PORT OF OAKLAND

Development of FY 2019 Operating and Capital Budget

Board of Port Commissioners

March 22, 2018

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Purpose of Presentation

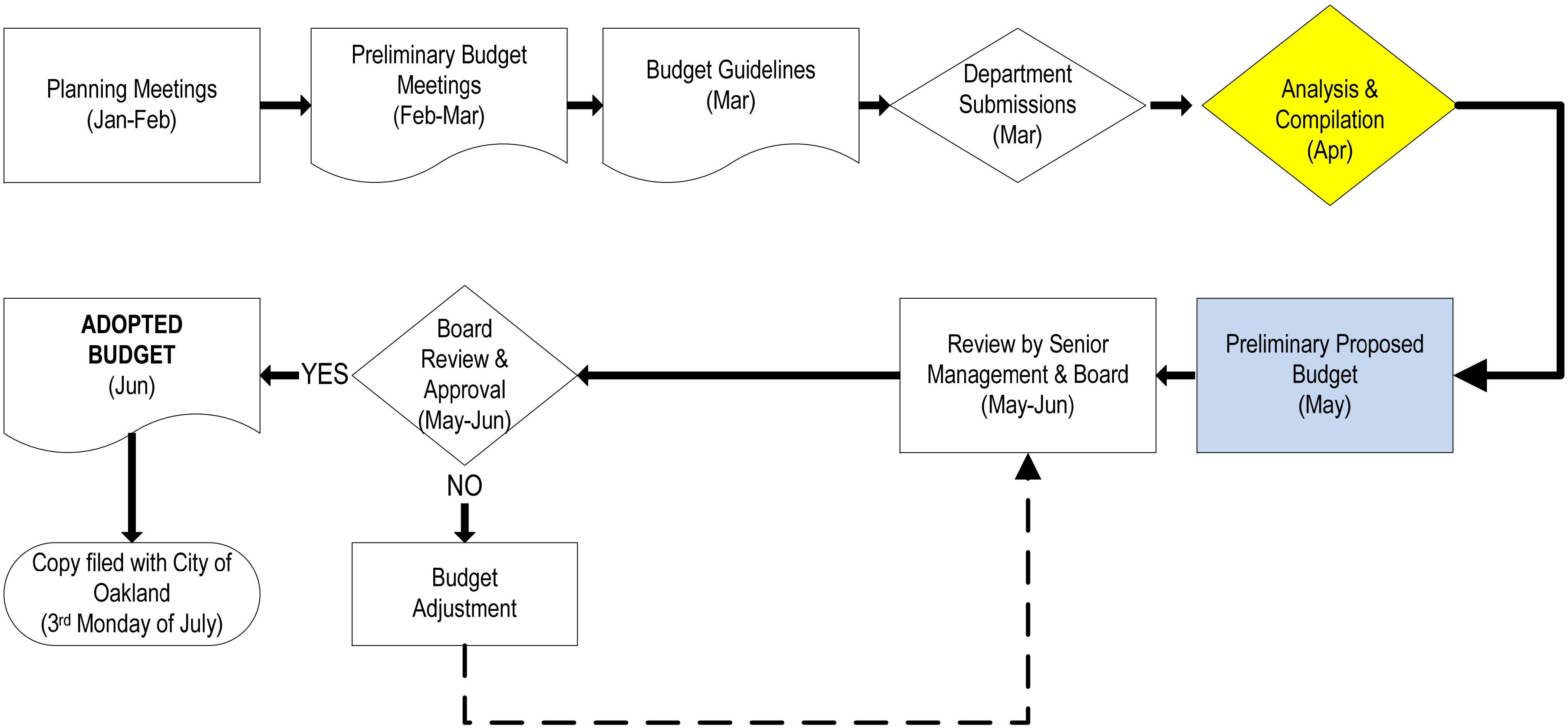
1. Provide overview of the Port budget process and budget

2. Discuss key factors influencing the development of FY 2019 Budget

3. Receive Board feedback on key budget objectives and assumptions

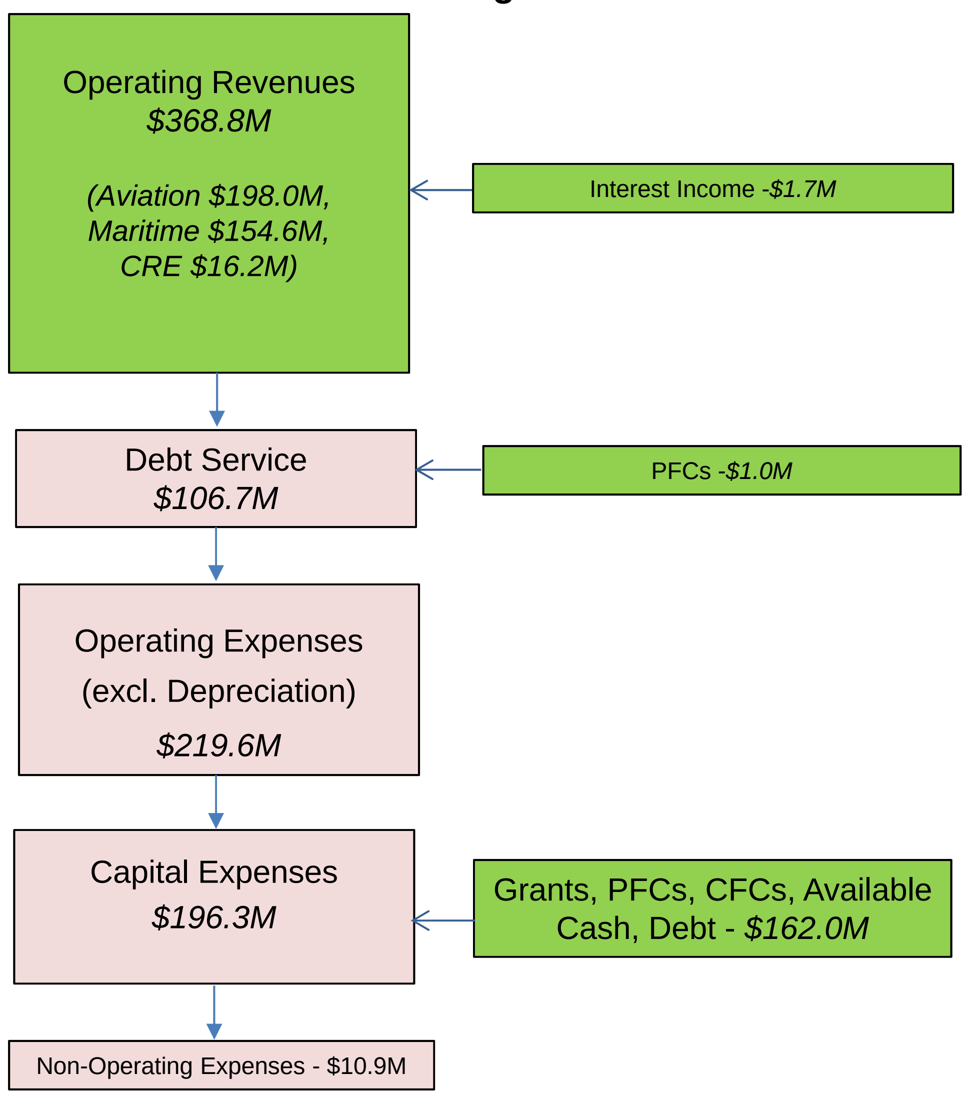
1. Overview of the Port Budget Process and Budget

Budget Process Overview



Operating revenues supplemented by grants, PFCs and CFCs pay for debt service, operating expenses and capital expenses.

FY 2018 Budget



Sources of Funds

Uses of Funds

CFC = Customer Facility Charges collected by rental car companies

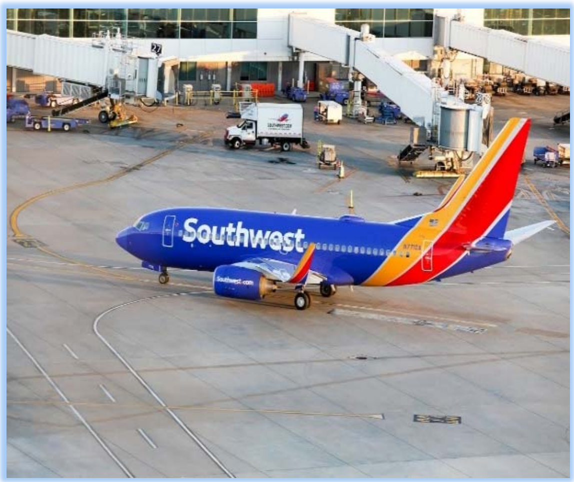
PFC = Passenger Facility Charges collected by the airlines

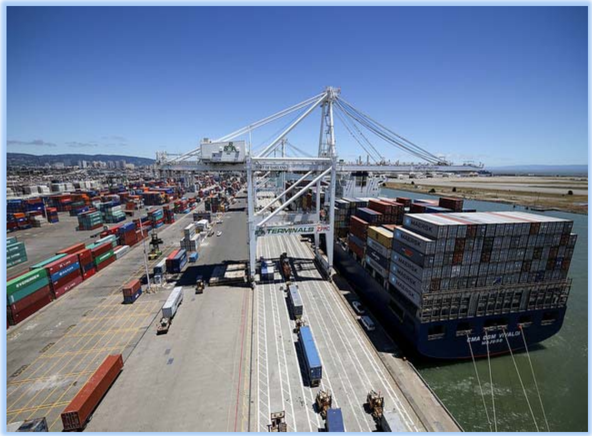
2. Key Factors Influencing the Development of FY 2019 Budget

The Port primarily serves as a landlord and manages three business lines.

Oakland Int'l Airport

- 13 million passengers
- 65 non-stop destinations*
- 14 domestic and international airlines*
- 4th largest airport in CA
- FY17 revenues = $191M





Oakland Seaport

- 2.4 million TEUs
- 4 marine terminals
- 22 international and domestic shipping lines
- Top 10 seaport in US
- FY17 revenues = $151M

Commercial Real Estate

- Jack London Square, Oak Bus Park, Embarcadero Cove
- 100 tenants
- 3 million visitors
- 630 acres of public access and open space
- FY17 revenues = $17M

** Operating in July 2018 (peak schedule with seasonal service and new routes)*

The Port possesses solid fundamentals, providing resiliency to Port revenues.

- The Port is geographically well-positioned and services a healthy local economy.
  - 87% of Airport traffic is "origin and destination"; closest airport to the majority of the population and downtown San Francisco; minimal weather delays
  - 85% of Maritime cargo is for local destinations; balanced import-export mix; shorter transit times to Asia; Class I railroad connections
- The three business lines provide diversity and stability to Port revenues.

The Port's financial position has improved significantly since the lows of 2009, but challenges persist.

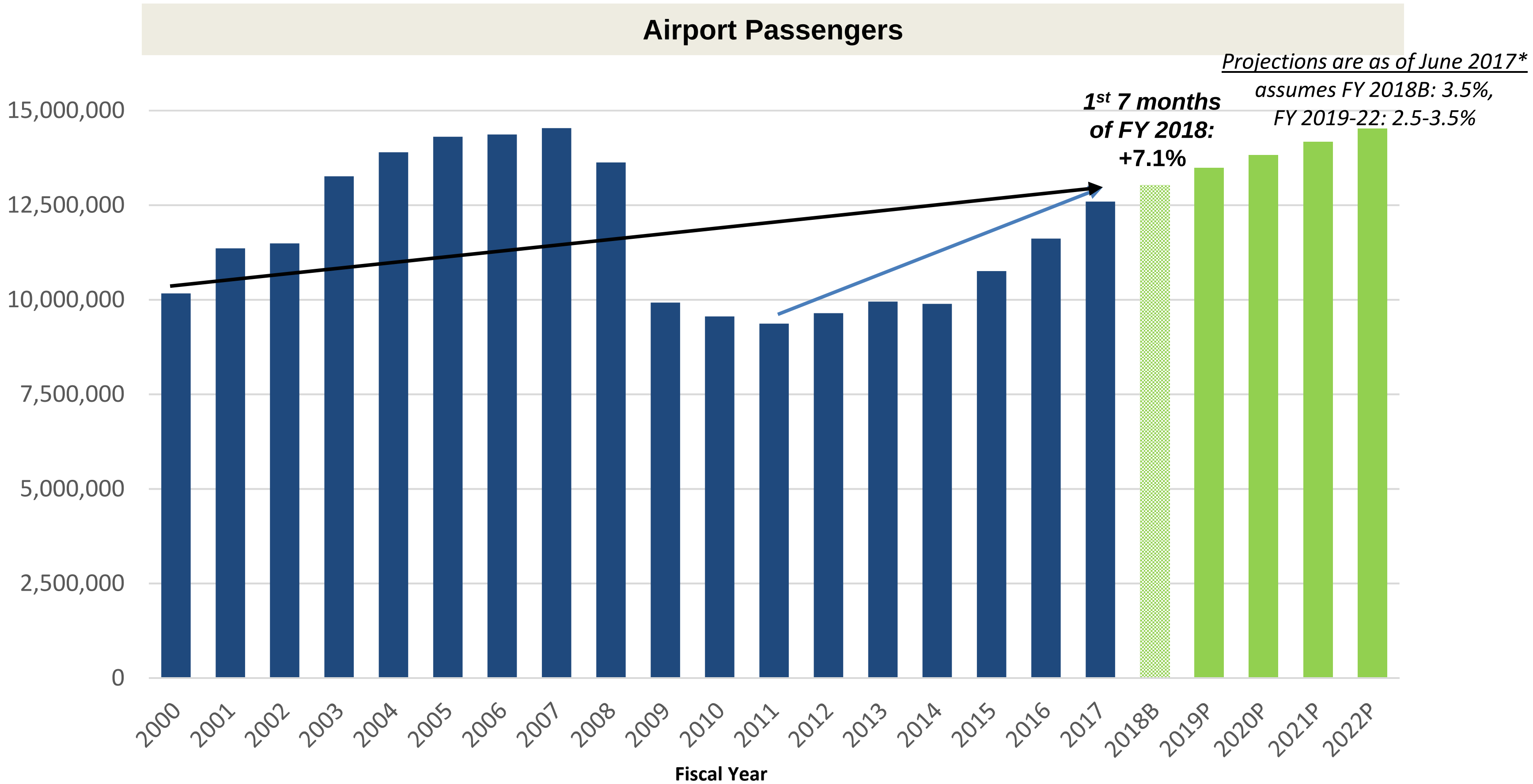
Accomplishments

- Airport traffic has rebounded significantly in the past 4 years
- Maritime has retained all cargo and maintained revenues in light of major terminal operator ceasing operations
- Port has reduced aggregate debt service payments by $250M
- Port's liquidity position is back to airport/seaport industry standards
- Major capital improvements recently completed: Terminal 1 and IAB renovations, and runway rehabilitation
- Capital investments by tenants demonstrate commitment to Port: Trapac, Cool Port, Centerpoint Oakland Development I, crane raising

Challenges

- Operating income is flat over the last 5 years
- Maritime revenues and TEUs in FY 2017 are flat to FY 2011, but Maritime operating expenses during this time are up 47%
- Maritime revenues are sufficient to cover only operating expenses and debt service
- Increase in passengers is not currently resulting in economies of scale. Passengers have increased 17% over the last two years, but Airport Cost per Enplaned Passenger (CPE) has risen 8%; CPE must be controlled to maintain competitiveness
- Pension, healthcare, security, and regulatory costs continue to rise significantly; Port personnel costs are a lifetime obligation
- Industry factors such as larger planes and ships, and increased competition among airports and seaports must be addressed
- Aging infrastructure must be addressed

Passenger level is approaching the highs of 10 years ago; and over a 17-year time frame has averaged 1.3% per year.

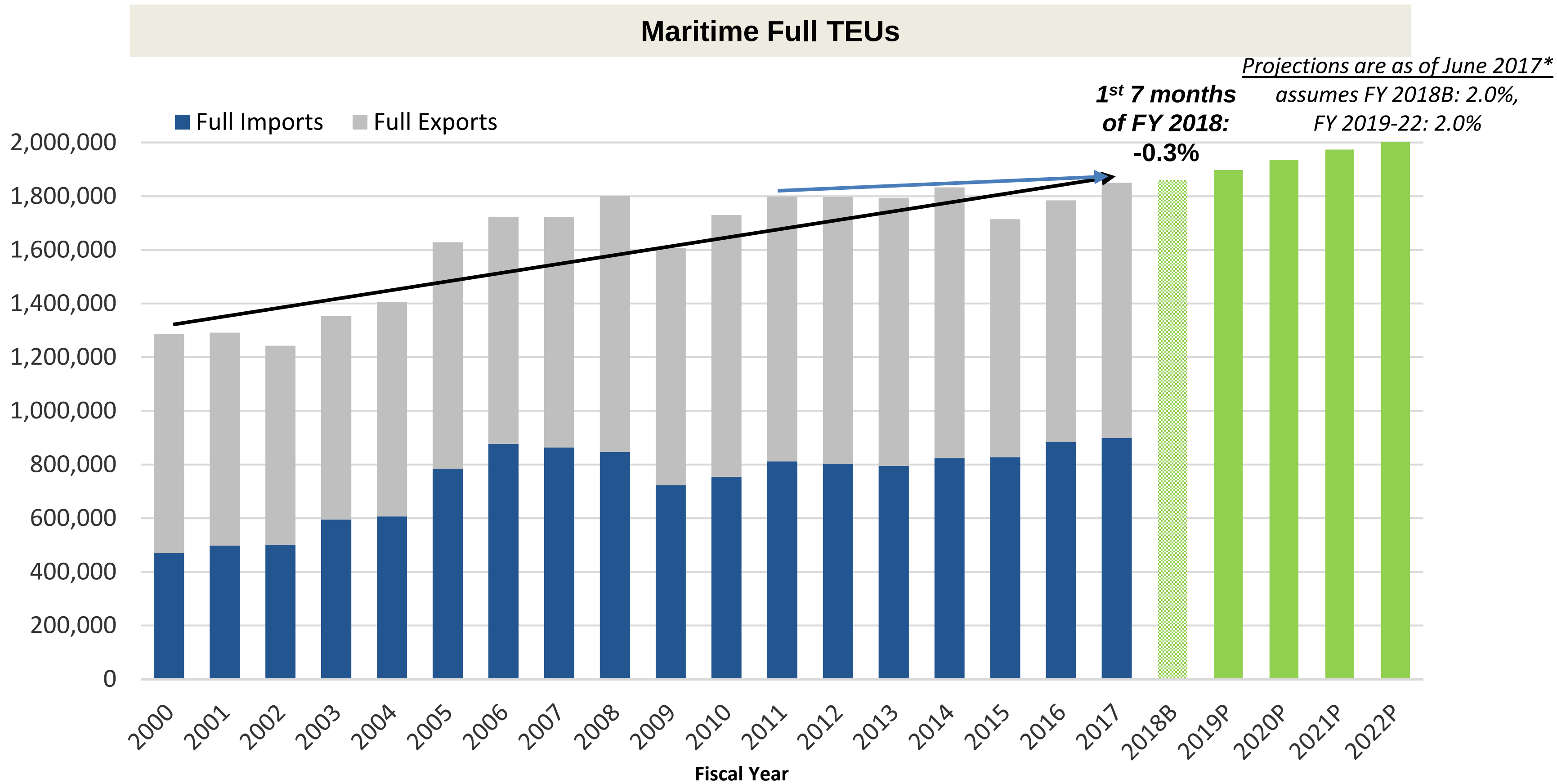


- Airport passengers is not directly correlated to Port revenues, but is an important indicator of Aviation health.

Compound Annual Growth Rate	
FY 2011 – 2017	5.1%
FY 2000 – 2017	1.3%

** Currently in the process of being updated; subject to change.*

Full TEUs has been relatively flat since FY 2011; and over a 17-year time frame has averaged 2.2% per year.



- ❑ Cargo volume is not directly correlated to Port revenues, but is an important indicator of Maritime health.

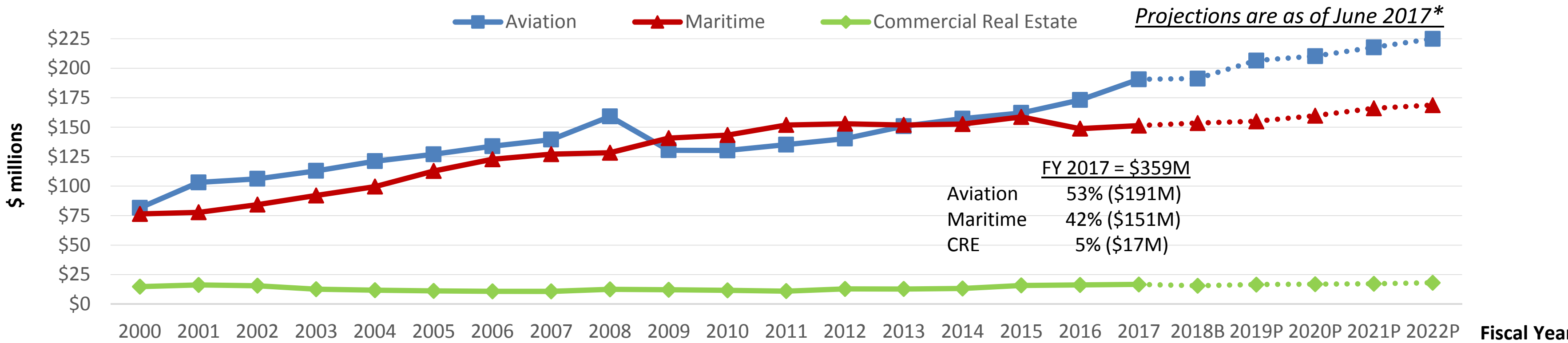
Compound Annual Growth Rate

	Full	Full & Empty
FY 2011 – 2017	0.5%	0.1%
FY 2000 – 2017	2.2%	2.0%

** Currently in the process of being updated; subject to change.*

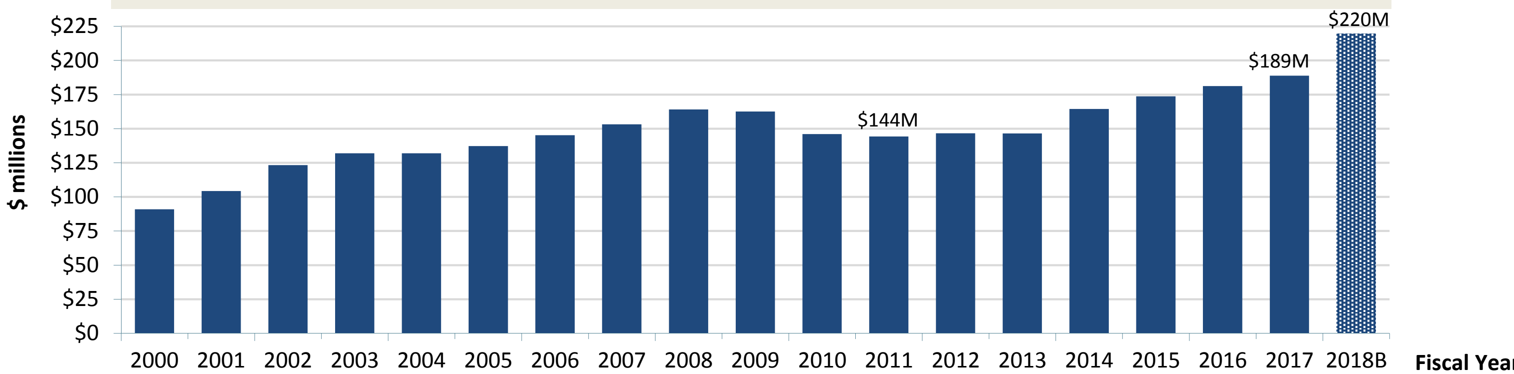
Operating revenues have increased in aggregate 20% since FY 2011, driven by Aviation and CRE revenue growth.

Operating Revenues by Business Line



Compound Annual Growth Rate	Aviation	Maritime	CRE	Total
FY 2011 – 2017	**5.9%**	**0.0%**	**7.2%**	**3.1%**
FY 2000 – 2017	5.1%	4.1%	0.7%	4.4%

Operating Expenses** (excl. Depreciation)

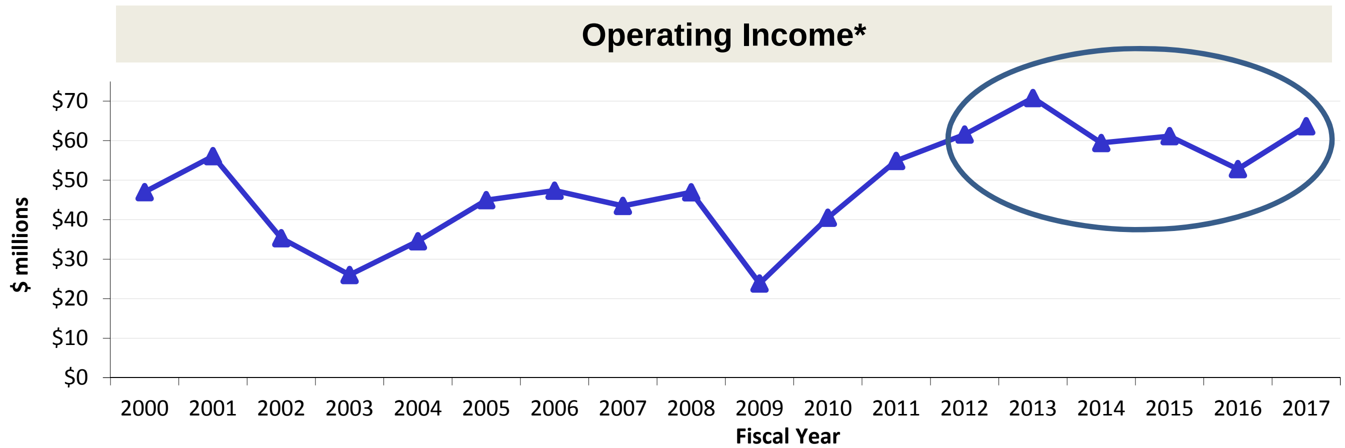


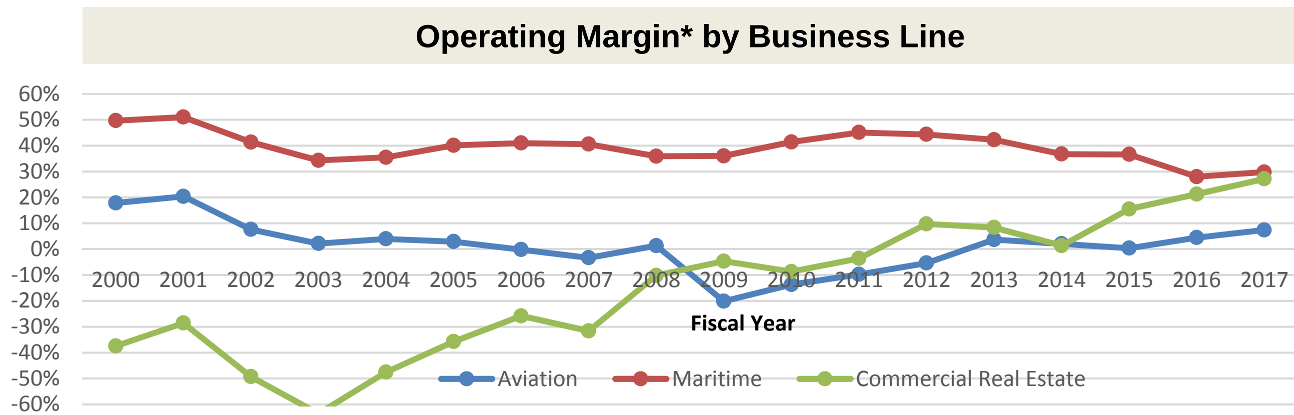
Compound Annual Growth Rate	Aviation	Maritime	CRE	Total
FY 2011 – 2017	**3.9%**	**6.6%**	**3.0%**	**4.6%**
FY 2000 – 2017	5.2%	5.0%	(2.5)%	4.4%

** Currently in the process of being updated; subject to change.*

*** See Slide 13 for footnote.*

Operating income is stagnant as operating revenues struggle to keep pace with increases in operating expenses.



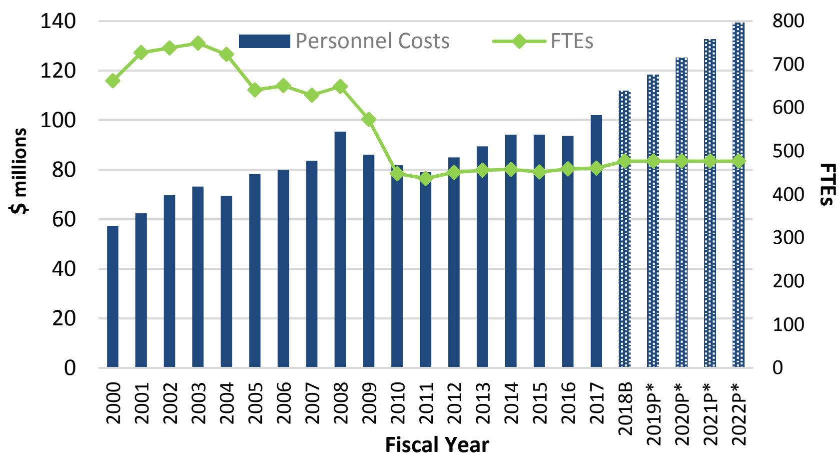


- ❑ **Operating income** measures the amount of earnings generated by the day-to-day business activities and correspondingly takes into account operating and capital costs (depreciation) necessary to generate the operating revenues. Operating income measures earnings at the time they are earned, which differs from timing of cash receipts and payments.
- ❑ **Operating margin** measures earnings as a % of revenues.

** Beginning with FY 2016, rental car busing costs (which are paid for with Customer Facility Charges) are no longer recorded as operating expenses and have been reclassified to non-operating expenses. FY 2008-2015 expenses have been adjusted to exclude rental car busing costs.*

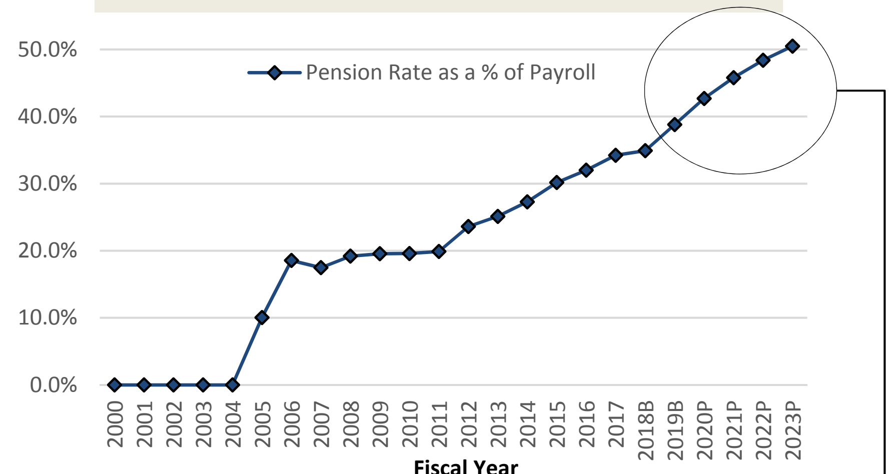
Personnel and security costs have increased and are expected to continue to rise significantly.

Personnel Costs and FTES



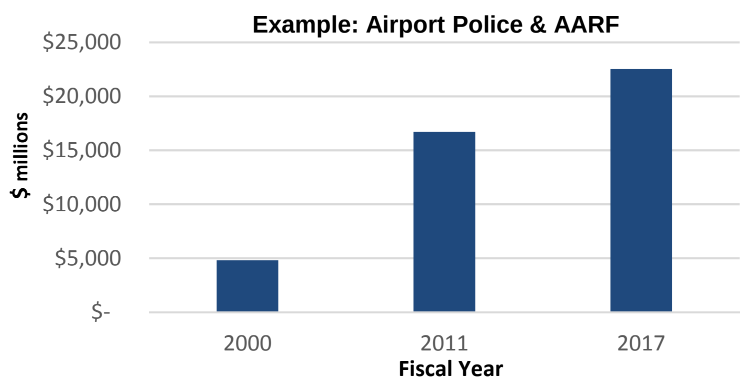
FTEs	(30%) (2000-2017)
Personnel Costs	+78% (2000-2017)

Pension Costs



Pension projections are based on CalPERS actuarial report dated July 2017

Security



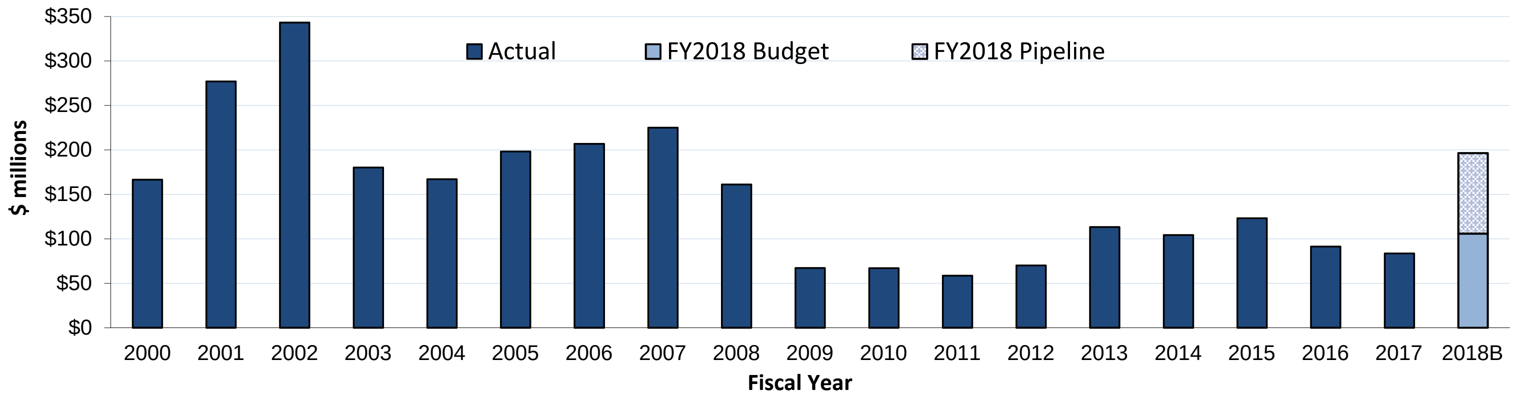
Compound Annual Growth Rate 2000-17 = 9.5%

** Currently in the process of being updated; subject to change.*

Operating performance must be strong so that future capital investments can continue to be made.

Port Capital Projects	Est. Costs	Est. Completion
Airport Perimeter Dike	~ $64M	Summer 2021
Various Terminal Improvements (e.g. TSA recapitalization, restrooms, wall window)	~ $30M	varies
Cool Port Infrastructure	~ $12M	Summer 2018
Various Utility Upgrades	~ $40M	varies

Port Capital Expenditures



At the Seaport, significant private investment is underway:
- Trapac Terminal Expansion and improvements (~$50M)
- Cool Port Oakland (~$90M)
- Centerpoint Oakland Development I (~$50M)
- Crane raising (~$20M)

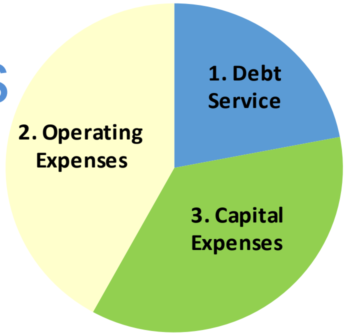
3. Key Budget Objectives and Assumptions

Key Budget Objectives

- Cash/Liquidity/Margins: Provide flexibility and liquidity to protect against inherent operational, financial, political, and economic uncertainties
- Debt: Maintain discipline of paying down portion of outstanding commercial paper notes
- Operating: Demonstrate smart, prudent and thoughtful budgeting to support long-term financial strength, resiliency and sustainability
- Investments: Strategically identify, prioritize and appropriately plan major capital projects
- Financial metrics:
  - Improve operating income
  - Achieve minimum Debt Service Coverage Ratio of 1.50-1.60x
  - Achieve minimum June 30, 2019 cash balance* of around $150 million (excluding Board Reserves, PFC & CFC balance, Bond reserves and contractor retention held in escrow)
  - Maintain Board Reserves, consistent with policy, of approximately $72 million

* June 30 cash balance is used to pay upcoming November 1 debt payment of $57 million, construction contracts already executed, 5-Year Capital Improvement Plan, day-to-day operating expenses and unfunded liabilities; balance also includes contractor retention and security deposits.

Preliminary Key Budget Assumptions

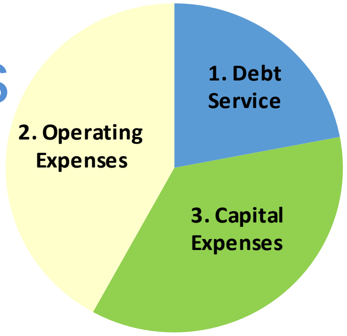


1. Debt Service Expenses

- Bond debt service payments will be $93 million in FY 2019
  - FY 2019 debt service is $9 million less, due to summer 2017 bond refunding
- Increase repayment of outstanding commercial paper from $4 million to $6-8 million
  - $105 million of commercial paper notes outstanding as of March 2018 ($44 million Maritime, $52 million Aviation PFC-eligible, $9 million Aviation)
  - Some commercial paper notes have been outstanding for 20 years
- Minimum debt service coverage ratio* of 1.50-1.60x:
  - Provides minimum operating financial cushion
  - Continues progress on capital improvements
  - Maintains sufficient liquidity
  - Preserves credit ratings
  - Complies with Port debt policy

* Debt service coverage ratio reflects the financial cushion to make debt service payments. That is, it measures the amount of operating revenues remaining after payment of operating expenses and compares it to debt service payments.

Preliminary Key Budget Assumptions

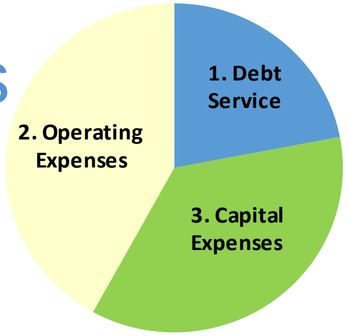


2a. Operating Expenses - Personnel

- No change in overall staffing levels, other than some possible considerations at the Airport. Instead prioritization shall be:
  - Review vacancies and ensure that the most effective and needed positions are identified and appropriately placed
  - Prioritize filling vacancies (41 vacancies as of March 2018)
  - Focus on smart and skilled management to achieve a high performing workforce

❖ *The Port will not be able to sustain the projected significant increases in pension and medical costs (including retiree medical) unless we proactively manage our current and future personnel costs*

Preliminary Key Budget Assumptions

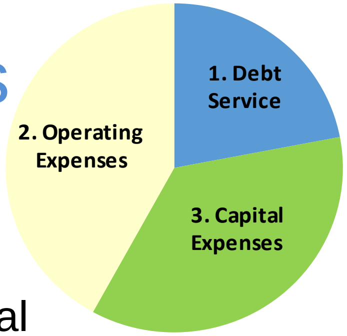


2. Operating Expenses – Non-Personnel

- Non-personnel budgets have been requested to remain in general flat with the following possible exceptions:
  - Contractually obligated increases, with no discretion and no reasonable offset
  - Maintenance and repairs, life-safety, environmental and regulatory matters
  - Costs are recovered in the same year (e.g. Airline Rates and Charges)
  - Support of longer-term planning efforts

- *Management will continue to closely manage, prioritize, and be prudent with expenditures, focused on long-term financial sustainability and spending smartly.*
- *Management will carefully evaluate actual rather than budgeted expenses, and review management practices, so that the Port's financial planning practices can continue to improve.*

Preliminary Key Budget Assumptions



3. Capital Expenses

- *Aviation* - With major projects substantially completed in FY 2018, the focus in FY 2019 will be on Airport perimeter dike, various terminal improvements, utility upgrades, security enhancements, and longer-term planning efforts (capital expenses for FY 2019 anticipated to be significantly lower, given normal capital planning cycle).

- *Maritime* – As a landlord seaport, and with limited cash flow, most of the development is being undertaken by private parties (Cool Port, Centerpoint Oakland). Port staff will continue to focus on related-infrastructure improvements to support private investment, as well as crane-raising, utility upgrade and security initiatives.

- Continue to focus on life-safety, regulatory, and revenue maintenance projects.

❖ *Capital budget always takes into account resources and balancing available cash against preserving liquidity and financial flexibility.*

❖ *Capital investments must be strategic, appropriately prioritized and well-planned for the Port to be successful in achieving long-term financial sustainability.*

❖ *Management will carefully evaluate actual rather than budgeted expenses, and review management practices, so that the Port's financial planning practices can continue to improve.*

Schedule

March 22	Board Update #1 – *Overview, Key Factors, Objectives and Assumptions*
May 10	Board Update #2 – *Key Assumptions and Preliminary Budget Numbers*
June 28	Request Board adoption of FY 2019 Operating and Capital Budgets
July 5	Submit Adopted FY 2019 Budget to City