

PORT OF SEATTLE
MEMORANDUM

DATE: October 19, 2009
TO: Port Commission
FROM: Tay Yoshitani, Chief Executive Officer
SUBJECT: 2010 Budget Message

INTRODUCTION

During the worst economic recession in decades that brought a significant drop both in passenger traffic at the Airport and container volume at the Seaport, we have taken a proactive approach in managing our costs. We went through a rigorous budget reduction process in preparing the 2009 budget, and then early this year cut an additional \$16.5 million from our expenses through employee furloughs and reductions in discretionary expenses. These cuts were short-term solutions to help meet an immediate need for 2009. For the longer term, we need to focus on cost reduction measures that are more sustainable.

We began our planning process early this year by implementing a zero-based budgeting approach with a goal of reducing our 2009 baseline costs by 5% from the 2009 approved budget. Our intention was not to simply make cuts across the board; rather, we looked for specific less critical activities or functions that could be reduced or eliminated to help meet the goal.

For the past few months, we have reviewed all the key functions for departments and identified significant savings by reducing or eliminating some programs and functions across the organization, implementing the voluntary separation program, modifying our medical benefits program and eliminating over 110 positions, which represent 6.2% of the total workforce. Excluding projected increases in environmental reserve expense for pollution remediation costs, these cost saving measures resulted in a total of over \$15 million or 5.6% reduction in operating and maintenance expenses and over \$6.8 million or 3.2% increase in net operating income from the 2009 approved budget.

At the **Airport**, enplanements were down 4.6% in the first eight months of 2009 and we are projecting a 4.5% decline for the year. We expect the demand for travel will likely lag the recovery, and may take up to 5 years to return to pre-2009 levels. Many airlines have responded by cutting jobs and capacity. As passenger volume and landed weight are down, it puts more pressure on the rates we charge airlines. The top 10 US airlines have lost nearly \$2.5 billion in the first half of 2009, and we expect the financial challenges will persist for the airline industry. While it is still too early to tell how the capacity reductions will affect us, we currently assume no passenger growth for 2010. The overriding goals at the Airport are to manage airline costs and increase non-aeronautical net operating income in the coming year.

The **Seaport** is anticipating 2010 operating revenue to be flat relative to 2009 budget due to a number of offsetting factors. On the growth side, there will be a mid-year CPI increase in the Container Terminal Eagle Rate, a full year of lease revenues at the recently reactivated Terminal 30 Container Terminals and an increase in cruise passengers. An offsetting reduction in revenue will come from the implementation of the Container Terminal Customer Support Plan. Container volumes are expected to decline 5-10% relative to 2009 budgeted volume but be up slightly from the 2009 current full year forecast. Cruise is expecting a 6% growth in the number of passengers. Critical activities in 2010 for the Seaport include delivering on the commitments made in 2009 for the Clean Truck Plan and the Container Terminal Customer Support Plan and continuing the transition and development of Terminal 91 into a multi-use facility.

For the **Real Estate** Division, operating revenue is also expected to be flat relative to the 2009 budget. A continuing soft real estate market could result in higher vacancies at commercial properties and recreational marinas. However, Third Party revenue from the Bell Harbor International Conference Center may increase with the addition of the Maritime Event Center and Terminal 91 Cruise Facility venues and due to more stability in the economy. Key challenges for the Real Estate Division in 2010 will be to manage costs while catching up on maintenance of Real Estate properties and to manage the Eastside Rail Corridor, the acquisition of which is expected to close in late 2009.

The **Capital Development Division** (CDD) delivers projects and provides technical and contracting services in support of the business plans and infrastructure needs of the Port. The three operating divisions of the Port are supported by the CDD based on level of project and contracting services required to support their operations and capital & expense project needs. The services by the departments within the division are demand driven.

Corporate departments reduced over \$4.6 million or 6.4% from the 2009 approved budget through the zero-based budgeting effort. Apart from cutting some programs and services, we are also eliminating 31 FTEs from nine different departments. These cuts are quite deep and broad and the impact can be felt by most departments.

BUSINESS PLAN/ OPERATING BUDGET

The fiscal management of the budget is the cornerstone of our success as a Port. The 2010 operating revenues are budgeted at \$478.1 million, a 1.7 percent decrease. Excluding the \$24.5 million environmental reserve, operating expenses are budgeted at \$257.1 million, a 5.6 percent decrease, while Net Operating Income before Depreciation is \$221.0 million, a 3.2 percent increase. Depreciation Expense is budgeted at \$158.6 million, an increase of \$1.5 million. Net Operating Income after Depreciation is \$38.0 million with environmental reserve and \$62.4 million without environmental reserve, compared to \$57.2 million in the 2009 budget.

Aviation

The Aviation Division manages Aeronautical and Non-aeronautical sides of its business. On the Aeronautical side, the Port's goal is to manage cost in terms of cost per enplanement (CPE). The budgeted 2010 CPE is \$12.61, compared to \$11.90 in the 2009 budget. On the non-aeronautical side, the primary goal is to increase cash flow as measured by net operating income (NOI).

Operating revenues are budgeted at \$354.4 million, a \$5.6 million decrease from the 2009 budget. Revenues from airlines are budgeted to \$209.4 million, a \$7.5 million increase over 2009; and non-airline revenues are budgeted to be \$135.6 million, a \$12.8 million decrease from 2009. Total operating expenses are budgeted at \$184.2 million, a 2.8 percent decrease.

Seaport

The Seaport includes two major groups: Cargo Operations, comprised of Container Operations, Seaport Marketing, and Cruise and Industrial Properties, and Professional and Technical Services, comprised of Environmental Services, Planning, Security, Finance Services, and Seaport Administration. These business and service groups oversee the development and management of cargo and cruise terminals, moorage facilities, and industrial properties connected to these businesses.

Seaport operating revenues are budgeted at \$93.4 million. Total operating expenses are budgeted at \$56.3 million. Net operating income (NOI) before depreciation is \$37.0 million.

Real Estate

The Real Estate Division includes five functional workgroups: Real Estate Development & Planning, Harbor Services, Maintenance, Property Management & Leasing and Pier 69 Facilities Management.

These business and service groups oversee the development and management of various Port assets and vessel moorage facilities. Financial services, project management, facility planning, and environmental services are provided by the Seaport Division.

Real Estate operating revenues are budgeted at \$29.8 million. Total operating expenses are budgeted at \$40.0 million. Net operating income (NOI) before depreciation is -\$10.2 million.

Capital Development

The Capital Development Division (CDD) includes six functional workgroups: Engineering, Port Construction Services, Aviation Project Management Group, Seaport Project Management Group, and Central Procurement Office, and CDD Administration. The CDD delivers projects and provides technical and contracting services in support of the business plans and infrastructure needs of the Port of Seattle. Capital Development operating expenses are budgeted at \$7.4 million.

Corporate, Professional and Technical Services

The three operating divisions of the Port are supported by a number of functional departments as well as service groups, including the Port's Police Department. These functional and service groups allocate their expenses according to the level of service they provide to the divisions. Corporate operating expenses are budgeted at \$72.0 million.

CAPITAL BUDGET

The total capital budget for 2010 is \$414.0 million and the five year capital improvement program is \$1.4 billion, which reflects the Port's continuing commitment to promoting regional economic activity through the investment in the development, expansion, and renewal of Port facilities that supports the Port's Business Plan and Green Initiative.

TAX LEVY

The Port's 2010 Budget assumes a levy amount of \$75.9 million, which will remain flat at the 2009 level; however, the tax levy rate is increased by 13.04% to \$0.2227 per \$1000 of assessed value from \$0.1970. The tax levy, Section IV of this document provides details on the uses of the Port's levy.

SUMMARY

The coming year will be challenging, but there are also exciting new investments underway that will further broaden business opportunities and improve the environment within the local community. The Sound Transit link to the airport will open by the end of this year; the construction of the Rental Car Facility is well underway; the development of Terminal 91 into a multi-use facility will continue; and the East Rail Corridor acquisition will be completed in the next few months.

With the right tools, resources and our highly capable employees, we are well positioned to continue to navigate through the economic challenges we face and build on our past record of success. The Port's annual budget is an essential management tool to sustain our businesses. I appreciate your continued support and commitment on the 2010 budget.

TABLE I-1: 2010 BUDGET SUMMARY

		(in 000's)					
OPERATING BUDGET		Aviation	Seaport	Corporate	Capital	Real Estate	Total
Operating Revenues		\$345,013	\$90,834	\$502		\$29,798	\$466,147
Security Reimbursement		\$1,025	2,535				3,560
Fuel Hydrant Facility		\$8,352					8,352
Total Operating Revenues		\$354,390	\$93,369	\$502	\$0	\$29,798	478,059
Operating and Maintenance Expense	3	125,113	27,962		0	\$27,147	180,222
Corporate Administrative Expense		40,983	10,472	1,015		4,539	57,009
Law Enforcement Costs	1	15,170	3,391			1,269	19,830
Environmental Reserve		2,971	14,500	\$0		\$7,001	24,471
Total Operating Expense		184,237	56,324	1,015	0	39,956	281,531
Net Operating Income before Depreciation		\$170,154	\$37,045	(\$513)	\$0	(\$10,158)	\$196,528
Depreciation		116,933	31,974	9		\$9,659	158,575
Net Operating Income after Depreciation		\$53,221	\$5,070	(\$522)	\$0	(\$19,816)	\$37,953
Revenue Bond Interest Expense		(134,889)	(12,821)			(2,360)	(150,070)
Interest Income		11,896	3,819			72	15,788
Other Non-Op Income (Expense)		(822)	(1,320)			(74)	(2,217)
Ad Valorem Tax Levy Revenue	2	7,035	47,371			21,493	75,899
Grants and Donations		37,208	12,944			0	50,152
Passenger Facility Charges & related Interest Income		61,273	0			0	61,273
Customer Facility Charge		28,438	-			0	28,438
PFC Bond Interest & Amortization		(10,497)	-			0	(10,497)
CFC Bond Interest & Amortization		0	-			0	0
G.O. Bond Interest & Amortization		0	(13,125)			(1,307)	(14,432)
Public Asset Expense		(9,575)	(36,289)			0	(45,864)
Net Non-operating		(9,933)	580	0	0	17,824	8,471
Revenue Over Expense		43,289	5,650	(522)	\$0	(\$1,993)	\$46,424
CAPITAL BUDGET		Aviation	Seaport	Corporate	Capital	Real Estate	Total
Committed		\$275,832	\$30,618	\$10,514	\$0	\$15,346	\$332,310
Business Plan Prospective		61,134	10,750	4,175	0	5,620	81,679
Total		\$336,966	\$41,368	\$14,689	\$0	\$20,966	\$413,989
EMPLOYEES		Aviation	Seaport	Corporate	Capital	Real Estate	Total
Total FTE's		746.1	60.4	450.2	268.0	154.8	1,679.5
CASH FLOW SUMMARY							
Beginning balance cash and investments		\$783,626					
Cash Receipts:	2010	% Total	Cash Expenditures:			2010	% Total
Revenues	\$478,059	52%	O&M expense		\$180,222	18%	
Interest Receipts	24,372	3%	Corporate Administrative Expense		57,009	6%	
Proceeds from Bond Issues	200,000	22%	Law Enforcement Costs		19,830	2%	
Grants	50,152	5%	Environmental Reserve		24,471	2%	
Tax levy	75,899	8%	Interest Payments		192,818	20%	
Passenger Facility Charges	61,273	7%	Other Expenses		23,706	2%	
Rental Car Customer Facility Charges	28,438	3%	Bond Redemptions		107,715	11%	
Other Receipts	932	0%	Public Asset Expense		45,864	5%	
Total Cash Receipts	\$919,127	100%	Committed Capital Expenditures		332,310	34%	
Total Cash Expenditures					\$983,945	100%	
Increase (Decrease) of cash during the year	(\$64,818)						
Ending balance cash & investments	\$718,807						

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Notes:

- 1) Budget 2010 law enforcement costs includes Police costs.
- 2) Portions of Levy has non-Seaport use, see Tax Levy Section IV for detail.
- 3) Capital Development Group allocates expenses to the Aviation, Seaport and Real Estate divisions.