

Preparing for a more competitive airports sector

Stakeholder working group – Eighth Meeting,

2pm to 5pm, CAA House, 12 November 2010

1. The CAA hosted a stakeholder working group meeting on 12 November 2010. At this meeting the CAA's CEO Andrew Haines and the Director of the Economic Regulation Group Dr Harry Bush were present to answer questions and discuss persistent issues raised by stakeholders in the course of the stakeholder engagement for this project.
2. The meeting was introduced by Chris Hemsley (CH), Director of Consumers and Markets, while Andrew Haines, CAA Chief Executive, chaired proceedings. A list of attendees is provided in Annex 1.
3. The following documents used in the meeting are available from the CAA website:
<http://www.caa.co.uk/default.aspx?catid=5&pagetype=90&pageid=586>):
 - a. CAA slides entitled "Guidelines for assessing competition in the airports market – Discussion with Andrew Haines and Harry Bush"; and
 - b. Ryanair slide entitled "Two-sided markets – characteristics and implications for airports' competition assessment" (not presented).
4. The discussion of the issues by stakeholders in the course of the stakeholder engagement process was introduced through presentation slides. The main points of discussion and issues raised by the stakeholders, covering both process and substance, are documented below. Due to time constraints the second half of the agenda set out in the CAA's slides could not be covered.
5. CH welcomed stakeholders and introduced Andrew Haines (AH) and Harry Bush (HB). He stated that only issues raised in relation to the Competition Guidelines project would be discussed but this was not the last opportunity for stakeholders to put forward views. AH added that an objective of this meeting was to emphasise the CAA's aim of meaningful

consultation and transparency and to take on board stakeholder views in the course of inferring evidence and making decisions.

Comments relating to the CAA's process

6. Some stakeholders stated, as they had in a July 2010 letter, that there was initial unease that the CAA might have pre-judged the outcome of this project. They added that the CAA's openness was appreciated but that there still remained some concerns over transparency, citing examples such as the work that the CAA commissioned from consultants. Asked whether any different course of action by the CAA would have likely resulted in a different outcome, some stakeholders replied that it might not have but that there has been a resulting delay in the project. Other stakeholders argued that they did not know whether the outcome would have differed because the project had not yet reached its end. A further point was made that the Competition Guidelines project relied a lot on theory and used little or no evidence. For example, it was argued that the CAA had asserted the existence of scarcity rents yet supplied no supporting evidence. HB replied that the guidelines were intended to outline how to undertake a competition assessment while empirical data would be important during analysis of specific cases.

7. It was suggested that, while the Issues document was generally welcome, the CAA could have provided more hypothetical examples for the different parts of a competition assessment to increase transparency. Further, there could be uncertainty for stakeholders if the weighting given to particular evidence was not clear. Particular airports also had specific attributes that should be accounted for during the assessment. CH replied that it might be difficult to add value as an example would have to be notional and not closely resemble any particular airport. Whereas, any actual assessment would need to reflect the particularities of the airports in question. He added that the working papers due to be published should provide additional information on the methods that could be used in a competition assessment.

Comments relating to multi-sided markets

8. The Ryanair slides were circulated but were not presented due to the absence, through illness, of the Ryanair representative. CH outlined the CAA view on two-sided markets, which can be found in the Issues document.
9. It was argued that there were two principal questions to be answered in determining the impact of the multi-sidedness of the airport market in a competition assessment. First, it should be determined whether an airport could be characterised as a platform. Second, if this were the case, the importance of the constraints imposed by the different demand groups would have to be established. Further, the attributes of an airport and its pricing may not be the only criteria for its users in selecting it.
10. Some stakeholders provided examples of multi-sided markets in practice. These included newspapers/magazines, credit cards and mobile phone networks.
11. CH outlined the general approach that could be taken in a competition assessment treating an airport as a multi-sided market. Since the abuse of market power could occur on any side of the market, all direct and indirect effects would be considered. In particular, the chain of indirect events, for example effects on passengers from airline switching, would be followed to calculate its empirical impact. Each side of the market might need to be analysed individually but the overall judgement would be reached after taking into account all sides of the market and the linkages between them. It was noted that some of the indirect effects might happen over the medium/longer-term. AH summarised that the potential impact of a 'two-sided' approach would be investigated using empirics on a case-by-case basis.

Comments relating to scarcity

12. CH outlined the CAA view on scarcity, which can be found in the Issues document. Importantly, scarcity could be a feature of a well-functioning market and could arise from different sources.

13. Stakeholders raised the issue that certain types of scarcity may be classified differently at different points in time. For example, the introduction of government restrictions on capacity expansion could lead to transitory scarcity becoming underlying scarcity. HB replied that the important issue was whether the airport was purposely restricting output, as this artificial scarcity could constitute an abuse. Further, not every type of scarcity would give the airport the opportunity to exert its market power. Stakeholders added that some effects of capacity scarcity could be offset in some cases by airline responses, such as employing larger aircraft.
14. A stakeholder pointed out that underlying and/or transitory scarcity could act as a barrier to entry in other markets without creating a competition problem. For example, in mobile telephony, there was spectrum scarcity but there was still competition between network operators using the scarce spectrum resource.
15. CH summarised that there was not an automatic jump from finding scarcity in a market to considering an airport to hold substantial market power. The causes of the substantial market power would be investigated by looking at passengers', airlines' and other users' substitution possibilities.

Comments relating to the competitive price level

16. CH outlined the CAA view on the competitive price level, which can be found in the Issues document. Rather than using historical costs, there might be a need to use replacement costs for a more forward-looking approach. The weight placed on the results of any analysis of the competitive price level would vary. For example, were there clear and reliable evidence of a large divergence between the prevailing and competitive price level, then this would be relevant for the competition assessment. By contrast, if there were no clear evidence about the relationship between the competitive price level and the prevailing price level, then it would not be necessary to attach much weight to any measured divergence.

17. Stakeholders generally voiced concerns about the difficulty of estimating the competitive price level in the airport market. They added that only the efficient cost level should be considered to calculate the competitive price level. Some stakeholders argued that for the purpose of market investigations, the efficient cost level should be the full economic cost including opportunity cost.
18. It was also suggested that although benchmarking airports would be difficult due to heterogeneity between airports in terms of scale and operation, benchmarking could perhaps be performed for certain aspects or particular costs of an airport such as individual elements of operating expenditure.

Comments relating to airline buyer power

19. There was some discussion concerning the degree of buyer power held by airlines. Although airlines could exert buyer power by switching part, or all, of their operations, the ability to do so would depend on opportunity cost and switching costs facing each individual airline. CH summarised that airline, and passenger, buyer power would be part of the evidence that would be considered in a competition assessment. Stakeholders accepted that this was a reasonable approach. Airlines had previously been concerned that the Issues document had assumed that airlines had significant buyer power in all circumstances.

New Legislation

20. A question was asked regarding the effect that the development of the new bill would have on these projects going forward. CH replied that the Bill was not the only reason that the Competition Guidelines were being produced. For example, this project also could inform the designation and de-designation decisions, the way the CAA regulated designated airports and Section 41 (of the Airports Act 1986).
21. AH went on to state that the CAA had not reached a view as to the timing of the Q6 price control reviews but that the situation would become clearer in the next four to five weeks, depending on the emerging timetable of the new bill. HB added that if the bill did not get a slot in the

current parliamentary session, then this could raise an issue as to whether the Airports Act or the new Bill would be used as the framework for the next quinquennium. Additionally, the constructive engagement process would proceed regardless of a change in legislation and initial work on Q6 had already begun.

22. As a way forward, stakeholders were asked to submit comments regarding the content of the Competition Guidelines by the end of November. A deadline of the 4th January 2011 was given to stakeholders for feedback on the working papers. The working paper on empirical methods relating to geographic market definition was due for publication on the 15th November, and the second working paper was due to follow soon after that. Dates for further Stakeholder Working Groups for January and February 2011 were to be confirmed.

Annex 1 – List of attendees

Alexander Dünki	(CAA)
Andrew Haines	(CAA)
Barry Humphreys	(BATA)
Chris Hemsley	(CAA)
Colin Garland	(Gatwick Airport)
Chris Gadsden	(easyJet)
Georgina Kwaszenko	(Virgin)
Gerry O'Connell	(IATA)
Harry Bush	(CAA)
Isabell Kohten	(CAA)
Isobel Knox	(BA)
Jim Hunter	(AOC LHR)
Jonathan Sandbach	(BAA)
Kyran Hanks	(Gatwick Airport)
Laurie O'Toole	(IATA)
Louise Congdon	(York Aviation working for Ryanair and SACC)
Melanie Everitt	(BAA)
Rebecca Stäheli	(CAA)
Richard Senior	(Bmi)
Robert Siddall	(AOA)