THE COMPETITIVE EDGE: AIRPORTS IN EUROPE

ACI EUROPE

AIRPORTS COUNCIL INTERNATIONAL

SYNOPSIS

This synopsis publication is produced by ACI EUROPE and aims to summarise and contextualise the key findings of the 2017 Oxera Study entitled *"The Continuing Development of Airport Competition".*

The Oxera study builds on a growing body of work about airport competition, including the 2012 study, *"Airport Competition in Europe"* by Copenhagen Economics and the ACI EUROPE publication *"How Airports Compete"* among others.

These publications are available in the 'Policy Library' section of the ACI EUROPE website:

www.aci-europe.org

INTRODUCTION

The European Single Aviation Market celebrated its 25th anniversary earlier this year –
a moment that served as a reminder of just how much has changed since its inception.
The ongoing Brexit negotiations have also underlined the potential implications of
undoing the benefits that open markets have brought to air transport connectivity and in
particular, to the dynamics between airlines and airports.

For a quarter of a century, Europe's airports have been free to market themselves to
airlines, big and small, Full Service Carriers (FSC) or Low Cost Carriers (LCC), Europeans or
(increasingly) non-Europeans. Yet, it has taken time for the resulting dynamics in terms
of business transformation and competition to be understood and recognised. Indeed it
took the study produced by *Copenhagen Economics* in 2012 to clearly demonstrate how
and to what extent airports in Europe compete - and to definitively challenge the old-
fashioned assumption about airports being intrinsically monopolist by nature.

Five years on, developments in the European aviation market have further accelerated.
Largely driven by continued growth in the demand for air travel, digitalisation and
disruptive innovation in the air transport sector, these developments have redefined
the structure of our aviation market. In doing so, they have logically exposed airports
to even more competitive pressures. In an effort to track this ongoing evolution, ACI
EUROPE commissioned the research consultancy Oxera to review and analyse the factors
of competition that today define the European airport industry and how airport-airline-
passenger dynamics stem from that.

The resulting study reveals more movement and more structural change than we had
initially suspected – with significant changes in both the nature and intensity of airport
competition.

This synopsis publication aims to provide you with a digest of the key findings of their
study.

BUT FIRST... HOW DOES AN AIRPORT ATTRACT AIRLINES?

Convincing an airline to establish a new air service to/from your airport can be a demanding and lengthy process, involving sustained collaboration with a wide range of external partners – such as tourism authorities, foreign direct investment agencies, the local business community and regional or national governments. Europe's airports have developed extensive airline marketing & route development departments specifically for this task and the objectives they set are part of the overall business strategy of each airport (for example, 'gain a new route to Asia and 2 new routes to Africa by year X'). These objectives are linked to the airport masterplan and investment in improving and expanding the facilities, so that the airport is able to provide the capacity and quality of service required by various airline business models.

In order to market itself to airlines effectively, an airport needs to regularly assess and research the features & benefits of its catchment area. Key information of interest to airlines includes: the population living within 1 hour and within 2 hours of the airport; how they get to the airport; the demographics & economic positioning of that population; significant employers in the region and the kind of international connectivity they require; tourism and other special attractions such as seasonal festivals.

Airports also need to financially entice airlines to develop at their location. This almost always involves systems of rebates and incentives on airport charges (the fees paid for the use of the infrastructure) as well as other forms of indirect support – such as financing airlines' marketing and communication plans relating to the routes they operate at the airport.

Moreover, airports also need to ensure their operational processes & infrastructure are efficient – and can be tailored to the requirements of specific airlines. They need to make sure there is enough capacity to accommodate future growth. In this regard, airport charges are just one side of the economic equation of operating at an airport for airlines – although they are never keen to admit it.

In all these aspects, airports are business-to-business suppliers, and like all suppliers, big customers can squeeze them for more, while smaller customers can bring the extra volume that can end up making the difference between a profit or loss at the end of the year.

All these network development & marketing strategies are now a must for airports across Europe. They are per se symptomatic of airport competition - as is the fact that European airports end up spending a lot of money to attend and exhibit at the ROUTES Conferences, which are events dedicated to air route development where they are literally courting airlines (who attend for free).

Airport route developers pitching to airlines during a speed-dating session at a ROUTES conference.

TOOLKIT OF AN AIRPORT ROUTE DEVELOPER

Market research

Incentives such as discounted airport charges for a set period of time

Traffic & route data on rival airports

Eye-catching marketing campaign, with publications, conference stand, etc.

Good working relations with the local, regional & national authorities

Contacts at key foreign embassies

Collaborative relationship with the local tourism authority, hotels & others
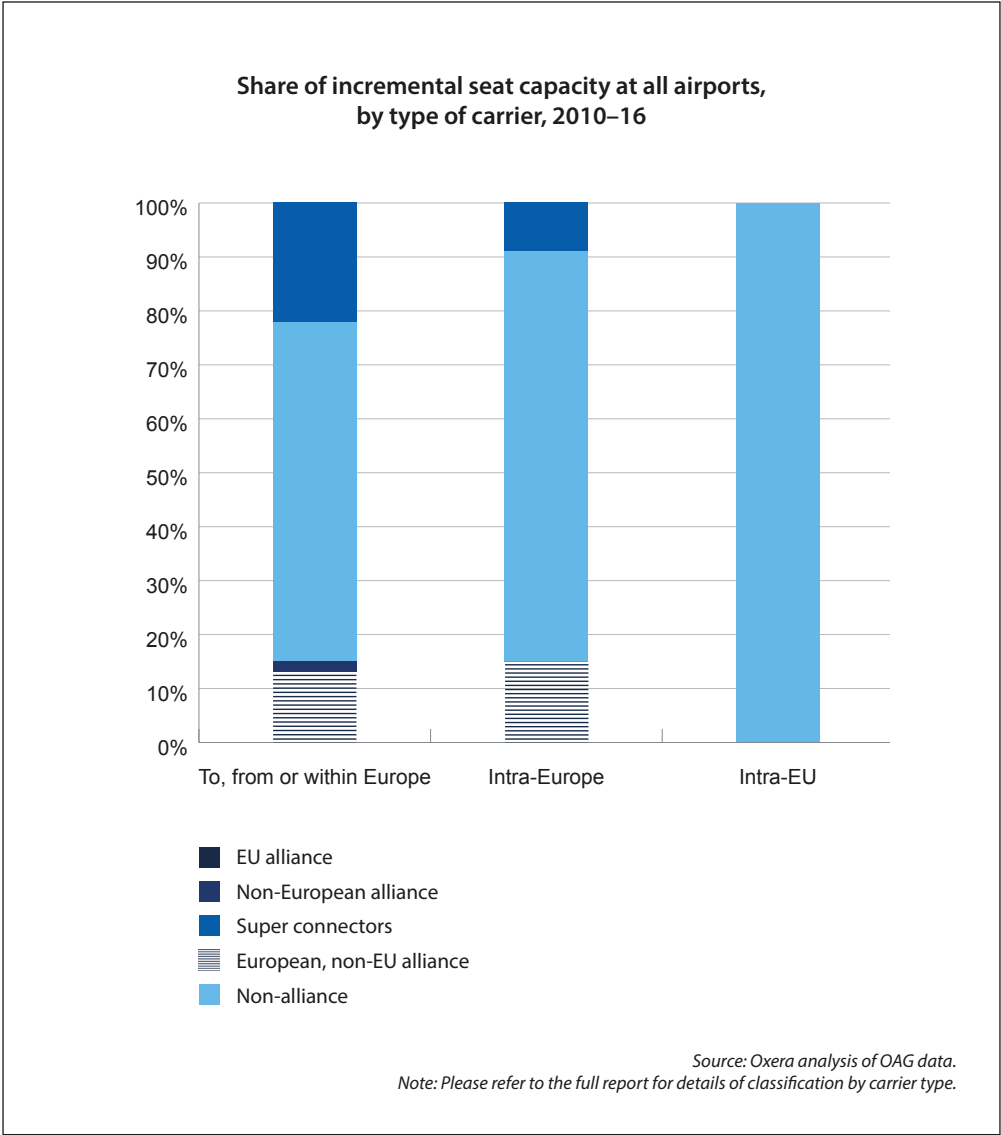
Travel budget for conferences & meetings with airlines

1

RECENT MARKET DEVELOPMENTS

The period of 2010 to 2016 was tumultuous, even by aviation's usual standards. The impact of the global financial crisis lingered on and was followed by severe spikes in oil prices in both 2009 and 2011. The rise of the smartphone, ongoing momentum of social media and other digital advances all had surprising implications during this time, in parallel to some very specific aviation industry developments – which all combined to create **disruptions** and **significantly increase competitive pressures on airports**.

1.1 MARKET GROWTH DRIVEN BY LCCs & NON-EUROPEAN AIRLINES

Between 2010 and 2016, as airlines became more careful in expanding capacity and focused very much on unit revenue growth (yields), growth in Europe became more selective. However, in those 6 years the market still grew by **+25%** in terms of passenger traffic – with that growth predominantly driven by new services and additional capacity from European Low Cost Carriers (LCCs), mainly on intra-European routes.

In fact, during that time, **76% of all growth at European airports came from LCCs**. These airlines operate **flexibly** on a pan-European basis, moving their assets in search of the best market conditions. This means that they are able to exercise **considerable pressure over airports** as they are prepared and able to switch their aircraft between different locations.

Another significant source of growth for airports was the **continued expansion of the 3 big Gulf 'Superconnectors'** (Emirates, Etihad Airways and Qatar Airways) **and Turkish Airlines**. This led to a very noticeable trend of Middle Eastern/Turkish hubs using their growing carriers and geographical advantages to expand the demand for air connectivity between Europe, Asia-Pacific and Africa. This is why the question of 'Where do I connect?' today firmly includes Abu Dhabi, Dubai, Doha and Istanbul airports alongside Europe's major hubs. While increasing rivalry with established hubs in Europe, the rise of the Gulf carriers and Turkish Airlines also led to rising competition between other European airports vying to attract these airlines to their location.

Share of incremental seat capacity at all airports, by type of carrier, 2010–16

Legend:
- EU alliance
- Non-European alliance
- Super connectors
- European, non-EU alliance
- Non-alliance

Source: Oxera analysis of OAG data.
Note: Please refer to the full report for details of classification by carrier type.

Capacity (seats) departing and arriving at selected airports, 2010 vs 2016 (millions)

Source: Oxera analysis of OAG data.

A sample of Bordeaux Airport's marketing to attract direct long-haul services.

1.2 THE CONVERGENCE OF AIRLINE BUSINESS MODELS

The global financial crisis and the unstoppable rise of digitalisation irreversibly changed consumer behaviour – with a strong focus on frugality and value for money. This proved to be a boon for LCCs as the key criterion – price – became a decisive factor for the majority of air travellers. During this time, LCCs reported record traffic figures and profits.

As business travellers acquired the habit of flying LCCs as well, when the economy gradually improved, passenger expectations did too. In order to retain the advantage they had and further expand, **LCCs sought to move upmarket**. This meant both **improving their quality of service** and **expanding into primary & larger airports** that were traditionally the fortresses of flag-carrying Full Service Carriers (FSCs).

For example, everyone in Brussels remembers the moment when Ryanair announced it was opening 10 new routes from Brussels Airport, while continuing its activities in Brussels-South Charleroi – an early stronghold of Ryanair's, just one hour's drive away. As of September 2017, the airline now operates 20 routes from Brussels and over 80 routes from Charleroi. Meanwhile, at Europe's 4th busiest airport, Frankfurt, Ryanair now has 39 routes, while the airline continues to operate 48 routes from Frankfurt-am-Hahn airport.

In parallel to these developments, the **FSCs have sought to replicate the success of the LCCs**. This has involved establishing or further developing their own LCCs (Air France-KLM with Transavia and Joon, IAG with Vueling and LEVEL and Lufthansa Group with Eurowings) and expanding their presence in airports other than their traditional hubs. In doing so, **FSCs have increasingly replicated the behaviour of LCCs vis-à-vis airports – in particular when it comes to negotiating tactics.**
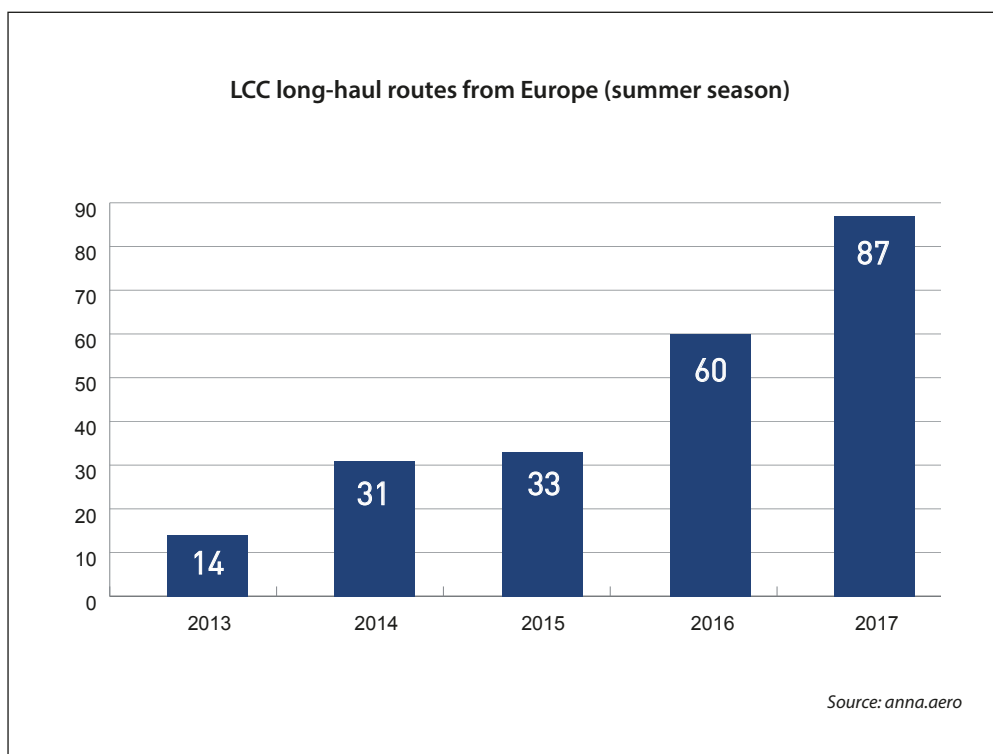
1.3 THE PURSUIT OF MULTI-HUB STRATEGIES

As airline consolidation continues to be the subject of much speculation in Europe, **the overt pursuit of multi-hub strategies by the major European airline groups** (in particular IAG, Lufthansa Group and Air France/KLM) is all part of regularly reminding hub airports that their main customer could choose to deprioritise one of them to the benefit of the others.

For example, IAG's Willie Walsh has been repeatedly vocal about his belief that Heathrow does not have to be epicentre of IAG's operations, as the group also looks to expand its already significant operations in Dublin (Aer Lingus), Madrid (Iberia) and Barcelona (Vueling & new brand LEVEL). Lufthansa Group's imprint at its hubs is equally impressive – as is their proximity to each other: Brussels (Brussels Airlines), Frankfurt (Lufthansa), Munich (Lufthansa), Vienna (Austrian) and Zurich (SWISS).

Multi-hub strategies now allow these airline groups to exert credible threats over their hub airports – in order to extract the best conditions both financially and operationally. As shown by the Oxera study, these threats can and do lead to action.

1.4   LOW COST LONG HAUL GETS ITS WINGS

Low cost long haul air travel is not new – but the past years have seen it become the **next stage in the LCC revolution**, with a significant increase in these services operated from European airports. The combination of contained oil prices, rising leisure-driven demand for air transport and the entry into operation of new game-changing aircraft in terms of efficiencies and range (such as the Boeing 787 and the Airbus A350, but also the A320NEO and Boeing 737Max) have allowed previously non-viable air routes to operate.

LCC long-haul routes from Europe (summer season)

Year	Routes
2013	14
2014	31
2015	33
2016	60
2017	87

Source: anna.aero

The advent of low cost long haul services now offers **the potential to medium-sized airports and even smaller regional airports to enter the long haul market** – a field that used to be mainly the preserve of larger hub airports. It means **new & direct long haul routes bypassing the established European hubs**. Consider for example the fact that in July, Cork airport in Ireland was able to launch a scheduled service to Boston-Providence in the US (operated by Norwegian), or that Manchester now has a direct service to Puerto Vallarta (Mexico) and that Doncaster-Sheffield saw the opening of a direct route to Montego Bay (Jamaica).

1.5 SO... WHAT DOES THIS ALL MEAN FOR AIRPORTS?

All these recent developments in the aviation market end up creating a situation where **more than 500 airports across Europe are now competing for airline capacity, with a few dominant LCCs and airline groups benefiting from ever-increasing negotiating power.** The move to primary airports by LCCs has been particularly disruptive in this regard, dialling up the competitive dynamics between larger airports, medium and smaller ones in a way few would have foreseen 6 years ago.

**MARKET DRIVERS OF AIRPORT COMPETITION
2010-2016**

LCCs offering connecting products

Market Growth
+25% passenger traffic (2010-2016)

1

Rise of Self-connecting

6

2

LCCs expansion
76% of market growth from LCCs

LCCs going long haul & hub by-pass

5

3

4

Gulf & Turkish Airlines expansion

7

Convergence of airline business models
LCCs move upmarket
FSCs adopt LCC business practices

2

AIRPORT COMPETITION: EVOLVING CHANNELS & INCREASED INTENSITY

In analysing the cumulative impact of these recent market developments since 2010, the Oxera study found significant changes both in the nature and intensity of airport competition across Europe:

- Airport competition is **now primarily driven by competition for airline services on a pan-European basis**.

- **Hub competition has also escalated** and hub airports see **challenges from many sources**.

- **Local competition for passengers with airports serving the same catchment areas has continued to rise**, with more airports offering competing routes.

- While **competitive pressures** were already high for smaller airports prior to 2010, since then they **have significantly increased for medium sized and larger airports** (over 10 million passengers) – **including for major hubs**.

A small sample of European airports' marketing campaigns towards airlines since 2010.

2.1 PAN-EUROPEAN COMPETITION FOR AIR SERVICES RULING THE GAME

Airport competition has long been a reality – albeit on a much smaller scale than it is now. Indeed, airports have always competed on a local basis & for passengers – with those airports located in the same catchment area. The limited geographical scope of such competition meant that competitive pressures used to be more contained.

What the **Single European Aviation Market** changed over time – as a result of the ensuing LCCs revolution – is **the very nature of airport competition**. The resounding success of LCCs comes from their operational efficiency and extreme flexibility in moving their assets. This may still surprise some people, but **LCCs are essentially route-agnostic**. They are simply looking for the most lucrative route development opportunities – which very much comes down to the lowest price and best operating conditions as far as airports are concerned.

From that perspective, LCCs and airports could not be more different. LCCs are highly mobile beasts, always looking for the best or a better market location. Conversely, airports are entrenched into their territory and cannot move to a better market location – they can only work on making their market location better.

As long as LCCs market penetration remained marginal – they did not really impact airport competition. But their phenomenal growth has now completely altered **the nature of airport competition** – giving it **a truly Pan-European dimension**.

Two important structural factors have combined to now make this pan-European competition for air services the primary driver of airport competition:

- The fact that airports are **naturally growth-driven** due to their economic features.
- The fact that since 2010, **76%** of the growth in passenger demand at Europe's airports has come from LCCs (and 100% on intra-EU routes) – along with their increasing penetration into primary airports & larger markets.

The result is that today for any airport in Europe – whatever its size & location – **LCCs are now the ones calling the tune**. In practical terms, this means that Cluj Napoca in Romania ends up competing with Cork in Ireland, or Cagliari in Italy and Kaunas in Lithuania to attract new air services or retain existing ones. Similarly, Barcelona airport must show what it can do for the airline compared to London-Gatwick, Copenhagen, Munich or Warsaw.

This reality is most clearly reflected in the network development of LCCs, as per the maps that follow, showing the evolution of the networks of Ryanair and Wizzair since 2010.

Growth in Ryanair airports served, 2010 versus 2016

Ryanair present 2016 only

Ryanair present 2010 only

Ryanair present 2010 & 2016

Growth in Wizz Air airports served, 2010 versus 2016

✈ WizzAir present 2016 only

✕ WizzAir present 2010 only

✈ WizzAir present 2010 & 2016

AIRPORT COMPETITION WORKS AT THE MARGINS

Airports are naturally growth-oriented, due to their economic features – in particular the fact that they are largely fixed-costs businesses with a high capital intensity. Therefore, marginal changes in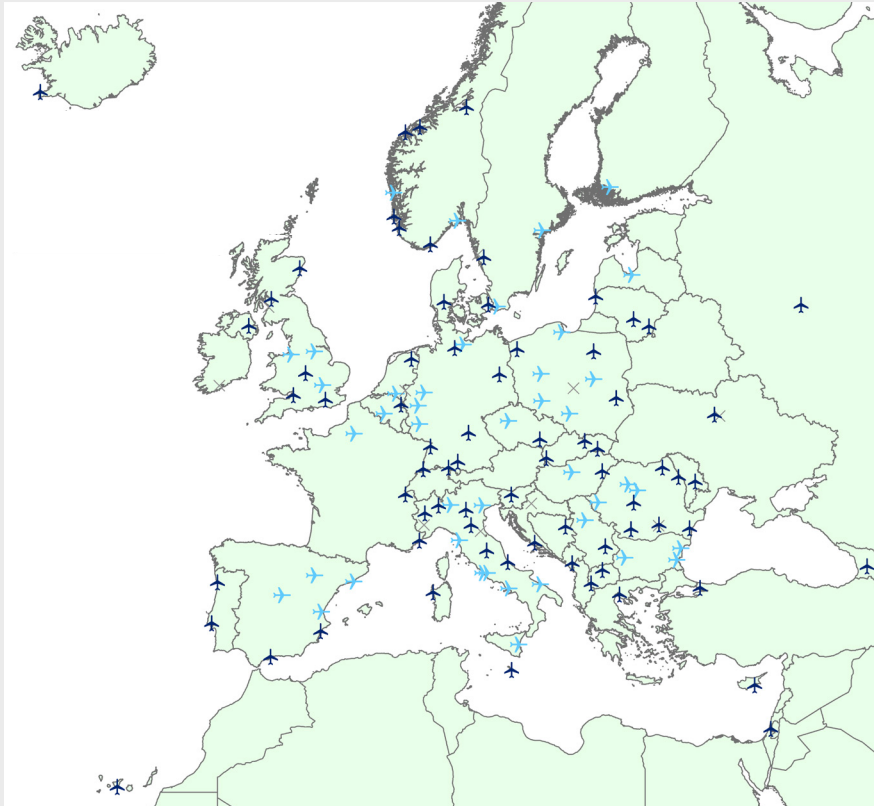 traffic can have a strong impact on profitability – either positive in case of traffic gains or negative in cases of traffic losses. An airport considering a change to its charges must ensure that it does not have a negative effect on traffic volumes.Competition at the margins drives the overall levels of competitive constraints upon airports.

→ Primary colours

The Pan-European dimension of airport competition and its increase in particular for medium-sized and larger airports (over 10 mppa) – including hubs, is also obvious from the level of **route churn**. In this regard, the Oxera study points to the following:

- The total number of routes between European airports now stands at 18,000 with over **3,000 routes opened and 2,500 routes closed every year** – reflecting the freedom airlines have in shifting routes and allocating new capacity.

- The **rates of route churn** (which indicates the extent to which airlines are able to switch between airports and thus reflects competitive pressure) have remained high and roughly stable for airports with less than 10mppa while they have **increased substantially for medium and large airports with over 10mppa** – with this being particularly pronounced for airports with between 10mppa and 25mppa.

  Overall route churn rates are progressively converging across the airport industry – pointing to an **upward convergence in competitive pressures**. In addition, Oxera also notes that beyond actual switching by airlines, the mere threat of an airline moving just some of its aircraft can compel an airport to lower its charges.

Route opening rates, by airport size, 2011 vs 2016

Legend: 2011, 2016
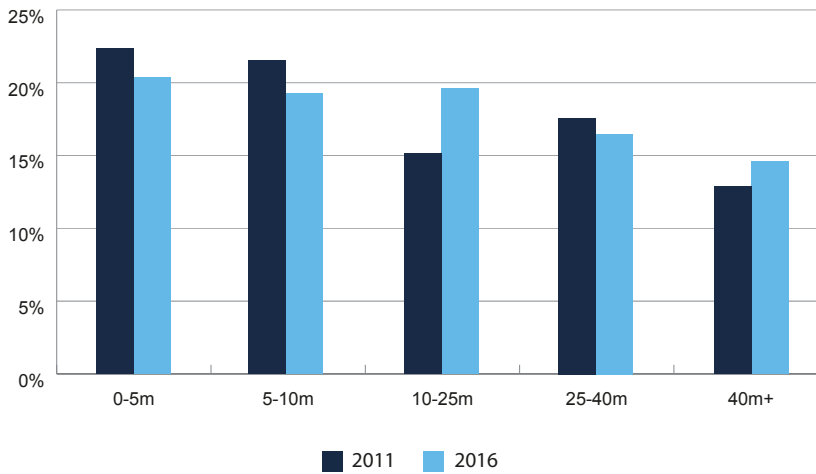
Source: Oxera analysis of OAG data.

Route closure rates, by airport size, 2011 vs 2016

Legend: 2011, 2016
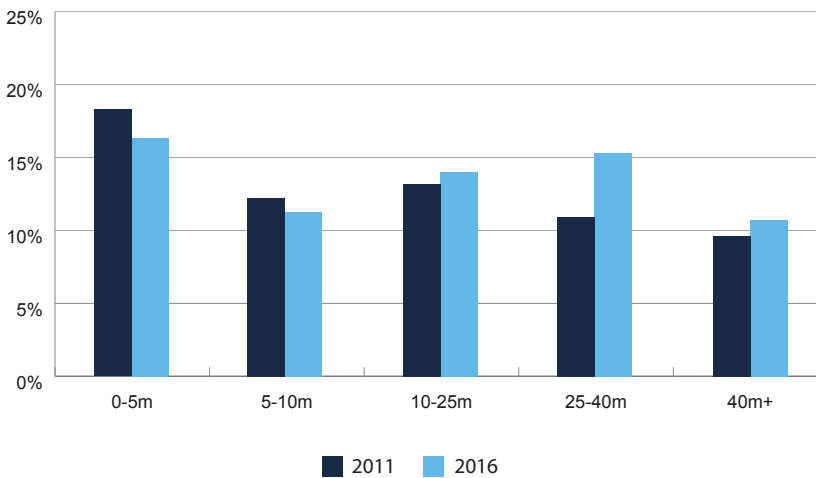
Source: Oxera analysis of OAG data.

➜ Beauty contests... for airports

This pan-European competition for air services is even more obvious in the fact that LCCs now routinely run **"beauty contests"** among airports to get the best deals. The following provides an example of the kind of standard letters airports now get from powerful pan-European airlines (in this example, the name of the airline has been deleted):

> *"[airline name] has now started planning the Summer 2018 schedule. Our aircraft delivery programme slows down somewhat until late 2019, and capacity for new routes or increased frequencies will need to come from underperforming route & destination reductions (…) We wish to give all airports in our network every opportunity to secure the optimum outcome from [airline name] 's Summer and Winter 2018 planning"*

➜ Not just LCCs

Finally, the Oxera study also noted another element of pan-European airport competition, as **European airports of all sizes compete to gain 'spokes' into the fast growing non-European airline hubs** - notably Dubai, Abu Dhabi, Doha and Istanbul. The 'super-connector' airlines have taken advantage of their geographic location and the rise in travel demand to/from Asia-Pacific to account for an increasing share of market growth in Europe. The super-connectors, with each new connection to Europe, seek to enter a wide range of airports (witness the establishment of flights such as Bologna to Dubai, or Edinburgh to Doha), with plenty of other medium-sized regional airports all eager to gain a frequent service with a wide-body jet.

November 2015: Emirates airline launching their service between Bologna and Dubai, their third city pair in Northern Italy. The airline also operates direct flights between Dubai and Milan-Malpensa and Venice-Marco Polo airport.

Footprint of airports with connections to the Middle East and Istanbul, 2010 vs 2016
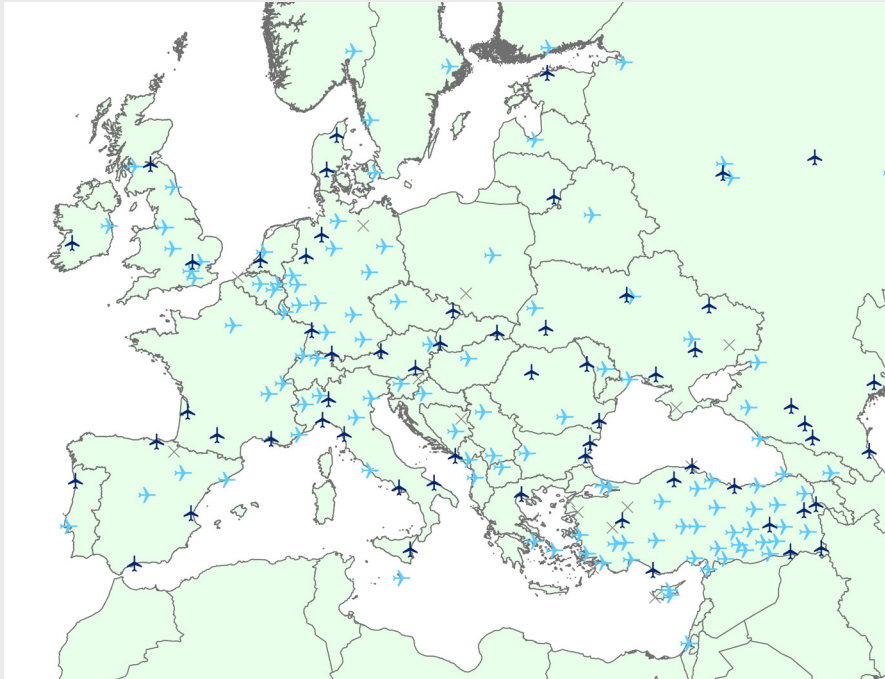
✈ ME & Istanbul spokes 2016 only

✕ ME & Istanbul spokes 2016 only

✈ ME & Istanbul spokes 2010 & 2016

Source: Oxera analysis of OAG data.
Notes: Only airports within European countries are shown. European countries are defined as the 45 countries with at least one airport that is a member of ACI EUROPE, based on ACI EUROPE's member list.

SWITCHING COSTS & BUYER POWER

Are airlines locked into certain airports?
This is often a source of confusion.

Firstly, switching costs mostly matter when airports are competing for the existing market. But, the market still shows high levels of route churn, with nearly 20% of the routes in the network being subject to change each year – either opening or closure. This percentage alone tells us that switching happens, affording a lot of flexibility in the choice of airport from/to which to deploy their aircraft.

The extent to which an airline may be "locked in" to an airport because of high switching costs is mitigated by the power an airline can exert as a primary customer. As a buyer of the services that the airport sells, it has a power to severely impact the airports revenues with the mere threat to close part of its routes and move them somewhere else.

This buyer power has been amplified by the proliferation of low-cost business models, which means airlines have much less invested into an airport and can move with relatively little cost. Airline consolidation also allows airlines to have the scope to more easily move aircraft - along with the use of multi-hub strategies.

Airports can also sweeten their offer by helping to offset the costs of an airline switching from another airport and setting up new routes. This is done, for example, through marketing of the new route for the airline by the airport, helping the airline reach a load factor that turns a profit.

Switching costs exist, but changes in the market since 2010 mean that today they are smaller than they used to be and as such, are less of a barrier to an airport seeking to attract airlines away from other airports.

2.2   HUB COMPETITION ESCALATING

Where hub airports were once deemed to be recipients of traffic, by mere fault of geography and dependence on one home-based airline, the past decade has seen them face **increasing challenges** to their business. In particular, the following **recent developments** are now firmly keeping Europe's hub airports on their toes:

➜   ## Competing for the transfer passenger with Gulf & Turkish hubs

When flying an indirect routing, connecting passengers can travel via any hub airport that fits their flight options, so in this regard airports compete to gain the traffic transferring between flights.

For Europe's major hubs, this connecting traffic is a defining business factor – as it amounts for an important share of their total passenger traffic: 30% at London-Heathrow, 32% at Paris-CDG, 61% in the case of Frankfurt airport and 38% at Amsterdam-Schiphol.

The Oxera study found that since 2010, European hubs have been exposed to an **impressive increase in the competitive constraints from hubs located in the Gulf & Turkey**. This is evidenced by the way these non-European hubs have developed their hub connectivity and the related impact on European hubs, in terms of competed connected routes.

•   **Key fact**: **Istanbul, Abu Dhabi and Doha have all more than doubled their number of connecting routes since 2010.**

Number of origin destination pairings served by a connecting flight through selected airports (bars, left) and growth in these (% points, right), 2010 vs 2016

Legend: 2010 · 2016 · Growth 2010 to 2016

Source: Oxera analysis of OAG data.
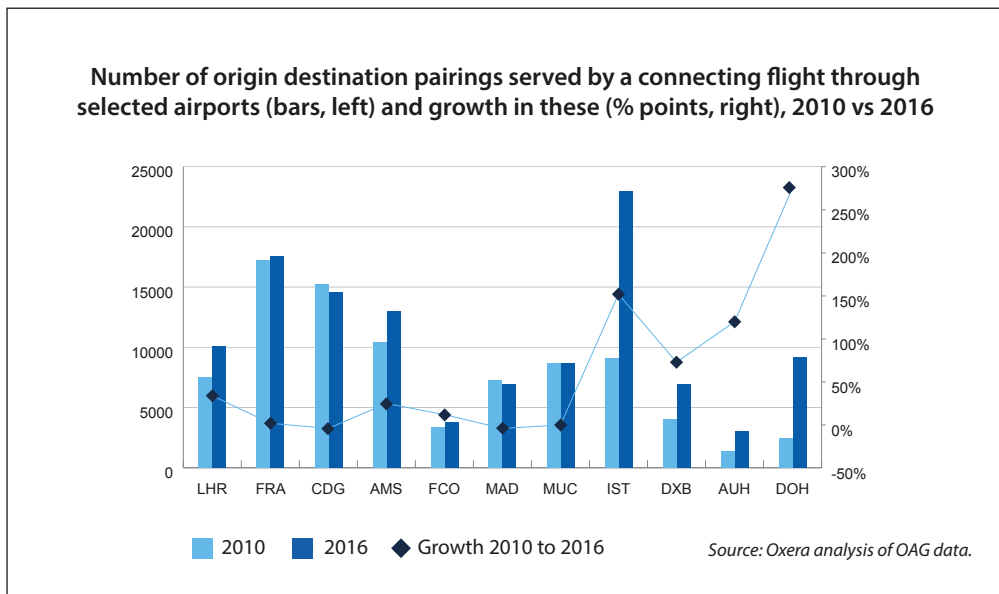
- **Key fact**: European hubs have seen a **significant increase in the proportion of their connected routes for which they face competition from Gulf & Turkish hubs**. This competition is exacerbated for connected routes to/from **Asia-Pacific**. Indeed, the depth of connections available via Gulf & Turkish hubs on these routes means that they impose a particularly strong constraint on European hubs – which are now typically facing competition on between **50%** and **60%** of their connected routes to Asia-Pacific.

Proportion of connecting routes (excluding intra-Europe) at selected European airports competed by Middle Eastern airports and Istanbul, 2010 vs 2016
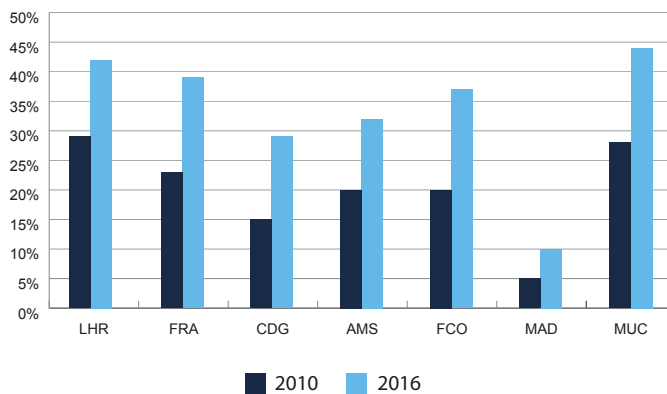
Source: Oxera analysis of OAG data.

Proportion of connecting routes (to/from Asia-Pacific only) at selected European airports competed by Middle Eastern airports and Istanbul, 2010 vs 2016
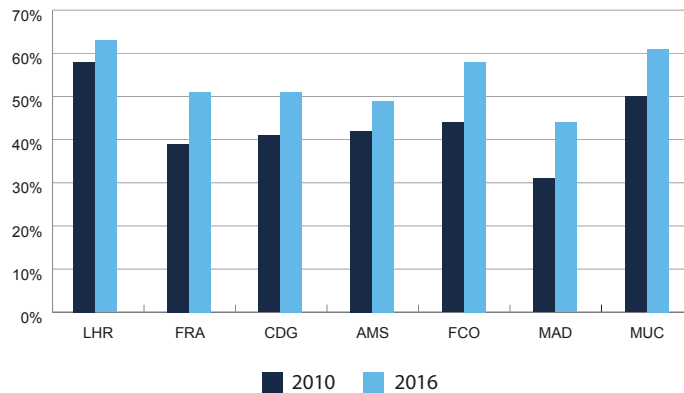
Source: Oxera analysis of OAG data.

➔ Besides the Gulf & Turkish hubs – more competitive pressures at home

The increase in the competitive pressure exerted by Gulf & Turkish hubs has coincided with **other market developments** within Europe also translating into **more competitive pressures for European hubs**:

- **THE DEVELOPMENT OF MULTI-HUB STRATEGIES BY THE MAJOR EUROPEAN AIRLINE GROUPS**

  In this regard, recent developments in **the relations between Frankfurt airport and the Lufthansa Group** are particularly telling. At the end of 2016, Lufthansa warned Fraport, Frankfurt's airport operator, that it could move some of its flights away from the airport due to its fee structure perceived as favouring rivals such as Ryanair. In June 2017, this was followed by the announcement that Lufthansa would be moving five Airbus A380s from Frankfurt to Munich. A Lufthansa spokesperson stated 'there is no direct connection [to the Ryanair dispute] but of course growth will happen where the best conditions are, and costs are of course a factor.' In turn, Fraport entered into a new agreement with Lufthansa which provided for reduced costs to Lufthansa. Et voila.

- **THE INCREASE OF DIRECT ROUTES RESULTING IN HUB BYPASS**

  The rise of the LCCs and their market penetration has resulted in the development of **new direct air services on routes which previously required a connection through European hubs**.

  For example, in 2010, passengers wishing to travel between Hamburg and Athens would have needed to connect via an airport such as Frankfurt, Amsterdam or Rome; now, they can simply use a direct service offered by easyJet or Aegean.

  Indeed, the Oxera study shows that since 2010 the availability of direct flights as an alternative to connecting services has increased across all of Europe's top 7 hubs. **This growth of hub bypass routes has added to competitive constraints for hubs**.

Proportion of intra-EU connecting flights via European hubs where a direct flight was available from origin to destination, 2010 vs 2016

Source: Oxera analysis of OAG data.
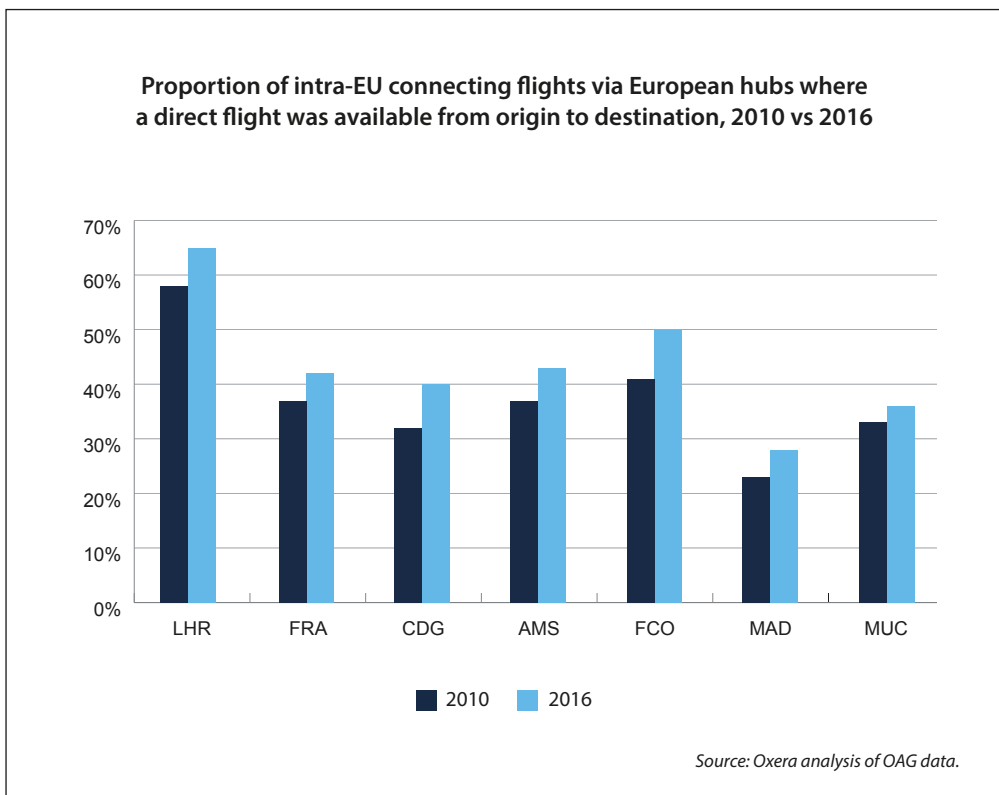
- **SELF-CONNECTIONS & LCCS DEVELOPING CONNECTING PRODUCTS**

The latest and upcoming development affecting Europe's established hubs is the development of **self-connections**, which has **paved the way for LCCs to develop their own connecting products**.

Several airports with predominantly point-to-point air services have been early adopters in seeking to help air travellers make their own hubbing-connections through their facilities, by offering a special service to this effect. **Dublin, Gatwick (GatwickConnects)** and **Milan-Malpensa (ViaMilano)** all offer this kind of service now and other airports are carefully taking note.

To give an example of the potency of self-connection, **at just 2 airports** that facilitate connections through guaranteed connection and bag transfer, a potential of **up to 11,000 connecting routes** have been opened up.

LCCs have noticed and have just recently launched their **own connecting platforms**, offering their passengers connections onto their own network or with other airlines flying long haul.

- Following the precedent set by Vueling, this Summer **Ryanair** started offering connections between its flights at Rome-Fiumicino and Bergamo-Orio al Serio airports.
- **easyJet** has just launched its new **"Worldwide by easyJet"** product at Gatwick, which ties up with GatwickConnects. easyJet presents this new connecting platform as replicating *"the costly and complex interline and codeshare structures of legacy airlines"* through self-connect and sales partnership enabled through a *"digital, virtual hub which will offer the same sort of connectivity but more simply and efficiently".*

There is no doubt that this further disruptive step in the evolution of LCCs business model will **increase hub competition** and that is now starting to **challenge established hub airports**.
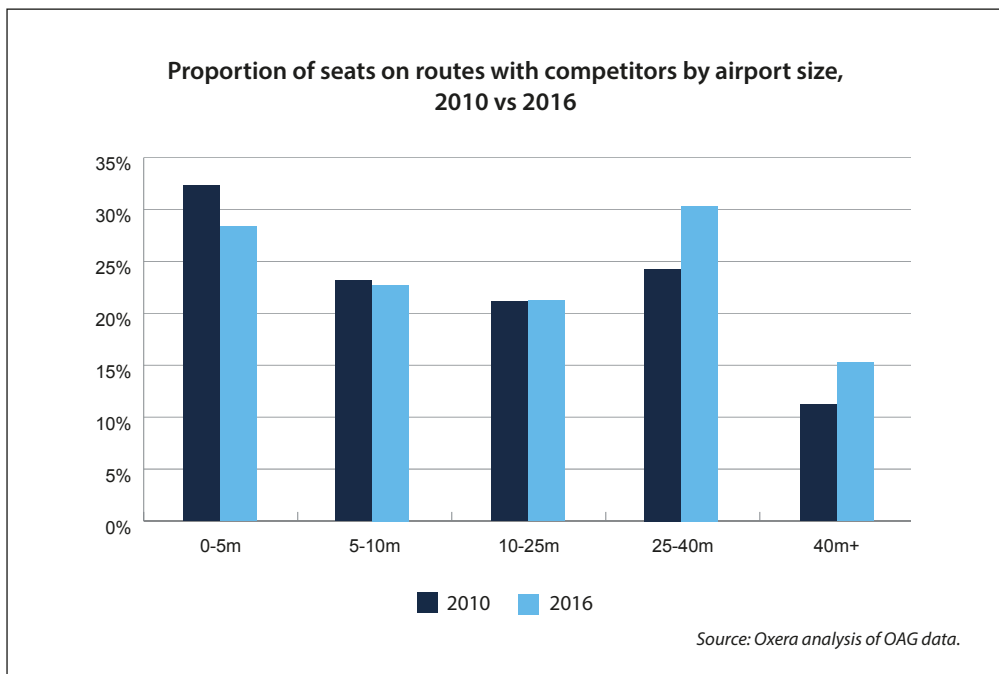
2.3   LOCAL COMPETITION STILL RISING

While competition on a Pan-European level for airline services and even beyond for transfer passengers has redefined the nature and the intensity of airport competition, the more traditional locally based competition between airports serving the same catchment areas has not stood still.

Previous research has already established that **63% of European citizens live within 2 hours of at least 2 airports**. But for local competition to be effective, passengers need to actually have similar options in terms of available routes and frequencies. This is precisely what the Oxera study has been looking into.

The study found that for larger airports, the proportion of traffic at these airports for which passengers can find alternative airports at other airports nearby has increased – pointing to growing local competition.

- **Key fact**: the total number of (capacity weighted) air routes with at least one competitor within 100 km of the departure airport **has increased from 21% to 23% since 2010**.
- **Key fact**: while the proportion of locally competed traffic at small and medium sized airports (below 25 mppa) has tended to decline slightly from a very high level, it has **increased significantly for airports with more than 25 million passengers**.

Proportion of seats on routes with competitors by airport size, 2010 vs 2016

Source: Oxera analysis of OAG data.

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Along with improved surface access by rail or by car/public transport, this increase in local competition also reflects airports' own efforts to expand their catchment area as much as possible. For example, Vigo airport in Portugal worked with a bus company to create a dedicated airport line to the Galicia region in Spain to expand its catchment area, ensuring the service was convenient and comfortable.

2.4   CONVERGENCE OF COMPETITION PRESSURES

Overall, the Oxera study reveals that **competitive pressures are progressively converging across the industry** – while these competitors pressure initially developed and focused on smaller airports, they are now also at play at large & very large and hub airports.

The **strength** and **cumulative impact of these competitive pressures** is now such that they are framing the behaviour of airports. What is at play here at industry level is an unprecedented **shift in the balance of the airport-airline relationship** – with airlines now increasingly able to exert dominance.

Summary of findings: changes in airport competition

Airport size (mppa)	New/existing routes	Connecting passengers	Local catchment
0–5	←→	n/a	↓
5–10	←→	n/a	←→
10–25	↑↑	n/a	←→
25–40	↑	n/a	↑↑
40+	↑	↑	↑↑

Source: Oxera.

Clearly, within each airport size category there are various situations.

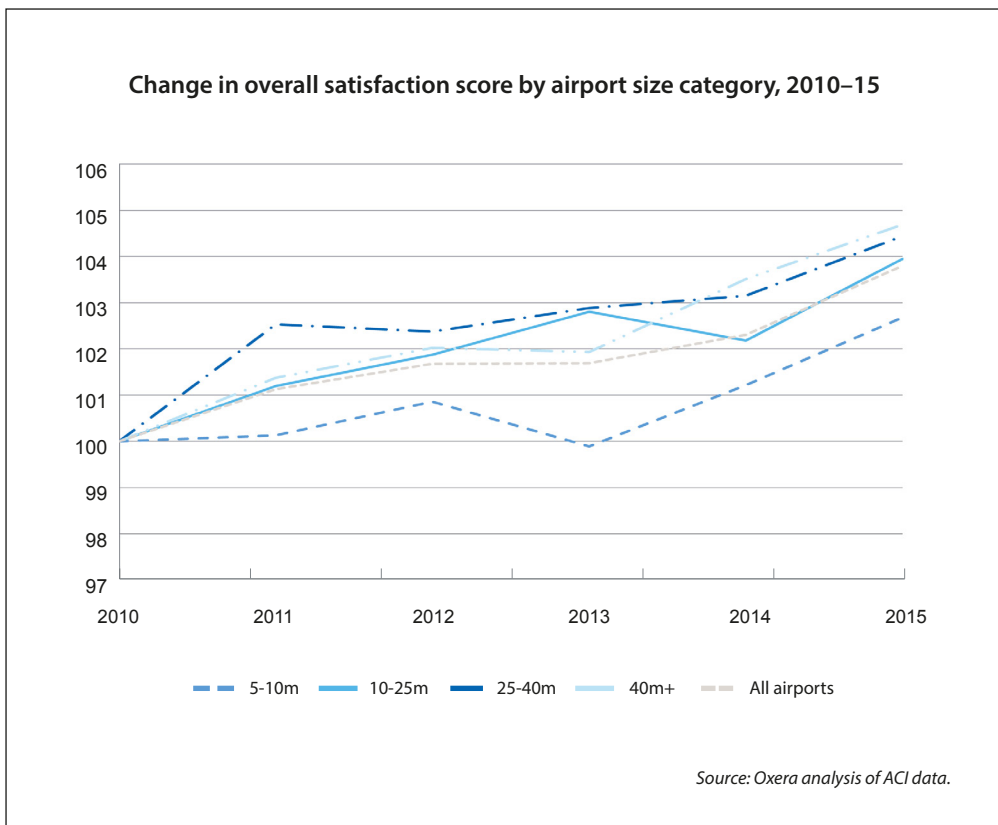| less than 10mppa	more than 10mppa & less than 25mppa	more than 25mppa but less than 40mppa	more than 40mppa
Competition remains high for small airports because of the continued significant presence of LCCs, the associated extent of switching by these airlines and the strength of the competition for airlines' services on new and existing routes.	These airports are now competing much more strongly for airline services on a Pan-European basis. Given the growth in LCCs since 2010, the extent of switching seen at these airports has increased significantly along with implication for airlines' buyer power. The market penetration of non-European airlines (especially Gulf airlines & Turkish Airlines) has also led to increase competition for spokes to their hubs.	Competitive constraints on those airports have also increased as a result of the growing presence of LCCs and consequent increases in route churn. The market penetration of non-European airlines (especially Gulf airlines & Turkish Airlines) has also led to increase competition for spokes to their hubs. These airports have also seen more competition from other airports serving the same catchment area.	This category includes Europe's large hub airports, which now face particular pressures on their transfer passenger business. LCC market penetration is also starting to become a reality – while route churn increases show that these airports are now having to fight to maintain existing airline services as well as new growth. Notably, these airports have faced the greatest increase in competition on routes from nearby airports. These airports have increased their service quality since 2010 by more than any other airport category and invested in substantial increases in capacity.

3

MARKET OUTCOMES

The Oxera study also looks at how the industry developments and increasing competitive pressures it has identified translate into market outcomes – especially as regards **prices (airport charges), quality and capacity**.

- **Key fact**: there is an almost balanced split between the number of EU/EEA airports that have increased their charges **(35)** and those that decreased them **(31)** – with the result showing no significant variations across the different airport size categories. The fact that airports have not systematically been able to raise charges and that many actually decreased them is consistent with the increase in competitive pressures that Europe's airports are now facing.

Number of airports obtaining real changes in aeronautical revenue per passenger by size category, 2009 versus 15

Increase
Decrease
No data

Source: Oxera analysis of ACI data.
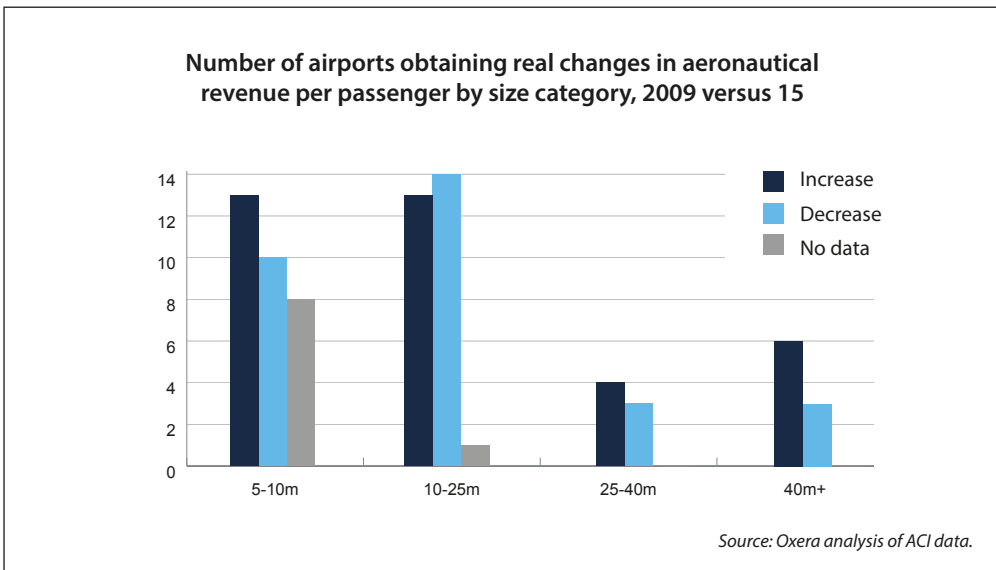
Of course, one should not assume that competition needs to systematically translate into decreases in charges. Airport costs are primarily driven by investments in capacity and quality (which are also important aspects of airport competition as well) and by regulatory induced costs over which they have no control (in the fields of security, safety and the environment). Airlines themselves face significant competitive pressures. This has not prevented air ticket prices in Europe from increasing by **+29%**[1] between 2005 and 2015.

• **Key fact**: European airports have **significantly increased their quality levels since 2010**, especially larger airports (above 25 mppa). These same airports have also **significantly increased their capacity**.

Change in overall satisfaction score by airport size category, 2010–15

Source: Oxera analysis of ACI data.

The top 21 EU/EEA airports have collectively increased their capacity by **+177.4 mppa** between 2005 and 2015. That increase is equivalent to adding another London-Heathrow, Paris-CDG and Paris-Orly to the European airport network.

Airlines often accuse airports of over-investing and link the accusation to the lack of competitive pressures to discipline airports' behaviour as regards charges and investments. Yet, it is striking to note that the capacity created by these airports almost perfectly matched traffic growth (over the same period, these airports saw their passenger traffic increasing by **168.5 million**). This actually points to airports being very disciplined and cautious in investing in new capacity – no doubt a reflection of competitive pressures.

Quality and capacity are essential features of airport competition. Indeed, airports do not only compete on price, but also on the quality/efficiency of their facilities and on the capacity that allows to attract new air services and grow their business. The findings of the Oxera study on capacity and quality are thus consistent with the way airport competition has developed and increased in Europe.

4

WHAT ABOUT THE FUTURE?

Airline consolidation will only reinforce airline dominance, posing greater challenges for airports. This is something airlines themselves are unabashed about predicting.

With so much having occurred in the past 6 years, it is reasonable to expect that the trends underpinning the evolution of airport competition are likely to continue for some time – on the back of demand for air transport that is set to keep growing.

The LCCs revolution is not over yet. LCCs' market expansion into larger airports & primary markets is now being supplemented by their foray into long haul and connecting traffic. Their ambitions are surely reflected in the fact that in Europe alone, these airlines have more than **1,000 aircraft** on order. Beyond fleet expansion, more disruption will also come from **big data** and **technology**. Earlier this year, Ryanair asserted that through its Ryanair Labs arm, it will continue to disrupt business models across air travel, from airports to travel websites and beyond.

> *"The future of air travel is that the clever airlines are going to 'own' the customer… We own the future of travel. Nobody else is going to come remotely bloody close to us."*
> **Michael O'Leary**, CEO, Ryanair (June 2017)*

Outside Europe, there is no reason to believe that market disruptions will come to an end either. While Gulf carriers & Turkish Airlines and their hubs have also changed the face of Global aviation, the market power of **Chinese airlines & airports** is still in the making – and is likely to have a far-reaching impact on airports well beyond the Asia-Pacific region.

Finally, a key development that will further intensify airport competition in Europe will be **airline consolidation**. Aer Lingus being snapped by IAG and Air Berlin's activities set to be grabbed by the Lufthansa Group are recent examples – but there are more to come.

> *"When fuel picks up you will see more airlines go out of business, you will see a period of consolidation. What you will end up with is the five big airlines - Ryanair, Lufthansa Group, IAG Group, Air France, KLM and easyJet - moving from somewhere less than 60pc market share to something like 85pc market share and you'll have less airlines in Europe, just as is the case in the US."*
> **Kenny Jacobs,** Chief Marketing Officer, Ryanair (August 2017)**

With **airport competition having expanded across the airport industry**, the resulting diminution in airports' market power and outcomes that reflect these new competitive dynamics, there is little doubt that **considering airports as natural monopolies is no longer a credible stance**. And the prospective market developments that we have just outlined only confirm the obviousness of this.

Ultimately, **the 'new normal' of the airport-airline relationship** evidenced by the Oxera study will **need to be reflected in the way airports are regulated**. This should actually question the need for any ex-ante regulation of airports – or at the very least result in less, more focused and proportionate regulatory intervention.

> *"Oxera's report for ACI EUROPE underlines the extent to which airport competition, often pitting airports in different parts of Europe against each other for highly mobile airline business, has continued to develop. The enhanced market penetration of LCCs and growth of Gulf and Turkish carriers has meant that the resulting competitive pressures are now increasingly felt also by larger airports. Consumers benefit as airports compete not only on price, but service standards and capacity. This is a success story for the European Aviation Area complementing the advantages brought to passengers by airline access and competition."*
>
> **Dr Harry Bush**, former Group Director of Economic Regulation at the Civil Aviation Authority in the UK

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* https://fora.ie/ryanair-future-travel-3464619-Jun2017/
** http://www.independent.ie/business/irish/ryanair-out-to-be-travels-amazon-selling-for-rivals-36026071.html

In the years during and following the global financial crisis, the economics of the air transport sector weathered some significant change. With the landgrab by Low Cost Carriers seeking market share in Europe, in parallel to newcomers from the Middle East and Turkey establishing more and more long haul air services from Europe, the competition between airports moved up several gears too.

In order to grasp the full extent of the implications, ACI EUROPE commissioned Oxera to research, examine and analyse the current state of airport competition in Europe. The resulting study, entitled *"The Continuing Development of Airport Competition"*, builds on a growing body of work about Airport Competition, including the 2012 study, *"Airport Competition in Europe"* by Copenhagen Economics and the ACI EUROPE publication *"How Airports Compete"* and others.

ACI EUROPE is the European region of Airports Council International (ACI), the only worldwide professional association of airport operators. ACI EUROPE represents **over 500 airports** in 45 European countries. Our members facilitate over 90% of commercial air traffic in Europe: **2 billion passengers, 20 million tonnes of freight** and **23.7 million aircraft movements** in 2016. These airports contribute to the employment of **12.3 million people**, generating **€675 billion** each year **(4.1%) of GDP** in Europe.

EVERY FLIGHT BEGINS AT THE AIRPORT.

Released at the European Aviation Club in Brussels on 26 September 2017.