



**UNITED KINGDOM
CIVIL AVIATION AUTHORITY**

DECISIONS ON AIR TRANSPORT LICENCES AND ROUTE LICENCES

4/98

Decision of the Authority on its proposal to vary licence 1B/13 held by British Midland Airways Limited and licence 1B/35 held by Virgin Atlantic Airways Limited heard on 26 November 1998.

Panel

Chairman: Miss G White
Mr R Birdseye

Adviser: Mr D Batchelor

Secretary: Mr G J Elsbury

Objections to the Authority's proposal:

Objector: British Midland Airways Ltd, represented by Mr M Crane QC, Instructing Solicitor, Mr T Soames, Norton Rose

Witnesses: Mr A Davis, General Manager Industry Affairs & Pricing, British Midland Airways Ltd

Sir Michael Bishop, Chairman, British Midland Airways Ltd

Objector: Virgin Atlantic Airways Ltd, represented by Mr R Lawson of Counsel, Instructing Solicitor, Miss J Durham, Virgin Atlantic Airways Ltd

Witnesses: Mr R Branson, Chairman, Virgin Atlantic Airways Ltd

Mr B Humphreys, Director of External Affairs and Route Development, Virgin Atlantic Airways Ltd

SUMMARY

1. This hearing was convened to decide which of two UK airlines should be allowed to operate between London and Moscow in addition to British Airways, given that the UK/Russia bilateral air services agreement currently restricts to two the number of airlines of each country permitted to operate on the route. British Midland Airways and Virgin Atlantic Airways were each seeking the second UK designation on the route.

2. This was a re-hearing of the case heard by the Authority on 25 August. Following that hearing the Authority found in favour of Virgin and published its reasons in Decision 2/98. In reaching its decision the Authority had regard, inter alia, to the fact that there could be no guarantee that an agreement which Virgin proposed to enter with Transaero, the second designated Russian carrier on the route, would be finalised. However, Virgin's plans were more advanced than BMA's and, if it did come to fruition, the proposed agreement would provide significant user benefits in that it would enable Virgin to operate seven services a week from the outset. BMA appealed against this decision and the Secretary of State held that the Authority was wrong in taking into account an agreement which could only be finalised after designation and with the agreement of the UK and Russian aeronautical authorities. Accordingly, the Secretary of State directed the Authority to re-hear the case on the basis that no more than four extra services a week are currently available to a second British airline on the London/Moscow route.

3. Having re-heard the case in accordance with the direction of the Secretary of State, the Authority has found in favour of BMA, having concluded that BMA's proposed London/Moscow service will further the interests of users more effectively than that proposed by Virgin.

THE NOTICE

4. On 5 August 1998 the Secretary of State, in exercise of his powers under Regulation 3(5) of the Civil Aviation Authority Regulations 1991, gave notice to the Authority that in his opinion, by virtue of provision made by or under the terms of the Memorandum of Understanding concluded on 21 May 1998 between Russia and the United Kingdom, the United Kingdom's share of capacity on air transport services between the United Kingdom and Russia which may be provided by British airlines would, within 6 months of the date of that notice, be insufficient to enable both Virgin Atlantic Airways Ltd and British Midland Airways Ltd to make available all the capacity which they planned to provide. This notice was published in the Authority's Official Record Series 2 on 11 August 1998.

THE PROPOSAL

5. Following the notice from the Secretary of State, the Authority published its proposal to vary the licences of British Midland Airways (1B/13/64) and Virgin Atlantic Airways (1B/35/141) in its Official Record Series 2 on 11 August 1998. After reciting the notice, this proposal stated that:

“2. The Authority is advised by the Secretary of State that not more than two UK airlines may operate from London and stop at Moscow and vice versa. British Airways plc is currently designated and operates such services. The UK may therefore designate only one further airline to operate services on the route between London and Moscow, and both British Midland Airways and Virgin Atlantic Airways wish to be the UK’s second designated airline on this route.

“3. For these reasons, the Civil Aviation Authority, in exercise of its powers under Section 66 (2) of the Civil Aviation Act 1982, hereby proposes to vary route licence number 1B/13 held by BRITISH MIDLAND AIRWAYS LIMITED (BMA) and route licence number 1B/35 held by VIRGIN ATLANTIC AIRWAYS LIMITED (Virgin) so as to provide that should it not be possible under the terms of the bilateral air services agreement between the United Kingdom and Russia for more than two British airlines to operate air services between London and Moscow, only one of BMA or Virgin may operate such services in addition to the existing services operated by British Airways plc pursuant to its designation by the UK Government with effect from 1 April 1984. Which of the two airlines may operate will be determined by the Authority in the light of its statutory duties and objectives and arguments advanced at the hearing.”

OBJECTIONS AND REPRESENTATIONS

6. British Midland Airways (“BMA”) exercised its right to be heard on the Authority’s proposal to vary its licence 1B/13 and made a representation in respect of the proposal to vary Virgin Atlantic Airways’ licence.

7. Virgin Atlantic Airways (“Virgin”) exercised its right to be heard on the Authority’s proposal to vary its licence 1B/35 and made a representation in respect of the proposal to vary British Midland Airways’ licence.

8. The Air Transport Users Council (“AUC”) made a written representation on the Authority’s proposal.

BRITISH MIDLAND AIRWAYS' CASE

9. BMA first applied for a licence to serve Moscow in March 1996. In the 1990s BMA had been pursuing a progressive and consistent commercial policy of developing services to major European capitals. In the 1970s BMA had been a regional domestic operator in the UK, in the 1980s it broke the monopolies of the domestic trunk routes, and the 1990s had been identified as a period for developing competition in Europe. While initially this had focused on high frequency routes to capitals in western Europe, growing slot congestion at Heathrow had meant that further expansion of international services from its Heathrow hub would have to be on routes requiring a smaller volume of slots and the airline had commenced services on a number of routes to eastern Europe. The proposed service to Moscow therefore represented an integral and consistent part of BMA's strategy of embracing the major eastern European capitals into its European network.

10. Indeed, BMA argued that, in addition to considerations of user benefit, there was also an issue of industry structure to be taken into account in this case. In its view, the addition of Moscow to the coherent European network operated from its Heathrow hub would enable BMA to derive operational and cost advantages which could, in turn, be passed on to users as benefits. In particular, the ability to combine passengers with different origins and destinations generally helped BMA secure higher traffic volumes and maintain viable operations. Restrictions on the ability of BMA to develop international connecting services from Heathrow would be likely, for example, to have an adverse impact on the performance of its UK regional services. It was relevant in this context that there had been significant increases in domestic passengers making international connections at Heathrow since 1984. Services of hub operators also tended to be more attractive to passengers by virtue of the enhanced frequent flyer benefits and corporate discount programmes they were able to offer. BMA was the only carrier in Europe offering a competing hub network to British Airways ("BA") on a pan European basis. In BMA's submission, Virgin did not operate a hub at Heathrow in the same sense. Rather it operated a number of flights on an independent basis and the connections between its existing services were not designed to feed each other in the same way as BMA's Heathrow services did.

11. BMA's plan was to use one of its four A321 aircraft, with a maximum capacity of 195 seats, to operate the Heathrow/Moscow route. Assuming a favourable decision from the Authority, it would be able to commence services on 1 February 1999, although in the event of an appeal against the Authority's decision BMA would propose to start services within eight weeks of an appeal decision. It would commence with four services a week and increase to a daily service from summer 2000, as permitted under the UK/Russia bilateral agreement. Its service would depart Heathrow at 0900, arriving in Moscow at 1545. The return sector would depart Moscow at 1655 and arrive back at Heathrow at 1755. This schedule would allow a check-in at Heathrow at around 0800 and would enable passengers travelling from Moscow to undertake almost a full day of business in Moscow prior to travelling to London.

12. In calendar year 1999, covering eleven months of operation, BMA forecast that it would carry 30,254 passengers at an average seat factor of 44%. In 2000, when it proposed to increase to a daily service from the beginning of the summer season, it would carry 61,338 passengers at a seat factor of 53%, and in 2001 it expected its traffic

to grow to 77,590 and its seat factor to 60%. According to these projections it forecast a loss of £217,000 in 1999, but anticipated returning a profit on the route of over £1.5m in 2000 and £3.1m in 2001.

13. BMA argued that it should be awarded the rights to operate as the second British carrier between London and Moscow for two principal reasons. The first was that it would best satisfy a substantial category of public demand which was not currently catered for adequately, namely UK-originating passengers who did not live in London or its surrounding area. Unlike Virgin, it proposed to offer a schedule which would provide new on-line connections for passengers between Moscow and six major UK regional airports. It would also offer its own round-trip connections between Moscow and a further five European cities, as well as connections with its wide range of code share partners to several international destinations. BMA believed the market between Moscow and the UK regions to be a potential market of size, citing in support the fact that around one third of the companies registered in the Russian-British Chamber of Commerce were based in the UK regions and KLM's active marketing of its own connections over Amsterdam to passengers travelling between Moscow and the UK regions. BMA believed that around 50,000 passengers a year might be travelling between the UK regions and Moscow, but that not all of this traffic would be identified in the CAA's statistics or survey data for a variety of reasons. Its traffic forecast included a conservative assumption that it would attract a proportion of this market to its own services, 4,500 passengers a year when operating four services a week, and 7,200 when operating a daily service.

14. Secondly, BMA believed that its proposal was best calculated to further the general interests of users. Its departure time from Heathrow of 0900 was clearly better tailored to the needs of the point-to-point market than Virgin's departure times of 0640 and 0730. BMA argued that extremely early departure times such as those proposed by Virgin and those offered by BMA on some of its shorter routes from Heathrow were tolerable for business passengers only where there was a real possibility of completing business and returning on the same day. This would clearly not be possible on a route the stage length of London/Moscow.

15. Unlike Virgin, BMA proposed to serve this route from the outset with an A321, which BMA believed to be the optimum choice of aircraft for a sector of this length. Indeed, Virgin's original plan appeared to be to use an A321 as soon as it became available, which would not be before the second year of operation. One advantage of BMA's product was the flexibility it was able to offer in terms of seat configuration. Its standard configuration on this route would be 74 business class seats and 105 economy class seats, a total of 179 seats. However, its ability to convert rows of economy class seats into business class configuration would enable it to accommodate up to 138 passengers in business class if necessary, while maintaining a minimum of 29 seats available in economy class. The quality of BMA's in-flight products had been repeatedly recognised by the travel and trade press and industry bodies, which had presented BMA with awards for all aspects of its service.

16. BMA had a proven track record and desire to provide effective competition using transparent and universally available published fares. However, under the present UK/Russia arrangements published tariffs were subject to the approval of both aeronautical authorities, and BMA would have little option therefore but to apply the IATA-agreed tariffs approved by the Russian authorities. In the absence of tariff liberalisation, BMA would aim to use its participation in IATA tariff co-ordination conferences to seek improvements for users in respect of published fares. It would at the same time compete

actively in the so-called “grey” market by offering widely discounted business and economy class fares. As soon as it is permitted, BMA would compete on published tariffs by introducing its standard tariffs structure.

17. BMA also raised a number of other factors which it felt should weigh in its favour in this case. These included the fact that it was the only airline in the world which offered a through ticketing facility on all its routes to London’s Paddington Station in conjunction with Heathrow Express. It also argued that Virgin’s proposal to use an A340 aircraft on this route would result in greater environmental detriment due to its higher fuel burn per passenger kilometre.

VIRGIN ATLANTIC AIRWAYS’ CASE

18. Virgin’s proposals to serve Moscow would, by offering passengers a real choice of schedule and product, maximise user choice and provide the most effective, differentiated competition against the existing incumbents on the route.

19. In the initial phase, while Virgin was able to operate only four services a week, it proposed to use an A340 aircraft. This would be configured with 40 seats in business class (with 55” seat pitch and 2 + 2 + 2 configuration), 28 seats in premium economy (38” seat pitch in 2 + 3 + 2 configuration) and 187 seats in economy class, a total of 255 seats. This was Virgin’s standard long haul product and as such its business class would be superior in comfort and service to any other business class offered or likely to be offered by any other airline on the route.

20. When it was possible to increase frequency to a daily service, it would probably switch to operating seven services a week with an A321 aircraft, unless the market had grown ahead of its forecasts, in which case the A340 might be maintained on the route. The A321 aircraft would be configured in two classes, with 48 seats in business class (with 36” seat pitch and 2 + 2 configuration) and 102 in economy class, a total of 150 seats. Virgin’s business class seat on its A321 would be to the same specification as on its A320 service to Athens and would be the biggest business class seat in Europe, wider and with greater seat pitch than in BMA’s current business class. In the case of both the A340 and A321, therefore, Virgin would be offering superior products compared to BMA, particularly in business class. It would also be widening consumer choice to a greater extent when its and BMA’s products respectively were compared with those offered by BA and Aeroflot.

21. In the current winter season, Virgin had obtained departure slots at Heathrow at 0640 on Wednesday and Friday and at 0730 on Saturday and Sunday. It would be scheduled to arrive in Moscow at 1330/1420, depart Moscow at 1500/1530 and arrive back at Heathrow at 1550/1620. Virgin’s aim was to move its departure slots from Heathrow towards 0800 over time, and indeed it had already been able to secure some improvements to its schedule for the summer 1999 season. It had secured departure slots at 0750 on three days of the week and at 0640 on Wednesdays only. While Virgin recognised that BMA’s proposed timings were better for those passengers who would want to make a connection at London, it believed that such passengers accounted only for a very small proportion of the market. It believed that for the vast bulk of the market, which did not make a connection at Heathrow, its preferred departure time of 0800 would be better than that proposed by BMA. It also believed that a further advantage in its proposal was that its departure and arrival times at Heathrow would benefit from being at

less congested times in Terminal Three than BMA's arrivals and departures in Terminal One.

22. Virgin submitted two sets of traffic forecasts. The first was based on its principal proposal to operate an A340 initially and to replace it with an A321 when it became possible to operate a daily service. On this basis, Virgin forecast that it would carry 50,671 passengers in the first full year of operation, at an average seat factor of 48%. In year two, when despite the higher frequency capacity would be only marginally higher due to the smaller aircraft, its traffic would grow to 59,732 passengers at a seat factor of 55%, and in year three to 65,856 at a seat factor of 60%. Virgin's second set of forecasts assumed that an A340 would be maintained on the route throughout the period. Due to the higher levels of capacity which would thus be provided in the second and third years, it believed that it would attract more traffic than under the original proposal. It forecast 73,158 passengers at a seat factor of 39% in the second year and 85,824 passengers at a seat factor of 46% in the third year.

23. Its financial results would depend upon the way in which aircraft ownership costs were allocated. For the first year, when an A340 would be used, Virgin submitted three sets of financial results. The first assumed that four-sevenths of the ownership costs of an entirely additional A340 were allocated to the route, and on this basis it would make a loss of £2.4m. The second assumed that the A340 was fully integrated with its other operations, so that it was used as part of a 10-aircraft programme. This is the way in which the Authority would normally expect such costs to be treated, and on this basis Virgin expected its first year loss to £775,000. The third projection was included for illustrative reasons, and assumed that there were no fixed aircraft costs incurred in connection with this operation, because the aircraft was available in any event. Under this assumption the route would return a profit of just under £2m. The financial results which Virgin submitted in respect of the second and third years were based on the assumption that the aircraft used were part of a fully integrated programme. On this basis, using an A321 for its daily services would result in a profit of £745,000 in year two, growing to £2.8m in year three. On the other hand, operating an A340 in those years was expected to result in a loss of £2.0m in year two and a profit of £880,000 in year three.

24. One of the advantages which Virgin's proposals therefore offered over BMA's was that it had the flexibility to respond to growth in the market. It also had a product which was good enough to enable it to withstand any competitive response on this route from BA. Indeed, Virgin submitted in evidence that BA had recently applied to the Moscow Airport authorities to operate a B777 on the Heathrow/Moscow route in place of its current B767. If BA were to upgrade its aircraft type on the route in this way, then it could be expected to be providing its long haul product instead of its short haul product. In such circumstances, Virgin's product would provide a competitive alternative, while BMA's would be significantly inferior in comparison.

25. Virgin also argued that its proposed operations would have no adverse impact on any other services because the slots it would use had originally been newly allocated to it. This was not the case for BMA, and so it was inevitable that BMA would have to move one or more of its existing services at Heathrow to accommodate its Moscow flights.

REPRESENTATION BY THE AIR TRANSPORT USERS COUNCIL

26. In seeking to arrive at a judgement as to where the consumer interest lay, the AUC considered separately the benefits accruing directly to travellers on the London/Moscow route and the wider benefits of enhanced competition between route networks. On the former, it regarded Virgin's proposal to offer better in-flight service, particularly in business class, as a real benefit to passengers. However, this was perhaps of less significance than on the long haul routes which formed most of Virgin's network. It regarded BMA's timings as far more convenient, not only enhancing benefits to point-to-point passengers but also, by providing connections to and from its domestic and European short haul routes, enabling BMA to compete for traffic which was currently being carried over other European hubs. The AUC also attached considerable importance to BMA's firm commitment to introduce lower fully flexible fares as soon as that became possible.

27. The AUC believed the question of which proposal would bring greatest benefits in terms of wider competition turned on whether London/Moscow was to be seen as part of the short/medium haul market or to be a long haul route. Its view was that Moscow fell more comfortably into the shorter haul market, and that it fitted into BMA's strategy of extending its European network eastward. It concluded that BMA's proposal would provide the greater direct benefit to travellers on the London/Moscow route and that it would also be likely to reinforce wider competition with the network of services offered by BA and its alliance partners.

ANALYSIS AND REASONS

Introduction

28. In this case the Authority has to decide whether BMA or Virgin should be the second British designated carrier on the London/Moscow route. It is clear that either BMA and Virgin could provide a viable service of a quality which would satisfactorily cater for the needs of users. That being so, the Authority regrets that the bilateral arrangements between the UK and Russia make it necessary to choose between them. In such a case it is likely that minor benefits and disbenefits will tip the balance one way or the other. In its previous decision the Authority attached weight to the fact that Virgin was more likely than BMA to be able to mount a daily service from the outset, but the Secretary of State's direction to rehear the case precludes it from attaching any weight to that particular benefit.

29. Somewhat different proposals and arguments were put forward at this hearing from those deployed at the earlier hearing. In particular, both parties have changed their plans as to the aircraft to be used on the route; Virgin has managed to improve its proposed timings to some extent, while BMA has somewhat developed and strengthened its industry structure argument.

30. Consistent with its duties under the Civil Aviation Act, the Authority's prime concern in licensing cases is to further the reasonable interests of users. It sees competition, both among British airlines and between British and foreign airlines, as the best available means of ensuring that users have the widest possible choice of products,

services and airports, that quality of service is maintained and that fares are set at reasonable levels in relation to cost. It believes that the interests of users are best met by the existence of a number of efficient and profitable British airlines strong enough to compete with each other and with foreign airlines, directly or indirectly, when the opportunity arises or can usefully be created. User benefits will exist only if the services are viable. Accordingly the Authority has considered the user benefits of the services proposed by BMA and Virgin under the following headings.

Viability

31. It was common ground at the hearing that either airline would be able to operate the London/Moscow route viably. Virgin argued that, in any event, viability should merely be a threshold. Provided that the Authority was content that neither party was putting forward proposals which were unsustainable, the question of viability should not be a relevant consideration. BMA argued however that while it was agreed that the route could be operated profitably with an A321 aircraft, the same did not go for the A340. It seemed to BMA that an A321 was the appropriate aircraft for this route, and that Virgin's proposal to operate the same aircraft itself from the second year onwards was an acknowledgement of that. The only reason that Virgin proposed to use an A340 in the first year was that it had spare A340 resource in its fleet. Virgin's first year loss figure was itself contained by what BMA regarded as an unrealistic passenger forecast, considerably higher than Virgin's first-year traffic forecast at the first hearing.

32. It seems clear to the Authority that both airlines would be capable of operating this route profitably. In particular it notes that by the third year of operation both airlines are forecasting broadly similar levels of profit, at least when comparing the two on the basis of an A321. Although Virgin forecasts incurring a larger loss than BMA in the first year, and to take longer to build the profitability of its service, the Authority has some sympathy with the view that in cases such as this viability should be regarded primarily as a threshold. The Authority believes it should consider whether particular proposals put forward by airlines are credible in a business sense. So long as it is satisfied on that count, and provided that market power is not being abused in any way, the fact that one airline is prepared to incur heavier losses in the start-up period of a new service because it is prepared to operate greater capacity does not seem to the Authority to be of itself particularly significant for the decision.

Capacity

33. BMA now proposes to use an A321 on the London/Moscow route. Virgin proposes to use an A340 in the first year, and to use an A321 thereafter unless, unexpectedly, demand built up sufficiently to justify the continued use of the A340. Thus Virgin would provide significantly greater capacity than BMA in the first year. If it then changed to an A321 Virgin's capacity would be smaller than that proposed by BMA because of the different configuration of the two airlines' A321s. In addition to having more seats, BMA's A321s can be used more flexibly than Virgin's because of the mechanism by which economy seats can be converted to business class and vice versa as necessary to meet demand.

34. In the event that Virgin maintained an A340 aircraft on the route, it would clearly maintain the substantial capacity advantage it proposes to offer in the first year. However, it seems to the Authority that while there must be a possibility that traffic growth will exceed current expectations, it would be wrong for the Authority to place weight on

such a possibility. BMA indicated in its evidence that in the event that BA upgraded its product on the London/Moscow route from its short haul to its long haul product, then it would compete and respond accordingly. If the market were to grow beyond expectations then it seems reasonable to assume that BMA, like Virgin, would wish to respond to that. For the purposes of this decision, therefore, the Authority will look primarily at the principal forecasts which were put to it.

35. While Virgin proposes to offer substantially greater capacity than BMA in the first year, the reverse is true, though to a slightly lesser extent, in the years thereafter. To the extent that users will benefit from greater capacity, therefore, it seems to the Authority that the two proposals offer, on balance, broadly neutral benefits when set against each other. Virgin offers a large one-off benefit in year one, whereas BMA offers slightly smaller but sustained benefits in years two and three.

36. It was clear that Virgin was proposing to use the A340 because it was available rather than because it was the most appropriate aircraft to be used on the route. There can be no guarantee that it will continue to be used and therefore we disregard any advantage the use of the A340 may give to Virgin in the long term. Indeed if Virgin were to downgrade to the A321 at the end of year one this might significantly damage passenger expectations built up by the A340 service.

Quality of service

37. BMA offers a good standard of service and has shown itself well able to compete in terms of service with BA on domestic and European services. However, it is not in dispute that the service on Virgin's A340 is superior to that of BMA, particularly in terms of legroom and in flight entertainment and, even on the A321, Virgin has the edge on BMA at least in terms of legroom for business class passengers. Moreover a number of Virgin's ground services for business class passengers are better than those of BMA and of its competitors on this route. This would enable Virgin to offer a distinctly different product from that offered by BA, thus widening user choice to a greater extent than BMA. However, additional legroom, in flight entertainment and pampering in the departure lounge, while welcome, are likely to be less important to the passenger on a medium haul service of three and a half hours or so than on a long haul service.

38. Virgin also argued that only it would be able to provide an effective competitive response should BA decide to upgrade its own services and offer its long haul product on the London/Moscow route. As referred to in paragraph 34 above, BMA submitted that in those circumstances it would compete and respond accordingly. It seems to the Authority that Virgin might well be the better placed of the two to respond in the very short term to any aggressive competitive response from BA. It has no reason to believe, however, that BMA would be unable to respond competitively to any such initiative by BA.

Fares

39. BMA's track record in introducing competitive fares speaks for itself but, while the present bilateral arrangements remain in force, there is little scope for competition in published fares, and such competition as there is will be in the "grey market". The Authority has little doubt that either BMA and Virgin, if designated, would participate in this market. The availability of "grey market" fares would depend on the available capacity and, as indicated in paragraph 33, Virgin would offer greater capacity in year one, but, depending on whether Virgin uses the A321, BMA might offer greater capacity

thereafter. In all the circumstances the Authority does not think that the issue of fares gives either party an advantage over the other.

Slots and Timings

40. Virgin has obtained departure slots at Heathrow at 0640 on Wednesdays and Fridays and at 0730 on Saturdays and Sundays. It aims to get slots as close as possible to 0800 when the opportunity arises. BMA intends to depart from Heathrow at 0900 on every Moscow service. Virgin said that since BMA had not obtained any new slots for the service, it could operate only at the expense of some other BMA service out of Heathrow. However the Authority has no reason to doubt that, given BMA's slot portfolio, it could accommodate the Moscow service with only minor adjustments to other services.

41. The Authority sees advantage in a departure time of 0900 rather than one of 0800 or earlier for point-to-point passengers who have any distance to travel to Heathrow, especially on a route where the passenger cannot hope to travel to his destination, complete his business and return home on the same day.

Connecting passengers

42. A significant feature of BMA's case was that its 0900 departure time would enable it to provide a service for connecting passengers from UK regions and from points outside the UK who at present use foreign airlines in order to travel to and from Moscow. While the London/Moscow route caters primarily for the point-to-point passenger, there are some passengers from the regions and elsewhere who would use a service by a British airline if connecting services were available, particularly if, as is the case with BMA, the transfer can be done without changing terminals at Heathrow. We are not convinced that the number of such passengers is as great as claimed by BMA. They do however exist and it is clear that not all of them will be catered for by BA's forthcoming Manchester/Moscow service. BMA will be better able to provide for them than Virgin because of the later departure time. Moreover BMA has the advantage over BA in that it would offer interlining in the same terminal at Heathrow and because of its earlier arrival back from Moscow.

Industry structure

43. BMA argued persuasively that the Moscow route would fit well into its current strategy of developing medium haul routes, particularly to Eastern Europe. Virgin's strategy is more opportunistic, seizing such opportunities as may arise. The Authority considers that the addition of the Moscow route would enhance, albeit to a small extent, the competitive strength of whichever of the parties is designated. BMA argued, and the Authority accepts, that it is BA's strongest competitor in the provision of European services at Heathrow. Accordingly it gives some weight to the argument that if BMA can develop a substantial network of Eastern Europe services this will increase its ability to compete with BA in that area to the long term benefit of the user of such services.

Conclusions

44. This has not been an easy case to decide and in many areas the two parties are evenly matched. The plus for Virgin is the standard of service it is able to provide, which has the effect of widening user choice. The most significant plus for BMA is the better timing of its proposed service, which is not only more convenient for the point-to-point passenger but will enable passengers from points outside London to connect with a British airline on journeys to and from Moscow. This may be a small category of demand but it is one which is not catered for at present.

45. The Authority does not think that on a route of this length the benefits of Virgin's service standards outweigh the various benefits flowing from BMA's better timings. On balance it finds that BMA's proposed service will further the interests of users more effectively than that of Virgin and accordingly it decides for BMA.

DECISION

46. The Authority withdraws its proposal to vary route licence number 1B/13 held by British Midland Airways Ltd.

47. In accordance with its proposal, the Authority hereby varies the route licence number 1B/35 held by Virgin Atlantic Airways Ltd by adding the following condition:

“Virgin Atlantic Airways shall not operate between London and Moscow if to do so would restrict or inhibit the ability of either British Airways or British Midland Airways to operate between London and Moscow.”

48. For the purposes of any appeal which may be made against this decision the 'decision date' (see Regulations 26(8)(a) and 27(4) of the Civil Aviation Authority Regulations 1991, as amended by the Licensing of Air Carriers Regulations 1992) is 21 December 1998.

G J Elsbury
For the Civil Aviation Authority
16 December 1998