

## **CAA Consultation - Economic regulation of Heathrow Airport Limited:**

### **H7 Initial Proposals (CAP2265A)**

#### **ABTA Submission - November 2021**

##### **Introduction**

1. Established in 1950, ABTA represents over 900 UK travel organisations, acting to advance their collective interests through giving a strong and united voice to the travel industry and supporting a successful and sustainable sector. Pre-pandemic ABTA Members represented more than £40 billion of consumer and business travel. Members constitute more than 4,300 consumer brands, with a workforce of some 80,000 employees and a further 12,000 self-employed independent travel agents.
2. ABTA's response to this consultation focuses primarily on Section 2, which sets out the provisional range for the H7 price control on airport charges, and Section 3, which describes the Civil Aviation Authority's (hereafter referred to as the 'CAA') approach to dealing with airport charges in 2022.
3. Heathrow Airport is a heavily constrained airport, where there is more demand from airlines wishing to use the airport than can be met by its capacity. More than 99% of available slots are already used by airlines. The 'passenger service charge' is normally passed through to customers as part of their air fare. Customers travelling from Heathrow already pay the highest passenger charges in the world.
4. ABTA recognises that, as has occurred across the wider travel ecosystem, Heathrow Airport Limited (hereafter referred to as 'HAL') has experienced extreme and unforeseen financial challenges because of COVID-19 and the subsequent restrictions that have been placed on air travel.
5. However, ABTA can see no justification for consumers being subjected to such significant increases in passenger charges to recoup losses of HAL, which is a privately operated business backed by wealthy global investors. There is little evidence that HAL has exhausted all alternative avenues open to it as an alternative to seeking such significant increases in passenger charges.
6. In addition, ABTA supports the CAA's approach to delay the full implementation of the H7 period, but believes a longer delay, until the end of 2022, would provide a better opportunity to accurately assess the recovery of air travel to and from the UK.

##### **Heathrow's proposals and passenger forecasts**

7. HAL has requested the CAA increase the cap on its charges per passenger to between £32 and £43.<sup>1</sup> These proposals are based on predicted lower levels of passenger numbers expected over the H7 period, which means that HAL has deemed airport charges will need to rise beyond

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<sup>1</sup> Figures taken from the updated business plan ("updated RBP") at the end of June 2021. Note: this takes into account the overall envelope of charges not just passenger service charge (including, for example, the cargo levy).

the level first identified in the revised business plan (RBP) in December 2020. Notably, however, HAL is forecasting a very slow recovery trajectory, which has resulted in excessively high figures for the proposed charges.

8. HAL is pessimistically forecasting a drop in demand of 36% in 2022, compared to IATA forecasting only a 5% reduction, versus 2019. HAL claims that 2019 levels of demand won't return until beyond 2026<sup>2</sup>, an average reduction of 24% in passenger volumes over the next five years (versus 2019). There appears to be little evidential basis supplied by HAL to support their forecast passenger levels.

#### **The CAA's provisional range for the H7 price control on airport charges**

9. In developing these Initial Proposals, the CAA has critically evaluated the passenger forecasts that HAL produced in its business plan and have assumed a level of passenger traffic about 7% higher than that assumed by HAL.
10. Nonetheless, these forecasts were produced some time ago and before the recent government announcements on the lessening of travel restrictions. ABTA believes the CAA assessment is likely to be pessimistic in light of the relaxation of restrictions on travel.
11. ABTA's own consumer survey, as well as the predictions on passenger growth put forward by the International Air Transport Association (IATA), both indicate that the passenger figures and trajectory of recovery for the sector put forward by the CAA and HAL are overly pessimistic. IATA expects Heathrow Airport is more likely to return to 2019 levels in 2024, due to its resilience as evidenced in previous crises.<sup>3</sup> While the pandemic is unprecedented, history has shown that HAL went into growth within months of the financial crisis. ABTA's recent consumer survey found that 61% of people in the UK were planning an overseas trip over the winter period, which represents a slight increase on 2019 levels. For summer 2022, consumers reported an intention to travel that would amount to 85% of 2019 passenger levels. Meanwhile, IATA has predicted that air traffic in the UK will recover to 95% of 2019 levels in 2022.<sup>4</sup> EUROCONTROL have also recently updated their forecast on the recovery of European air travel for next year, which is a significant revision of their May 2021 forecast, with the baseline scenario indicating 9.8 million flights in 2022, just 11% down on 2019.<sup>5</sup>
12. Given the assumptions the CAA has made on forecasts of passenger numbers, they have concluded that it is likely that there will need to be significant increases in airport charges per passenger to support the necessary further investment to maintain a safe, secure and resilient operation of the airport. The CAA also indicates it considers that passenger charges are a relatively small proportion of the costs of air travel from London Heathrow.
13. The top end of the CAA's Initial Proposals for a provisional range of airport charges over the H7 period is about £34.40 per passenger, which would involve a real increase in airport charges of around 60%. Meanwhile, the bottom of the CAA's provisional range for airport charges of about £24.50 would represent a real increase of about 15%.

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<sup>2</sup> H7 Revised Business Plan – Update 1

<sup>3</sup> IATA Tourism Economics Air Passenger Forecast, July 2021

<sup>4</sup> IATA Tourism Economics Air Passenger Forecast, July 2021

<sup>5</sup> EUROCONTROL Forecast Update 2021-2027, October 2021

14. ABTA believes that the proposed increases in the passenger charge put forward by the CAA, which is in the range of 15-60%, remains disproportionate and unfair to consumers.
15. While it is welcome the CAA has sought to reduce the level of increase put forward by HAL, we can see no justification for loading such a large proportion of the costs of recovery on to passengers using London Heathrow at this time, especially in the absence of any attempt by HAL to seek additional investment from shareholders.
16. Linked to the above, the CAA's analysis states that their Initial Proposals should be "acceptable for shareholders" in the notional business as they offer an expectation of returns consistent with the allowed cost of equity and would allow the notional entity to return to paying dividends before the end of the H7 period. Crucially, the Initial Proposals do not assume that the notional entity is supported by an equity injection.
17. ABTA is dismayed that in the midst of the worst crisis ever to hit the travel industry, HAL is trying to recoup all of its pandemic losses while increasing its profitability, prioritising its private shareholders at the expense of airlines and consumers. The entire aviation and travel industry has suffered greatly throughout the COVID-19 pandemic, but other businesses across the sector, including airlines, tour operators and travel agents, have not, and will not, simply be able to load the costs of recovery on to consumers in such a manner due to operating in a free market and with full price competition. The CAA must act to prevent an unfair sharing of the burden of recovery.

#### **The CAA's approach to dealing with airport charges in 2022**

18. HAL's current price control expires on 31 December 2021. At present, the final decision and licence modifications for a new five-year control period will not be made and take effect until the summer of 2022.
19. The CAA's Proposal is to introduce a holding price cap of £29.50 for 2022. This is in contrast to HAL's suggestion of airport charges of £37.6 per passenger (nominal prices) which has been derived from the assumptions included in HAL's updated RBP. ABTA is understandably concerned with both the scale of HAL's proposed increase in charges and the underlying assumptions (as outlined above). ABTA's position is that there should be no increase in the passenger charge for the interim period.
20. ABTA agrees with the CAA's assertion that they may need to put in place a licence condition to prevent HAL unduly increasing prices for 2022 to the detriment of consumers. Given the importance of 2022 to consumers any such licence condition would need to be in a form that compelled HAL to price no higher than the level of the holding cap in 2022 rather than leave its existing charging proposals in place and rely on the operation of the correction factor mechanism with the price control licence condition.

#### **Impact of the current proposals**

21. The proposed changes would clearly result in increased costs for consumers using Heathrow airport post-pandemic, of which a significant amount appears to be going to increased dividends paid to HAL shareholders. This is particularly hard to justify at a time when the entire aviation and travel sector is attempting to recover from the largest global crisis ever faced, in terms of the closure and severe restriction of international travel.

22. In addition, these proposals also undermine ambitions for 'Global Britain' and will damage Britain's economic recovery. Heathrow has already slipped to 10th busiest airport in Europe and the UK's only hub airport will become less attractive compared to EU hubs with extortionate charges that hamper competition and connectivity – presenting a disproportionate disadvantage to the home-based long-haul carriers that connect Britain to the world. The UK Government's stated 'Levelling Up' ambition would also be at risk, as many passengers using regional airports to fly long-haul will have no choice but to travel via Heathrow.

### **Conclusion**

23. ABTA believes the CAA has a duty to protect consumers, and the airlines that use Heathrow, and it must ensure a more equitable approach between all stakeholders. The current proposals do not, in our view, represent a fair and proportionate balance, with consumers still being asked – even at the lower end of the CAA range – to shoulder unfair costs with no input required by HAL shareholders.
24. With this level of uncertainty, the CAA should roll all current levels of charges to cover the entirety of 2022 so that full and informed assessment can be done to reach a fair settlement.
25. Heathrow's shareholders have benefited from a decade of growth in international travel to and from the UK, and yet have not invested permanent equity during the pandemic. Just as UK airlines have raised significant funds from shareholders to weather the pandemic, it's only right that Heathrow turns to its equity owners first, rather than expecting the CAA, industry and consumers to effectively compensate for its losses.
26. Following Heathrow's previous request for a RAB adjustment the CAA took the decision that an early intervention on the scale of its request – an attempt to recoup pandemic losses of £2.6bn – was disproportionate and not in the interests of consumers. The forecasts made by HAL within their proposals, and the resulting proposed level of charges, appear to be another attempt to disproportionately load the costs of recovery on to consumers. ABTA believes these attempts should be resisted on the same grounds.

### **Further information**

For further information, please contact ABTA's Public Affairs Team (E: [publicaffairs@abta.co.uk](mailto:publicaffairs@abta.co.uk))

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