

Distortions to Airport Competition: *Guidelines for a level playing field*

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The Emergence of Airport Competition

1960s: Airports-monopolies in their catchment area

- Only one airport in most regions
- Limited ground transport between regions
- Government operated entire airport systems (typically)



The Emergence of Airport Competition

Today: increasing airport to airport competition

- **New airports build in catchment area**
- **Military fields converted around catchment area**
- **Improved ground transport**
- **Privatization of some airports**
- **Multiple operators**
- **Branding of airports**



The Emergence of Airport Competition

LCC model: Use cheaper, secondary airports

- Cheaper for air carrier
 - Lower aeronautical fees at converted fields
 - Higher aircraft productivity
 - 3 min vs 20 minute taxi time
 - Uncongested operations improve service reliability and reduce airline operating cost
- Passenger charges less
 - e.g., parking



Emergence of Airport Marketing

- **1970s: non-existent**
- **1980s: some airport marketing to airlines**
 - **Primarily spoke end airports seeking hub service**
- **1990s: active airport marketing**
 - **Airports solicit new/expanded/better timed air carrier service**
 - **Hubs seek intercontinental linkages**
 - **Some passenger marketing**
 - **Development of financial incentives to air carriers**

Emergence of Airport Marketing

- **2000s: airport marketing is major management area**
 - **Large budgets linked to incremental airport revenue**
 - **Emergence of airport marketing institutions**
 - **Routes, Network, Jumpstart conferences**
 - **Trade magazines, major consultancies**
 - **Adoption of modern route planning methods**



Questions Regarding Airport Competition

- 1. Does Airport Competition exist?**
 - Yes
- 2. How do airports compete?**
 - Other presentations
- 3. Is airport competition sufficient to constrain airport pricing?**
 - Not a topic today
- 4. Do government policies distort airport-to-airport competition**

Who is the Airport Customer?

Who are the airport's customers?

- **Traditional: airlines**
 - They pay the fees to airports
- **Today: airlines and passengers**
 - **Passengers pay fees to airports**
 - **Parking**
 - **Food/beverage/retail/services**
 - 50% of total airport revenue
 - **Direct passenger charges**

Types of Passenger Choice of Airports

1. **Airline A service from Airport ORG (origin) to destination FUN.**
2. **Airline B service from Airport ORG (origin) to destination FUN.**
3. **Airline C service from Airport ALT (near origin) to destination FUN.**
4. **Airline B service from Airport ALT (near origin) to destination FUN.**

B serves both airports

Types of Passenger Choice of Airports

Literature on Air Fares

- **LCC Service at alternative airport**
 - Reduces fares at primary airport 10-20% (SNIP)

No research on effects on airport charges

- But clearly passenger purchase of tickets influenced by airport competition

2. Enter your origin and destination cities



Round-Trip

From:

Vancouver

To:

Barcelona

Compare Surrounding Airports

Passenger Choice of Airports

Passenger choice of airport is a function of:

- **Air fare.**
*the all in fare,
including fuel surcharges and charges for ancillary service*
- **Certain airport prices.**
Airport charges directly on passengers
- **Government taxes on passengers at specific airports**
- **Prices of complementary airport services**
especially parking, but other prices are involved as well
- **Airport Service level**
- **Consumer perception of airport (*tastes*)**
- **Ground access time to the airport.**

Airline Choice of Airports

Airline choice of airport is a function of:

- **Airport charges**
- **Other costs at the airport**
*e.g., fuel costs may differ by airport,
including airport specific 'fuel flowage' charges*
- **Airport levels of service**
*E.g., congestion level
This can significantly affect airline operating costs*
- **Percent of metropolitan area
that generally utilised the airport**

Sources of Distortion in Airport Competition

1. **Airport Incentives to Airlines**
2. **Non-airport Commercial Incentives to Airlines**
3. **Government Fees**
4. **Modal discrimination**
5. **Land Rents**
6. **Property taxes linked to Governance Model**
7. **Governance Model**
Multi airport vs. single airport

#1. Airport Incentives to Airlines

- **Increasingly common in past 20 years**
 - **Discounted or zero aeronautical fees**
 - **Could be negative fees (subsidy to airlines)**
 - **Justified if strong cross-elasticity from aero to non-aero revenues**
 - Daily A320 generates roughly 100,000 pax/year
 - \$500,000 aeronautical revenue
 - \$2.3 million in incremental annual revenue (Parking, retail, pax fee)
 - SW typically starts with 10-15 flights per day (or Ryanair base)



Airport Incentives to Airlines

Airport Marketing Incentives Should be Allowed

- **These are price discounts**
They indicate competition is working
- **There may be price discrimination issues**
 - Can all airlines access the discount schedule?
 - But this does not distort competition ***between*** airports
- **Competition Law must be applied**
 - Price discrimination, predatory pricing

#2. Non-airport Commercial Incentives to Airlines

Paid by :

- **Passenger coalitions** (*e.g., Chamber of Commerce*)
- **Key businesses**
- **Motivations** (*lower price, greater capacity*)
 - **Create carrier competition**
 - **Obtain non-stop service**
 - **Increase capacity**

Non-airport Commercial Incentives to Airlines

Community based Non-airport incentives should be allowed

- These internalise an externality benefit
 - Beekeeper and apple orchard

#3. State Aid to Airlines

State aid should not be automatically dismissed

- In some regions, air access and affordability have significant externality (econ efficiency) benefits
 - This was motivation for much subsidy to transport
 - Railway land grants or direct subsidies
 - Airport/port land at no cost
- Each case needs quantitative justification
 - E.g., incremental visitor tourism tax revenue exceeds state aid to airport



#4. Modal Discrimination

**All modes must be treated equally
re government taxes and fees**

E.g., Border processing tax/fee

- **US and Canada only levy on air transport**
- **not on autos or commercial bus/rail**
- **Incentives push to drive/bus/rail across border**
 - **Distorts market**
 - **Duplicate infrastructure, lower Economies of Scale**
 - **Higher carbon impact**
 - **Affects upstream/downstream businesses**

#5. Land Rent Must be Justified

Many regimes provided land to airport for \$1

- **Original commercial airports**
- **Converted military fields**

**Most others provide land
at rate below cost of private land assembly**

- **Canada: rent is charged but below land assembly**
- **Australia: competitive bidding for airport shares**
 - **But in many cases, land element of bid was below private land assembly cost**
 - Exception: 2nd Sydney airport expected to be at land assembly cost

Land Rent Must be Justified

Inequitable treatment distorts competition

- **Canada charges airports annual rent**
US charges no rent
 - And US subsidizes airport capital and finance costs
- **\$10 per round trip passenger gap from rent**
 - 15% gap with other U.S. subsidies



Land Rent Must be Justified

Land Rents must be justified and treated consistently across airports

- **There may be externality justifications for reduced land access costs**
 - **But these must be justified**
 - **And there must be consistency at competing sites**
 - **Competitive bids for airport land could be problematic**
 - **Airport A has strong bids with high land values**
 - **Airport B bids reflect no land value**
 - **Is it more economically efficient to close airport B?**

#6. Property Tax and Airport Governance Model

In many jurisdictions

- **City enterprises pay no annual property tax**
- **Other entities pay tax**

In Canada, there is un-level playing field

- **City run airports have no tax**
- **Others pay considerable tax**
 - **Current disputes, but some proposed taxes are 25% of annual revenues!**

Property Tax and Airport Governance Model

Property Tax

should not depend on governance model

- **If there is economic justification (externality benefit) for property tax relief, then it should be available to any airport governance model**
- **If there is no justification, then city enterprise must make payment/grant in lieu of tax**

#7. Privatiser *en bloc* or Individually?

Typically, but not always:

- Privatisation *en bloc* generates greater proceeds to treasury
- A monopoly has a higher enterprise value
 - Value of land rents embodied in share price
 - Plus value of monopoly rents
- Privatising individual will reduce (but perhaps not eliminate) monopoly rents

#7. Privatiser *en bloc* or Individually?

En bloc airport corporations, typically, but not always:

- **Do little marketing**
 - Sometimes, civic groups will organise to market their airport
- **Will organise around a main hub**
 - And seek to protect the main hub
 - But protecting a hub is not possible in EU
 - Traffic will be diverted to other hubs in other countries
- **Will rarely discount airport fees or provide other incentives**

#7. Privatiser *en bloc* or Individually?

En bloc airport corporations deliver lower economic benefits to their regions

- **The removal of competition results in higher prices**
- **Non-hub airports have lower service**
 - **Fewer non-stop flights**
 - **More routing via national hub and competing hubs in other countries (hence higher fares)**
 - **This applies to air cargo as well.**
 - **Often trucked to main gateway rather than flown direct**

#7. Privatiser *en bloc* or Individually?

If economic efficiency and the large regional benefits of competition are the objective, then do not privatise *en bloc*.

If maximum cash to the treasury is the objective, then privatise the monopoly *en bloc*.

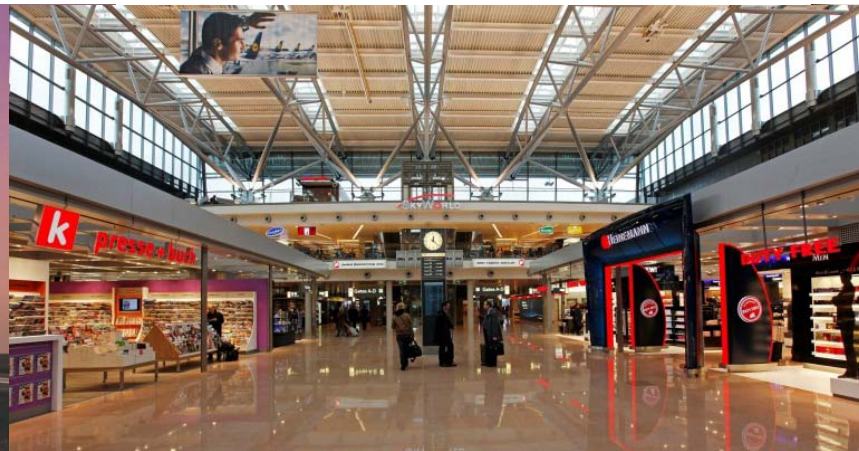
- **The conflict between the two objectives is obvious**
- **It can pit regional against federal interests**

#7. Privatised *en bloc* or Individually?

- **Examples**
- **BAA, privatised *en bloc***
 - Monopoly profits subjected to one time \$500 million pound tax on shareholders
 - Competition Authority later pursued breakup of BAA
- **Australia, privatised individually**
 - Government chose regional development over maximum cash to treasury
- **Canada, “privatised” individually**
 - Agenda was driven by local communities, not by treasury objectives

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