed Dallas with a year over year construction cost increase of 4% and a quarterly decrease of 0.1%

# High Build Out Costs are Common

- Increased tenant build-out costs are becoming more of an issue at airports across the U.S. (DFW Terminal D construction costs exceeded those at other DFW Terminals)
  - Higher development standards required in new terminals
  - LEED certification and other environmental requirements
  - Typical ratio used by concessionaires – ½ of first-year projected sales
- Some recent build-out costs per sq ft at U.S. airports:

<b>RETAIL</b>	
<b>DFW (Term D*)</b>	<b>\$464</b>
LAX	\$530
MIA	\$415
IAH	\$390
ORD	\$500
RIC	\$425
DEN	\$435

\*News/Gifts

<b>FOOD &amp; BEVERAGE</b>	
<b>DFW (Term D*)</b>	<b>\$537</b>
LAX	\$680
JFK	\$665
SEA	\$615
MIA	\$525
MEM	\$500
ORD	\$640

\*Quick-Serve

# Recommendations

- ***Term Length*** - Five (5) year contract terms for quick service restaurants without extension options are not typical in the industry. A seven (7) year term for quick service restaurants is recommended.
- ***Construction*** - DFW should periodically review its policies and practices to ensure concessionaires do not spend more than is necessary to provide facilities that meet the DFW quality and durability standards.
- ***Hours of Operation*** - Review of sales during early morning and late evening hours is recommended to determine if sales are adequate to support the required hours of operation. If not, keeping fewer units open may be an option.

# Good Street Pricing Procedures

- **Street Pricing** - Price adjustments based on a recognized economic indicator (e.g., Consumer Price Index) for non-branded concepts may reduce staff monitoring workload and improve turnaround times on price requests, which are important to concessionaires.
  - Indexing provides objective standard where menu, merchandise remains constant
  - Consider portion sizing, when applicable, in comparisons
  - Develop price increase request documentation requirements
  - Enforce non-compliance penalties
  - Establish and document appropriate location comparisons
  - Set price review timeframes with flexibility for unanticipated, significant cost increases as needed
  - For branded units, continue using off-Airport direct comparables



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