Economic inefficiencies and over-regulation in air transportation – current issues in Europe

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Overview

1. Introduction
2. Framework: Some fundamental changes in air transport
3. Do all stakeholders work efficiently?
   1. Airlines
   2. Airports
   3. Regulators / Policymakers
4. Conclusion
1. Introduction

What is efficiency?

- To do things right!
- Profit-maximization (company resp. total welfare level)

Is air transport provided in an efficient way?

Where – in the sector – are efficiency gaps worth pointing a finger at?

- Airline-related issues
- Airport-related issues
- Policy-related issues
2. Some fundamental changes in air transport

- The world has changed, new economies have emerged
  - BRIC was only the beginning!
  - Declining dominance of Japan-US-Europe-axis
  - New traffic flows

- Cost increases (fuel, security, environmental…)

- Liberalized vs. isolated (air transport) markets
2. Some fundamental changes in air transport

- **LCC** operating in growing P2P markets, taking over the bulk of continental traffic

  Air travel = commodity

- However, **airports do not all grow at the same pace**
  - **LCC** need cost-efficient airports and ATM to be able to implement their business model
  - **Network carriers** need sufficient hub capacities to grow on long haul markets where they are condemned to succeed
3. Do all stakeholders work efficiently?

3.1 Airlines

- **Low Cost Carriers: efficient business models**
  - Low operating costs
  
  ![Chart showing unit costs versus stage length](www.airlinetrends.com)

- Main risk: External cost increases
  - Charges
  - Taxes
  - Fuel
  - Security…

[Chart from www.airlinetrends.com]
3. Do all stakeholders work efficiently?

3.1 Airlines

- Legacy carriers: Sustainable business models?
  - Small, mixed fleets

**AUA:**
76 aircraft
8 aircraft types
4 manufacturers

**Ryanair:**
303 aircraft
1 aircraft type
1 manufacturer
3. Do all stakeholders work efficiently?

3.1 Airlines

- Legacy carriers: Sustainable business models?
  - Small, mixed fleets
  - High overhead costs
    - General Overhead

Headquarters LH

Cologne: Built 2006 to be closed 2017
Cost: ??? €

FRA: Cost: > 200 Mio €

Headquarters Ryanair / easyjet

Ryanair old HQ (left): Cost: 3,2 Mio. € + 244,000 € rent p.a.
Ryanair new HQ: Cost: 20 Mio. € minus annual rents from 3rd parties

easyJet HQ: former aircraft hangar
Cost: ??? €
3. Do all stakeholders work efficiently?

3.1 Airlines

- Legacy carriers: Sustainable business models?
  - Small, mixed fleets
  - High overhead costs
  - Old-school pricing / Frequent Flyer Programmes: Why make things simple when one can make them complicated?
    - FRA-JFK oneway 2,627 € (economy), return from 548 €
    - Reward ticket DUS-Paris v.v.: 30,000 miles + 144 € Tax
    - 30,000 miles = up to 120 return flights in economy class
    - Normal ticket same date: 48 € + 50 € Tax = 98 €
    - Spiegel.de: „Lufthansa miles have a purchasing power similar to the Sudanese Pound“


Sooner or later, passengers will notice they get ripped off
3. Do all stakeholders work efficiently?

3.2 Airports

- Is capacity provided where needed?
  - No!
  - Overcapacity vs. underinvestment

**Ciudad Real Airport, Spain**

Spain’s €1bn white elephant airport could be yours for just €100m

The first private international airport in Spain that turned into one of the country’s biggest white elephants is being sold off for just €100m.

Source: http://www.telegraph.co.uk/finance/newsbysector/transport/10228961/Spains-1bn-white-elephant-airport-could-be-yours-for-just-100m.html

Source: DLR
3. Do all stakeholders work efficiently?

3.2 Airports

- Overpriced investments
  - Berlin (too small and too expensive)
  - Dublin Terminal 2 („gold-plated“ €609M terminal)
  - …

- Airline views hardly considered in planning processes
  - Cost
  - Night curfews…

- „Formula“ applied at many regional airports:
  - Expensive infrastructure + Public Service Obligations (as low charges are objected by EU)
  - = high costs and low traffic
3. Do all stakeholders work efficiently?

3.3 Regulators / Policymakers

- **Slot Allocation:**
  - Grandfathering at highly constrained airports, even for small aircraft (=low slot productivity)
  - Market entry for LCC at hubs difficult

- **Bilateral Air Service Agreements:** Cap on frequencies/destinations to protect national carriers

- **Consumer protection:**
  - 250-600 EUR compensation in case of cancelled flights, regardless of the ticket price
  - Railways: 25% of ticket price
3. Do all stakeholders work efficiently?

3.3 Regulators / Policymakers

- **Airline Mergers:**
  - Trans-border mergers virtually impossible due to ownership clauses
  - This promotes the high level of fragmentation in the industry

- **Taxation:**
  - High passenger duties especially in Europe
  - Incentive to operate smaller, less fuel-efficient aircraft and to charge higher fares
  - Negative welfare effect as air transport facilitates global trade

- **ATM / Single European Sky:** No progress

Rising costs, rising fares, declining demand!
Is there any industrie which is less regulated than air travel?
4. Necessary steps

Traditional airlines:
- Simplify your business to reduce costs!
  - You don’t need 8 different aircraft types and a €200M HQ to produce a good inflight product!
  - Is it really essential for your platinum customer to select between Porsche Cayenne and Mercedes for the aircraft transfer?
- Provide your consumer with a real added value, and not with fakes!
- …

Airports:
- Earn your money with retailing, parking etc.!
- Keep your costs down and your processes simple, avoid gold-plating!
- Do not invest in infrastructures that are not needed by the airlines!
- …

Policymakers: Treat air transport like other industries!
- Let the suppliers decide where to invest!
- Market protection reduces consumer welfare … and promotes inefficiencies with the carriers!
- Don’t charge taxes exceeding the ticket price!
- Does overexaggerated consumer protection really help the customer?
- …
Thank you!

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