

Competition Commission's Airports Market Investigation: Invitation for submissions

Submission from Gatwick Airport in response to the Competition Commission's invitation of 18 November 2010

Competition: One year on

Introduction

We welcome the Competition Commission's (CC's) invitation to provide evidence on the need for further airport disposals by BAA. It is now a year since Gatwick changed ownership, and we also reflect on how a year of competition has benefited passengers and airlines.

On 18 November, the CC invited submissions on whether there have been any relevant developments it should take into consideration since it made its decision in March 2009 requiring BAA to sell three airports (including Gatwick Airport, which was sold to GIP in December 2009). In particular, the CC wants to consider representations on whether there have been any developments which constitute a material change in circumstances such that it should amend the remedy package set out in its report, for example, the timing of the proposed divestitures. The CC in its invitation identified three specific such developments which might be relevant:

- the decision by the Coalition Government to cancel the building of a third runway at Heathrow Airport and to oppose new runways at Gatwick and Stansted airports;
- changes in the economic climate and financial market conditions since the report was published; and
- issues identified regarding the ease of separation of airports, such as separation of IT facilities.

This submission sets out Gatwick Airport's view on each of these developments. We have limited our submission to commenting on the remedy requiring BAA to divest Stansted Airport.

Current Government's decision to oppose additional runway development in the South East

Additional runway capacity, when delivered, would provide a source of downward pressure on prices from the current level in the South East market, due to the increase in supply. However, as noted by the CAA in its work to develop competition guidelines¹, scarcity in a market is not per se a

¹ See a discussion of this issue in the CAA's Competition Guidelines Issues paper at <http://www.caa.co.uk/docs/5/ergdocs/CompetitionGuidelinesIssuesPaper.pdf> paragraphs 4.19 to 4.35.

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barrier to effective competition in a market. The CAA, in its Issues paper, makes the critical distinction between temporal scarcity, underlying scarcity and artificial scarcity, with the latter being potential evidence of market power and competition problems. In contrast, the former two forms of scarcity are characteristics present in a number of effectively competitive markets. These include, but are not limited to, housing markets in desirable geographic locations, mobile telephony markets, where there is a scarcity of suitable spectrum, airline markets and oil and gas production markets.

Runway capacity scarcity in the South East can be thought of as either being temporal (depending on the time period used) or underlying. The fact that there is such scarcity has not, and will not, prevent the development of effective competition between airports under separate ownership. Moreover, while the lack of additional capacity in the South East might preclude one source of downward pressure on prices, this source of downward pressure on prices will be absent in both cases of common and separate ownership of airports.

Moreover, the CC itself recognised in its Airports Market Investigation that separate ownership will provide competition both within existing capacity but, importantly, competition for new capacity – which may or may not include more runway capacity. Gatwick will shortly be publishing its Masterplan which outlines the long term development potential of the airport. This will include various runway options, including a second runway.

We recognise of course the policy of the current Government, and we will be engaging with the Government as it seeks to develop a new policy framework. The case for extra runway capacity in the South East has not gone away, and we will be pressing the Government to update the analysis that supported the 2003 White Paper. It seems to us that as the Government considers the future of aviation, an independently owned Gatwick can only help the development of a coherent, evidenced policy. If and when government policy changes, then – as concluded by the CC in its Airports Market Investigation report – passenger and airline interests would be best served by airports being in separate ownership and competing for the right to be the provider of additional capacity.

We note in passing that continual changing of Government policy makes it very difficult for companies to commit to long term infrastructure development, a theme that was reflected in the CC's report.

Benefits of competition: Gatwick experience

As noted above, effective competition can be achieved in markets with scarcity and this is a common feature in many markets. In terms of competition between airports, the sale of Gatwick from BAA to GIP illustrates the benefits to passengers and airlines that can be delivered through separate ownership and competition, even where there are capacity constraints. Examples of these benefits over the last 12 months include:

- Initial focus on passenger security screening to ensure that we provide a product that meets our passengers' needs, in some cases exceeding the quality standards required by the current regulatory price control settlement;
- A comprehensive review of the BAA capital investment programme to ensure that it was fit for purpose and delivered in the passenger and airline interests. We have been able to identify

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major cost savings compared to the BAA plan, as well as delivering more projects than the BAA plan. This has led to:

- cancellation of the development of Pier 7 as it was judged too expensive for the increase in pier served stands; we now have plans to provide pier service by an extension to Pier 6, a much more efficient option;
 - cancellation of the refurbishment of Pier 1, with a revised combined Pier 1 and south terminal baggage factory at a significant saving;
 - the introduction of a new south terminal security project, to provide a world-class security product;
 - revising the proposals for the south terminal forecourt redevelopment to ensure that it is passenger focussed;
 - implementing a new car-park construction process that has allowed a faster construction process.
- The re-opening of the inter-terminal transit system two months earlier than planned for by BAA, in time for the summer peak;
 - The introduction of our innovative Assistance Lane security screening for passengers with reduced mobility (PRM) and families with young children, to help to reduce the hassle and stress of passing through security;
 - Collaborative working between the airport, airlines and NATS to explore ways to increase the capacity of the airfield, within existing infrastructure limits;
 - Collaborative working with Network Rail to secure a £53 million upgrade to the Gatwick Airport rail station;
 - Re-contracting the provision of PRM services as the previous contractor was not delivering a sufficient service;
 - Introduction of a long-haul incentive programme to help airlines establish and sustain new long-haul services from Gatwick;
 - Securing the granting of initial permissions to allow for the commercial operation of A380 aircraft;
 - Achievement of a number of environmental standards;
 - Pioneering innovative check-in products with airlines to make the check-in process more passenger friendly; and
 - Publishing ground-handler baggage performance in an effort to provide transparency for passengers and drive up service delivery.

These achievements highlight some of the changes that can be achieved through separate ownership and the competition between airport operators that this brings, even within existing capacity and regulatory constraints.

Our experience also demonstrates that there is active competition between airports in the South East, with airlines expanding the number of services from Gatwick and actively taking advantage of the opportunity to switch their services between competing airports. For example, Norwegian switched its base from Stansted, Air Berlin introduced new services from Gatwick in preference to extending its operation at Stansted, Ryanair similarly introduced new winter services from Gatwick, in preference to Stansted and BA extended its range of services from Gatwick. However, some airlines are signalling a reduction in routes from the airport. While this is not good news from Gatwick's perspective, this is a further demonstration of the competitive environment in which we now operate, which can only be in the interests of passengers.

Taking all of this together, we do not consider that the change in government policy on runway capacity in the South East is a material change in circumstances which would warrant the overturning of the CC's report findings.

Changes in the economic climate and financial market conditions

The economic recession has clearly had a detrimental impact on the whole air sector. At Gatwick, passenger numbers are down by around 4 million passengers per annum from our peak. This fall has also been seen at Stansted and Manchester. Interestingly, Heathrow's traffic has been much more robust, highlighting the unique nature of that airport and the significant constraints that it imposes over competing airports in the South East. Despite these challenging times for airports, there seems to be no reason why the benefits that separate ownership has already brought to passengers and airlines at Gatwick should not be seen by users of Stansted. We do not therefore see a case for changing the CC's remedy.

Issues identified regarding the ease of separation of airports

The experience of the sale of Gatwick to GIP shows that it is possible for BAA to divest an airport while that airport continues to provide high quality and innovative service and operations to passengers and airlines. However, the sale of Gatwick also demonstrates that there are a number of complex issues that need to be addressed, including the separation of IT systems. At Gatwick, there were 143 separate BAA systems to be separated. Full separation from BAA remains some months away.

The other areas where there were significant practical implications arising from the separation of Gatwick from BAA were concentrated on the provision of stand-alone capability to the airport management, legal and regulatory functions. This included the recruitment and formation of a new management executive team as well as for our public affairs, regulation, legal and finance teams. We also constituted a Board of Directors, and introduced associated Board reporting and other relevant governance processes. It is important to note that we did not experience any significant operational issues arising from separation.

The experiences at Gatwick clearly show that there will be much to be done in the event of divestment by BAA of Stansted. We would also note that although there have been a number of complex issues related to separation, particularly in relation to the separation of IT systems, BAA and Gatwick have worked constructively with each other throughout this process of separation. This has eased the process and made separation more efficient than it could have been.

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Our experiences demonstrate that the complexities involved in separation is not a material change in circumstances which would warrant the overturning of the CC's report findings and should not be a barrier in itself from requiring the divestment by BAA of Stansted.

Conclusion

The issue of capacity constraints in the South East is not a bar to the development of effective competition between airports. The experience at Gatwick clearly demonstrates that there is scope for airports to increase their efficiency and introduce innovation to the provision of services to passengers and airlines.

Gatwick considers that the interests of passengers will be best served by an effectively functioning market, with airports competing with each other to attract passengers and airlines. The achievement of this will only be aided by the divestment by BAA of Stansted. However, it is important that any future sale is conducted in a way that secures such a well functioning market and does not risk the creation of a dysfunctional one. If the market is dysfunctional, this can only act to increase pressures on the Government and the regulatory authorities (the CAA and the CC) to continue to intervene in the market dynamics. Such continued intervention can only hamper the development of effective competition and reduce the benefits of competition that this would bring to passengers.

We are happy for the CC to publish this submission.