

## *Original Paper*

# Commercialization and Privatization in the Melbourne Airport

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### **Abstract**

*Airport management is now become a more business-like market. The research of commercialization and privatization in the Melbourne Airport focuses on a study of airport management and the strategies used in facing the growing aviation transport demand and the airport competitions. The combination of theoretical analysis and case study of Melbourne Airport is used in this paper. According to the comparing in reports, privatization, strategies, it shows that the privatization process in Melbourne Airport success and it could be a good example for other Australian airports.*

### **Keywords**

*airport managing, public investment, Melbourne Airport, commercialization, privatization*

### **1. Introduction**

With the multifunctional construct of airports the past decades, airports are now becoming not only a spot of the public transportation but also a profit growth spot of the economy. As an essential part of the air transport system, in considering many features such as safety consideration, most airports are owned by the local government or running and operating in various forms by the state.

By producing far more important roles in economic, tourist and productive, there occurs some more forms in airport marketing including operating by regional government and private investments. The main problems for the new airport operators occurred in the contradictions between investments and policies. There are some new issues for the new airport operators as well such as airport competitions in the regional area, marketing strategies.

After years of derivations and demonstrations, airport privatizations are finally considered to be an effective way to rebuilt or improve airports to meet the growing demand. Some airports came through the privatization process and became a hub of both a transport center and an economy center. However, not all the privatizations have been successful due to a number of different reasons. Some airports

finally become commercialized but not totally private organizations.

This paper describes the background of airport privatization from an international aspect and the privatization process conducted in Australia. This paper also investigates the detail privatization process of Melbourne Airport, which is the second busiest airport in Australia. The comparing with a totally privatized airport and a commercialized but partly privatized airport shows the status of Melbourne Airport's privatization status. The study from Melbourne Airport's annual reports focuses on the marketing strategies it adopted to reduce the government-related revenues and make more profits from the non-aeronautical services. The study also shows the strategies that Melbourne Airports used in the competition with other airports. Australian airports are still ongoing a phased privatization process. The study of Melbourne airports assesses how success has it done and provides a case study to other Australian airports.

## **2. Methods**

The research methodology is a combination of theoretical analysis and case study. The privatization and commercialization of airport is a complex process. The reforming and changing brings up many other issues including business transformations, government divestment, privately or partly privately ownership of airports.

Using the theoretical analysis, the clearly analyzing will help to understand the main cause of privatization and commercialization. With the long process of privatization and commercialization, the new airport owners will face with many new challenges and new competitions from both the local competitors and the international investments.

Using the cases study, the representative airport from Australia will show the success and failure of the privatization and commercialization. The strategies adopted by the airports will show how the culture and economic level has an impact one the privatization and commercialization process.

Using the study, the similarities and difference between representative airports shows how the environment, policy and regular, economic level have influence airports on their strategies developing.

## **3. Background**

### *3.1 Privatization of Airports*

In the traditional airport ownership and management model, all airports are traditionally owned by the public sector by many different forms such as wholly owned or holding companies (Graham, 2008). The public sector includes both local and national governments. Before the raising of privately or partially privately owned airports in 1990s, the only privately owned airports are small General Aviation (GA) or aero club airports (Graham, 2008). After the privatization on airlines, many public owners began to view the airport management more like a commercial enterprises with a more

business-like management. It is the beginning of airports commercialization (Graham, 2008).

The airport privatization process started about ten years later after the beginning of airports commercialization. By transferring economic activities or controls from the public to the private sector, which means the privatization, airports will reduce the needs from public sector investments and provide access to the commercial markets. Also, the privatization promotes more competitions. Due to the environment limitations, policy and regulation controls and other government considerations, the privatization process is not simply defined as the transfer of ownership to private organizations. The privatization model is now classifying into five types: share flotation, trade sale, concession, project finance privatization and management contract.

Every continent is facing different choices in the process of airport privatization process. Each country has its unique considerations. The Europe, especially the UK, is leading the process of airport privatization. The USA is slowly facing the privatization. Australia and New Zealand is under a phased privatization process.

### *3.2 The Melbourne Airport*

Melbourne Airport, which is also called Melbourne Tullamarine Airport, is the second busiest airport in Australia serving the Melbourne area. Melbourne Airport is also the only international airport among four airports serving the Melbourne area. It is called by Tullamarine Airport because of its location near the Tullamarine suburb. This calling also distinguish it from the other Melbourne located airports: Essendon, Avalon and Moorabbin.

Essendon Airport was officially designed and serviced as the main airport in Melbourne in 1950. Due to the limitation of expansion space and the growing numbers of passengers and the appearance of large airplanes, Essendon Airport could not meet the demand of the growing domestic and international aviation market. A new designed larger international airport, which is the later Melbourne Airport, was built in the north Tullamarine suburb in 1959.

In 1980s, all of the major airports in Australia were owned and operated by the Federal Government. The Federal Airports Corporation (FAC) was founded in 1988 to reform the public sector and increase the scope for competition. The FAC conducted the Airport Privatization Program in 1994. The aim of the program was to “improve the efficiency of airports investment and operations in the interests of users and the general community, and to facilitate innovative management”. The sale of airports was divided into two phases. The Melbourne Airport, as a capital airport, was sale to the Australian Pacific Airports Corporation in 1997 together with other two airports in phase one. The path of the privatization was to sell long-term leases for the airport as going concerns. The contract was a 50-year long-term lease with an optional 49-year extension.

#### 4. Literature Review

With continues economy growth internationalization of the world, the aviation industry has grown rapidly over the past decades. New types of large and big aircrafts were invented to meet the high passenger transporting demand in both the biggest carrying capacity, Airbus A380 aircraft, and the longest flying distance, Boeing 787 aircraft. The new innovations together with the growing demands require airports providing more flexible and verities of service.

Several researches have been done to assess the commercialization and privatization of airports from both regional aspects and international aspects. Graham (2008) wrote a book named “Managing airports an international perspective”, which talked about the history and the development of airport commercialization and privatization process. The book lists some key aspects which has high values in managing airports. Things including airport economics and performance benchmarking, airport operations and service quality, the airport-airline relationship, the provision of commercial facilities, airport competition and the role of airport market, the economic and social impact of airports and he environmental impact of airports are key points which the airport managers and owners need to consider. The book talks about the airport management with all elements from a theoretical point of view. Up to now, the book is a good explanation in theoretical teach but lack of links with the reality.

Forsyth, Gillen, Knorr, Niemeier and Starkie (2004) also did a research about how does economic regulation have influence Australia, North America and Europe airports development. The research discusses how the airport marketing affects the regional economy in Australia, North America and Europe area. The research also mentions the confliction between airport marketing and regulations and the competition between airports. However, the research was published in 2004 and the air transport industry had grown in a fantastic speed after that.

Graham and Halpern (2013) did another study focusing on the airport marketing the study introduces the principles and practice of airport marketing. It was published in 2013 which is very close to the recent industry situation. The study also lists some major changes and future marketing challenges to the airport sector. The study is good for airport marketing learners as it particularly focusing on marketing aspects. It pays less attention on the competition between airports and innovations from the deregulation aspect.

Hooper, Cain and White (2000) did a research about the privatization of Australia’s airports. The research dentally describes the Airport Sale Program conducted by the FAC, Australian Federal Government Department. The research tells the path from government department to private ownership, the privatization process and the regulatory framework. Melbourne Airport is one of the airports those sold from the FAC to the private owner. The research is good and it just describes the privatization process with no mentioning of airport management aspect.

The Australia's case study conducted by the International Civil Aviation Organization (ICAO) (2014) is an official document which tells the changing history of both Australia's airport development and the Air Navigation Service Provider's (ANSP) development. The document does not mention any airport management aspects. And, it does not mention any changes after the management transferred from the public holders to the private sectors.

## **5. Results**

### *5.1 Melbourne Airport Annual Reports Study*

#### 5.1.1 Basic Facilities

The Melbourne Airport is now having four terminals and a Southern Freighter Apron servicing both passenger and cargo transport. The current terminal numbering system was introduced in July 2005 with forty domestic and sixteen international. Terminal 1 is now providing services to Qantas and Jetstar airlines with their domestic flights. There are sixteen parking bays served by aerobridges and five non-aerobridge gates. Twelve of them are single aerobridges and the other four are double aerobridges. Terminal 2 is now servicing all international flights out of Melbourne Airport from 1970. There are twenty aerobridge gates. Cathay Pacific, Malaysia Airlines, Qantas, Singapore Airlines, Air New Zealand, United Airlines and Emirates Airline are operating all airline lounges in the terminal. Terminal 2 is a two levels satellite terminal. Departures take place on the first floor and the arrivals on the ground floor with above-ground corridor to both Terminal 2 and the car park. Terminal 3 is now the home for Virgin Australia and Regional Express Airlines. There are eleven parking bays served by single aerobridges and eight bays with non-aerobridges gates. Terminal 4 is a domestic terminal. It was designed to serve Virgin Blue (Virgin Australia) and it was finally rebuilt in 2007 by Tiger Airline. The Tiger Airline is now using Terminal 4 as its hub in operating domestic flights. The Southern Freighter Apron has five freighter parking positions with twenty-one freighter operations a week.

Melbourne Airport is about 23 kilometers away from the city and is accessible via City Link and the Tullamarine Freeway. Melbourne Airport has five car parks. All of these car parks operate twenty-four hours a day and seven days a week. They are divided into short-term, multi-level long-term, business and express car parks. The main multi-level car park is in front of the terminals with over-ground access to the terminal buildings. There are also Skybus Super Shuttle services transferring passengers from the Southern Cross Station in Melbourne city to the airports. There are four local bus services to the airport as well. In 2013, the Victorian Liberal government announced that the Melbourne Airport Rail Link would be constructed in the future running from Melbourne central business area to the airport.

## 5.1.2 Passenger and Cargo Transport

**Table 1. Busiest International Passenger Routes into and out of Melbourne Airport in 2013 Financial Year**

| Rank | Airport                        | Passengers handled | % Change |
|------|--------------------------------|--------------------|----------|
| 1    | Singapore, Singapore-Changi    | 1074034            | 1.7      |
| 2    | New Zealand, Auckland          | 962217             | 4.7      |
| 3    | Malaysia, Kuala Lumpur         | 650356             | 3.6      |
| 4    | Hong Kong, Hong Kong           | 53242              | 1.4      |
| 5    | United Arab Emirates, Dubai    | 460812             | 19.7     |
| 6    | United Stat, Los Angeles       | 458041             | 3.6      |
| 7    | Thailand, Bangkok-Suvarnabhumi | 431041             | 3.4      |
| 8    | Indonesia, Denpasar            | 325564             | 12.5     |
| 9    | New Zealand, Christchurch      | 256997             | 0.5      |
| 10   | RPC China, Guangzhou           | 236236             | 22.3     |

**Table 2. Busiest Domestic Passenger Routes into and out of Melbourne Airport in 2013**

| Rank | Airport                                | Passengers handled | % Change |
|------|--|--------------------|----------|
| 1    | New South Wales, Sydney                | 8244000            | 2.4      |
| 2    | Queensland, Brisbane                   | 3198800            | 0.3      |
| 3    | Western Australia, Perth               | 220970             | 3.       |
| 4    | South Australia, Adelaide              | 2195199            | 5.3      |
| 5    | Queensland, Gold Coast                 | 1675400            | 6.4      |
| 6    | Tasmania, Hobart                       | 1388800            | 12.1     |
| 7    | Australian Capital Territory, Canberra | 994500             | 0.9      |
| 8    | Tasmania, Launceston                   | 872800             | 4.4      |
| 9    | Queensland, Cairns                     | 677600             | 16.5     |
| 10   | New South Wales, Newcastle             | 437500             | 2.9      |

Melbourne Airport broke the record of transfer more 29.9 million passengers in 2013 financial year. There were over 6.2 million international travellers and 21.7 million domestic passengers by 206798 aircraft movements. The domestic passenger transport is still the majority. For the past years, the compounded average annual growth rate for passenger movements is between 3.3% and 4.3%. The compounded average annual growth rate aircraft movement is between 1.8% and 2.6%.

### 5.1.3 Airport Competition

In 2004, Qantas established its own Low-Cost Carrier (LCC), Jetstar. The new LCC choose Avalon Airport as its base in Melbourne to providing service to Adelaide, Brisbane, Perth and Sydney. This made Melbourne became the only city in Australia with two commercial airports and generated the first airport competition in an Australia city. In order to compete with Avalon, Melbourne Airport decided the policy to establish Budget Terminal with lower landing fees. The policy made Melbourne Airport become the cheapest arrival point in Australia and one of the cheapest international airports in the world. Then, Jetstar moved all its flights to Melbourne Airport.

### 5.1.4 Awards

Melbourne Airport has numerous awards. It has won national and state tourism awards, the Service Partner Award and Premier Business Partner Award. In recent years, it has won the best Airport hotel in Australia/Pacific in the World Airport Awards.

## 5.2 Privatization Comparing

Following is a comparing between the Melbourne Airport and the Manchester Airport, a partly privatized airport, and the Frankfurt Airport, a totally privatized airport. The aim of the comparing is to assess the difference between three airports and providing more data to measure the possibility of success of the Melbourne Airport.

### 5.2.1 The Manchester Airport (Partly Privatized)

The Manchester Airport is an international airport in Manchester, England. It is the third busiest passenger transfer airport in the United Kingdom and the twenty-first busiest airport in Europe. The Manchester city owns ten airports with providing flights to about two hundred destinations.

All the British airports were owned by the Government before the establishment of British Airports Authority (BAA) in 1965. In 1966, BAA assumed ownership and responsibility for four of the twenty two Government-owned airports. Other government-owned airports were transferred to respective local authorities. In 1985, the government intended to privatize BAA in the context of the privatization and reform of public sectors. In 1987, BAA was offered for sale and listed on the London Stock Exchange. The Manchester Airport has experienced the change of corporate structures. In March 2002, the Manchester Airport became one of trading subsidiaries of the Manchester Airport Group plc (MAG). MAG s owned by the Manchester City Council (55 percent) and the other nine district councils (5 percent each). MAG operates the Manchester Airport.

### 5.2.2 The Frankfurt Airport (Totally Privatized)

The Frankfurt Airport is one of the major international airports in Frankfurt, Germany. The Frankfurt city is the fifth largest city of Germany and one of the world's leading financial centers. The Frankfurt Airport is the third busiest passenger transfer airport in Europe and the busiest airport in Germany. It is also the busiest cargo transfer airport in Europe. The Frankfurt Airport is now providing service to 264

destinations among 113 countries and international areas which makes it the most international destinations in the world.

The German Federal Government started airports privatization program in 1982. In June 2001, the Frankfurt Airport went to the Frankfurt Stock Exchange with an Initial Public Offering (IPO). It was transferred from wholly owned by the Federal Government to Frankfurt AG. The Frankfurt Airport is currently held by the Frankfurt Airport company, which is one of the subsidiaries companies of the Frankfurt/Main AG (FAG). The Frankfurt Airport is now remaining one the most successful cases in airport privatization all over the world.

### 5.2.3 The Privatization Model

The Melbourne Airport is now held by the Australia Pacific Airports Corporation Limited (APAC) in a form of management contract with the Australian Federal Government on a 50-year contract with an optional 49-year extension. Currently, the Melbourne Airport is a totally privatized airport and the Commonwealth Government still remains the possibility to take it back to public holders.

The Manchester Airport is operated by MAG with a share flotation by the Manchester City Council and the other nine district councils. The Manchester City Council is remaining a public sector so that the Manchester Airport is now a partly privatized airport.

The Frankfurt Airport is wholly owned by the Frankfurt AG by share flotation on the Frankfurt Stock Exchange. Without any public investor, the airport is a wholly privatized airport.

Both the Manchester Airport and the Frankfurt Airport choose to be sale on the stock exchange as the path to the privatization. This is a very common way in Europe. It is because both this two airports are the major airport in high population density areas. The passenger turnover and the cargo turnover keep on a high demanded level since the setup of them. By selling to private stock holders, airports can quickly gain revenues and resources from business markets.

By contrast, the Melbourne Airport is sold with a long-term management contract. It is because the high demand of aviation industry turns up later in the Australian area than the Europe. Although Australia is the southern hemisphere's largest economy, there are still gaps between Australia's economic level and European countries. With the rise of low-cost carriers and the growing market in Asia-Pacific area, Australia starts cooperation with other Asian countries in all aspects of economic and political. The growing aviation industry is highly related to these national and international economy levels. The Australian Federal Government has its own consideration on the aviation industry. The Melbourne Airport might be sold on a stock exchange after its leasing. By now, the long-term management lease looks still remaining as a good choice for the Federal Government with a gradual process of development.

### *5.3 Strategies Comparing*

Sydney and Melbourne are the first two largest cities in Australia. Coincidentally, the Sydney Airport and the Melbourne Airport are the first two busiest airport in Australia. Usually, Sydney and Melbourne are always being compared with each in various aspects. In the process of airport privatization, the Melbourne Airport was sold in the first phase with other three airports. The Sydney Airport was the last sold airport by the Federal Government. Two airports adopt some different strategies in the airport competitions.

#### *5.3.1 The Sydney Airport*

The Sydney Airport is an international airport servicing Sydney area. It is one of the oldest continuously operated airports in the world and he 31st busiest airport in the world. The airport is now providing service with forty six domestic and forty three international destinations. The airport is currently managed by Sydney Airport Corporation Limited.

#### *5.3.2 Basic Facilities*

The Sydney Airport is now having four passenger terminals. The international terminal is separated from other terminals. In order to keep the service level the airport requires a minimum connection times. The interchange between domestic flights is thirty minutes. The interchange between international flights is one hour. The interchange from domestic flights to international flights is one hour. The interchange from international flights to domestic flights is one hour and fifteen minutes. Also, the airports operate shuttle service between the terminals which cost AU\$5.50. Besides the passenger terminals, the airport also has a freight terminal which providing cargo service. It is also used as a backup for terminal one as an overflow parking.

The Sydney Airport was used to be suffered from a limitation of the runways expansion problem. The two runways cross each other limit the number of flights taking off and landing for several decades. Eventually, the airport built another runway to help increasing the capacity of the growing demand. The Sydney Airport provides a variety of transport into and out of the airport. Besides the shuttle bus between terminals, there are also shuttle buses deliver passengers to the city and to the door of their hotel. The ticket is available from the information desk and online as well. The Airport Link underground rail line is the other link connecting the airport and the city. It is located below the international terminal with another domestic railway station. The rail stations are parts of the Sydney Trains suburban network. There are single ticket and day-return tickets which provide by the station holder, the Airport Link consortium. There are also buses between the airport and the city.

The airport has road access to all directions of the city. The road facilities include motorways, Freeways, avenue and even a bicycle path.

## 5.3.3 Passenger and Cargo Transport

**Table 3. Busiest Domestic Routes into and out of Sydney Airport in 2013**

| Rank | Airport                                | Passengers handled | % Change |
|------|--|--------------------|----------|
| 1    | Victoria, Melbourne                    | 824400             | 2.4      |
| 2    | Queensland, Brisbane                   | 4424920            | 0.8      |
| 3    | Queensland, Gold Coast                 | 255930             | 4.9      |
| 4    | Western Australia, Perth               | 1800400            | 0.6      |
| 5    | South Australia, Adelaide              | 1027600            | 2.4      |
| 6    | Australian Capital Territory, Canberra | 1027600            | 2.4      |
| 7    | Queensland, Cairns                     | 978600             | 4.8      |
| 8    | Tasmania, Hobart                       | 517200             | 8.2      |
| 9    | Queensland, Sunshine Coast             | 464600             | 0.3      |
| 10   | New South Wales, Coffs Harbour         | 368000             | 14.9     |
| 11   | Northern Territory, Darwin             | 357000             | NA       |
| 12   | New South Wales, Ballina               | 315800             | 12.5     |
| 13   | Tasmania, Launceston                   | 272600             | 22.4     |
| 14   | New South Wales, Albury                | 234600             | 5.1      |
| 15   | Queensland, Hamilton Island            | 200900             | 0.1      |

**Table 4. Busiest International Routes into and out of Sydney Airport in 2013 Financial Year**

| Rank | Airport                         | Passengers handled | % Change |
|------|---------------------------------|--------------------|----------|
| 1    | New Zealand, Auckland           | 1394417            | 0.2      |
| 2    | Singapore, Singapore            | 1336560            | 14.4     |
| 3    | Hong Kong, Hong Kong            | 922156             | 3.7      |
| 4    | United States, Los Angeles      | 888861             | 0.6      |
| 5    | United Arab Emirates, Dubai     | 597600             | 21.3     |
| 6    | Thailand, Bangkok-Suvarnabhumi  | 569150             | 3.6      |
| 7    | Malaysia, Kuala Lumpur          | 562377             | 44.3     |
| 8    | New Zealand, Christchurch       | 447801             | 2.6      |
| 9    | Fiji, Nadi                      | 445386             | 1.       |
| 10   | United States, Honolulu         | 401364             | 15.2     |
| 11   | RPC China, Shanghai-Pudong      | 385525             | 7.4      |
| 12   | United Arab Emirates, Abu Dhabi | 375968             | 0.2      |
| 13   | Japan, Tokyo-Narita             | 361556             | 7.9      |

|    |                                 |        |      |
|----|---------------------------------|--------|------|
| 14 | United Kingdom, London-Heathrow | 344220 | 13.1 |
| 15 | South Korea, Seoul-Incheon      | 338934 | 1.5  |

With servicing over 40 international and domestic passenger airlines and 16 cargo airlines, the Sydney airport is now remain as a hub in Australia connecting the other of the world. Table 3 and Table 4 show the busiest domestic and international routes in the year 2013 in Sydney Airport. Obviously, domestic routes handle a much more passenger capacities than the international routes. The native aviation demand in Australia is very large. Between international routes, the connecting Asia-Pacific regions provide more passengers than other regions. As the aviation market is growing fast in this area, Australia is now focusing to having more cooperation and making more profits from the Asian-Pacific business markets.

#### 5.3.4 Limitation

Due to the increasing aircraft movements, the noise pollution becomes a main issue to the Sydney Airport. In 1995, the Australian Parliament passed the *Sydney Airport Curfew Act 1995* to limits the operating hours of the airport. This was the effort made by curb complaints about aircraft noise. The limitation announces there would be no aircraft from taking off or landing between the hours of 11pm and 6am. The limitation does reduce the movement of aircrafts but cannot stop the increasing numbers of flights. Besides the curfew policy, there is also a cap of 80 aircraft movements per hour limitation to the airport. The policy is made to control delays during peak hours.

#### 5.3.5 Further Plan

An announcement was made by the Sydney Airport said that the airport would be divided into two airline-alliance-based precincts integrating international, domestic and regional services under the one roof by 2019. The current domestic terminal 2 and terminal 3 would be used by members of the *Oneworld* airline alliance. The international terminal 1 would be used by Virgin Australia and is international partners with other international airlines together. The airport chooses to become airline-alliance-based terminals because the holders are in favour of terminals “based around specific airlines requirements and passenger transfer flows”. In 2013, the airports released its *2013 Masterplan*. The plan describes that the airport will use “swing gates” to service domestic and international flights from the same terminals. The upgrading in Terminal 3 will provide a better service to the Airbus A380 aircrafts.

The common aspects between the Melbourne Airport and the Sydney Airport are:

- 1) Both of them focus on upgrading basic facilities and infrastructures including Terminals, runways and servicing A380 aircrafts.
- 2) Both of them pay attention to the airport-airline relationships. The cooperation has interfered with each other and has influence on their future planning.

3) Both of them want to be the center hub of the area. Becoming transportation is an inevitable. They wish to be a regional economy center as well.

There are several differences between them:

- 1) They have different environment limitation. They choose a different way in control the noise population, for example.
- 2) Melbourne Airport has a more close relationship with the ANSP. The Melbourne's ANSP is one of the two ANSPs in Australia servicing the whole South-West areas.
- 3) Sydney Airport has more public transportations connecting the airport and the city. Melbourne Airport does not have that much of choice.

## 6. Conclusion

The long-term lease management contract of Melbourne Airport has been over 10 years. After privatized, the airport adopts several strategies in managing a business-like model. By using strategies in setting up tourism center, hotels it wins the outstanding awards among other Australian airports. By using Budget Terminal policy, it becomes a cheap arrival point in the world and gets more aircraft movements. The long-term lease model of privatization is a good choice to the Australia Federal Government because the government will have a long time to measure how successful will the airport be. Also, sharing flotation model like Manchester Airport and Frankfurt Airport is still a possibly way in the future. The privatization process in Melbourne Airport success and it could be a good example for other Australian airports.

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