

# CAA Stansted Market Power Assessment – Response from Gatwick Airport

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## Introduction

The CAA published for consultation on 31 January 2013 its 'minded to' position on its market power determination for Stansted Airport. Gatwick welcomes the opportunity to submit its response to this consultation to the CAA. Gatwick is in a very different position to Stansted; it will offer significant commitments to airlines in the event it is not licensed, and has demonstrably embraced the ability to compete with both Heathrow and Stansted, and other airports.

There have been important developments since the publication of the CAA's assessment. The acquisition of Stansted has taken place and, as Gatwick expected, the new owners have signified their intention to compete. The CAA will be able to verify the new owners' public statements against their discussions with the Competition Commission and the strategic plan the Commission will have requested. This has an important bearing for the CAA's market power analysis of both Stansted and Gatwick. The behaviour of Stansted under BAA's ownership sheds little or no light on its competitive significance in the future.

There are, however, a number of issues raised by the CAA's analysis of Stansted's market power that may have parallels with Gatwick. We are extremely concerned that if the CAA repeats these approaches in its analysis of Gatwick's market power and fails to take account of Gatwick's different position, it will risk reaching erroneous conclusions.

Below we set out our response on the CAA's analysis of Tests A, B and C of the market power test at Stansted. Note, this response does not take into account the CAA's recently published summary of its market power assessment at Gatwick Airport.

## Test A – whether Stansted has, or is likely to acquire, substantial market power in a market, either alone or taken with such other persons as the CAA considers appropriate

As the CAA is aware, Gatwick has made a number of substantive submissions on the issue of whether Gatwick has, or is likely to acquire, substantial market power (SMP). From those submissions it will be clear that our view is that Gatwick does not have SMP and as such should not be issued with a licence under the Civil Aviation Act 2012. In this response we do not revisit the content of those submissions. Here we limit our response to key areas of concern to Gatwick arising from the CAA's Stansted analysis. In particular, we highlight areas where we consider that

# YOUR LONDON AIRPORT

## *Gatwick*

the CAA is being inconsistent with its own and others' precedents (without it justifying these departures), where it has made errors in its analysis and where it fails to make balanced assessments of factual evidence and others' views.

### Overview of Gatwick's response

Below we set out the issues that we consider are particularly important in leading the CAA to conclude erroneously that Stansted has SMP.

- **The relevant market covers low cost carriers (LCCs) and charter airlines at Stansted, Luton, Southend and possibly Gatwick** – However, this conclusion on market definition fails to take into account the reality of competition from, and route overlaps with, what the CAA is characterising as Full Service Carriers (FSCs), and which it concludes are in a separate economic market;
- **Little evidence has come to light of actual switching of established airline capacity from London airports to Europe** – However, this fails to recognise what happened when Ryanair reduced capacity at Gatwick equivalent to about 1 million passengers over the last couple of years, and what will happen this summer when Ryanair makes an even larger reduction than that at Stansted. The CAA should conduct more comprehensive analysis in this area;
- **Stansted has a high market share** – However, this conclusion is reached on the basis of an incorrectly defined market scope;
- **Stansted is pricing above the competitive level** – However, this is based on a benchmarking exercise with obvious limitations and uncertainties (on which we have responded separately), and whose terms of reference were never intended to assess the competitive price level;
- **The most likely source of market power possessed by Stansted is the inherent attractiveness of the London market and its strategic importance to airlines, combined with capacity constraints in the London system, which limit the number and size of available alternatives** – The implication of this is that the airlines cannot reduce their capacity serving London and have no other options as to where they use their capacity. However, this is clearly not the case for the larger LCC's and charter carriers who have many options as to where they deploy their fleets and for whom London capacity is by no means immutable, as the Ryanair examples mentioned above demonstrate clearly. (Moreover, the inherent attractiveness of the London system should figure in any assessment of the competitive price level, so that it reflects the full economic value of the service).

### Lack of consistency

The CAA's analysis of Stansted's market power is inconsistent with a number of previous documents and analysis, and in most cases without any adequate explanation of why a divergent approach is now required. A key area of inconsistency is with the Competition Commission's (CC) analysis of the airport market in the South East of England, including its final report<sup>1</sup>, its report on material changes in circumstances<sup>2</sup>, the evidence that it presented to the Competition Appeal

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<sup>1</sup> *BAA airports market investigation: a report on the supply of airport services by BAA in the UK*, CC, March 2009

<sup>2</sup> *BAA market investigation: consideration of possible material changes in circumstances*, CC, July 2011

# YOUR LONDON AIRPORT

## *Gatwick*

Tribunal (CAT)<sup>3</sup> and the reasoning of the CAT in its dismissing of BAA's appeal and its upholding of the CC's decision<sup>4</sup>.

Gatwick believes it is crucial, as a matter of coherent regulatory policy, that any decision on regulation of Stansted and Gatwick is consistent with the CC's analysis (in the absence of a material change of circumstances) as that analysis led to the most intrusive remedy available, namely the break-up of BAA. It would not be consistent for the CC to require the break-up on the grounds that Heathrow, Gatwick and Stansted could compete with one another and for the CAA to regulate on the basis that they did not, or did so only to a limited extent.

Other areas of inconsistency include inconsistency with:

- Its own competition guidelines<sup>5</sup>;
- Its own previous analysis of Stansted's market power, presented in its Initial Views consultation<sup>6</sup>;
- Its own previous analysis of Stansted's market power, presented in its Stansted de-designation advice<sup>7</sup>;
- Its own previous analysis in the context of its evidence to the Competition Commission's (CC) airports market investigation<sup>8</sup>;
- Its own ad hoc studies e.g. on low cost airlines<sup>9</sup>;
- Its own reasoning in its decision on the allocation of capacity on the London to Moscow route<sup>10</sup>;
- Its own reasoning in its decision on its section 41 investigation of the structure of Gatwick's charges<sup>11</sup>;
- The Department for Transport's (DfT) decision on Stansted de-designation<sup>12</sup>; and
- The European Commission's analysis of airline merger decisions involving airlines operating in airports in the South East airport's market<sup>13</sup>.

While it is acknowledged that policy and thinking on regulation can and should evolve over time, it should do so on a principled and evolutionary basis. These departures lack such a basis and have

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<sup>3</sup> For example see Transcripts of Hearing.

<sup>4</sup> *BAA limited vs Competition Commission vs Ryanair Limited: Judgment*, CAT, February 2012

<sup>5</sup> *Guidance on the assessment of airport market power*, CAA, April 2011

<sup>6</sup> *Stansted – market power assessment: the CAA's initial views*, CAA, February 2012

<sup>7</sup> *De-designation of Manchester and Stansted airports for price control regulation: The CAA's advice to the secretary of State*, CAA, July 2007

<sup>8</sup> For example, *The Competition Commission's market investigation of BAA Ltd: The Civil Aviation Authority's response to the provision findings and remedies notification*, CAA, September 2008

<sup>9</sup> *No frills carriers: revolution or evolution, a study by the Civil Aviation Authority*, CAA, CAP 770

<sup>10</sup> *Decision of scarce capacity allocation certificates SCAC1/12*, CAA, October 2012

<sup>11</sup> *Investigation under Section 41 of the Airports Act 1986 of the structure of airport charges levied by Gatwick Airport Limited*, CAA decision, CAA January 2013

<sup>12</sup> *Decision on the regulatory status of Stansted airport*, DfT, 2008

<sup>13</sup> For example *COMP/M.4439 – Ryanair / Aer Lingus* European Commission, June 2007, also *COMP/M.6663 – Ryanair / Aer Lingus III*, European Commission, February 2013

not been accompanied by the presentation of compelling evidence that supports a different approach being taken and different conclusions being reached.

#### Selective use of evidence

The CAA, in its analysis of Stansted's market power, is selective in its use of available evidence and prior analysis of other competent authorities, using such evidence and referring to it when it supports its current argumentation and conclusions. In our view the CAA should take a more balanced view of the evidence as a whole.

#### Inappropriate analytical framework

The CAA begins its analysis of constraints at Stansted at the airport-to-airline level. The CAA then goes on to consider constraints at Stansted from the airline-to-passenger level. However, this is an unconventional approach, at variation with its own and others' previous approaches, for assessing competition in markets with a derived demand. This leads the CAA to defining incorrectly the scope of the relevant economic market. It is only after the CAA has considered the nature and extent of constraints at the airline-to-passenger level that it should consider any additional constraints at the airport-to-airline level.

If the CAA were to start its analysis at the airline-to-passenger level it would become clear that passengers have significant choice between the different airports in the South East of England, as clearly shown by the route overlaps in Table 5.3 of the CAA's "minded to" paper. This, together with other data and analysis, should lead to the incontrovertible conclusion that the geographic scope of the relevant economic market is at least the South East of England and would include Heathrow, Gatwick, Stansted, Luton, London City and Southend airports. The other data and analysis that supports this conclusion includes:

- The CAA's passenger survey analysis;
- The CC's airports exposure analysis from its airports market investigation;
- The clear implication of the CAT's decision on the BAA appeal that Stansted and Heathrow are in the same relevant economic market; and
- The European Commission's rebuttal of Ryanair's arguments that the London airports are in separate economic markets.

An example of the problems caused by the CAA's proposed analytical framework is its analysis of the product market definition in the Stansted consultation. This leads to the CAA seeking to identify whether there are separate product markets for, amongst others, long haul versus short haul passenger airlines, and based versus inbound operations. The CAA begins its analysis without any consideration of the constraints at the airline-to-passenger level.

The CAA does analyse passenger switching, but it does not apply this to market definition, as it has traditionally done (including in its February 2012 initial views analysis). Rather the CAA deploys this material in its assessment of market power. The CAA's analysis demonstrates that there is a substantial proportion of passengers for whom Stansted is not their first choice airport and, indeed, for whom Heathrow and Gatwick are preferred ahead of Stansted, or as a second preference. When this is combined with other CAA evidence that demonstrates that Stansted passengers have used both Heathrow and/or Gatwick in the recent past, together with the CC's

“exposure analysis” from its market investigation which demonstrated that Gatwick is Stansted’s closest substitute and Heathrow is Stansted’s second closest substitute, these all support a definition of a broader, rather than a narrower, geographic market.

#### Lack of clarity on market boundaries

It is notable that the CAA does not define what it means by short haul, where the market boundary lies, or what the boundary will be going forward. However, from the CAA’s reasoning it is clear that it assumes that short haul is synonymous with LCCs and charter carriers as these make up the vast majority of traffic at Stansted. However, there is no analysis by the CAA of the extent to which passengers view LCCs and FSCs as being substitutable, or the extent to which the distinctions between the business models have been eroded and could be expected to disappear over time as a result of product innovation (such as easyJet’s introduction of assigned seating and BA’s introduction of discounts for passengers who do not check in baggage).

The CAA, in its provisional analysis of the airline market, has not taken account of certain matters. In particular, the CAA appears to misunderstand the differences between short haul FSCs and LCCs. For example, short haul services offered by FSCs do not only act as feeder traffic for their long haul FSC services. Indeed, the majority of short haul FSC traffic is point to point traffic, not feeder traffic, and as such provides a direct substitute for point to point passengers using LCCs<sup>14</sup>.

#### Lack of consideration of the cumulative impacts of constraints

A competition analysis should seek to assess the cumulative impact of constraints on a firm on the market. However, the CAA’s analysis of Stansted’s market power does not do this. Instead, the CAA discusses each source of potential constraint in isolation and concludes that each constraint in isolation is not sufficient to constrain Stansted’s behaviour.

#### Undue weight to the views and historic behaviours of airlines

The CAA’s analysis is notable for the greater weight that it places on the views and behaviours of airlines, in contrast to those of airports. In a number of cases, the CAA appears to accept airlines’ views with minimal investigation or challenge. Moreover, the CAA has changed its view of airline evidence on a number of occasions. Some examples of these issues include:

- **Removal of discounts at Stansted** - The CAA has in the past been sceptical of the relevance of airlines’ changes in behaviour subsequent to Stansted ceasing its discounts in 2007. Previously, the CAA has interpreted this along the lines of a market-growing discount coming to an end after its purpose had been served (as evidenced by the significant traffic growth experienced when the discounts were in place) and the price reverting closer to the competitive price level. The CAA is now interpreting this as evidence that airlines have switched in response to an increase in price but to such an extent that they could not shift any more capacity out of Stansted as it is central to airlines’ ability to serve the strategically important London market. The latter point is clearly undermined by Ryanair’s recent announcement that it intends to reduce its planned flights from Stansted by 9%, from 12.5 million passengers to 11.4 million passengers, for the year beginning April 2013 in response to the 6% increase in

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<sup>14</sup> *No frills carriers: revolution or evolution, a study by the Civil Aviation Authority, CAA, CAP 770*

airport charges<sup>15</sup>. There is no explanation of why the CAA has changed its view of its interpretation of this data or what evidence supports this view.

- **Prior easyJet analysis** - The CAA revisits data and analysis submitted previously by easyJet in 2007 for the Stansted de-designation review and in 2011 for the current market analysis. The CAA now appears to place substantially more weight on data which it previously treated sceptically as being limited and airline specific.
- **Airport views on passenger substitutability** - The CAA summarises airports' views on passenger substitutability, which all state consistently that travel time and the associated population is a key metric on which airports consider that they compete and on which they market themselves to airlines. However, this is done in a selective manner and little weight is given to them in the conclusions reached.
- **Airline switching** - The CAA discusses airline switching, including Air Asia X and airberlin to Gatwick from Stansted, which has formed part of our evidence that Gatwick does not have SMP. However, the CAA concludes, given the relatively (in its view) low level of switching observed and the lack of price motivation for the switching that has taken place, that the switching does not provide sufficiently strong evidence to support the inclusion of Gatwick in the same market as Stansted. In reaching this conclusion the CAA has made no allowance for the distorting impacts of economic regulation and of Stansted being in joint ownership with Heathrow until very recently.

#### Analysis of market power is conducted without the CAA concluding on the definition of the relevant market

The CAA defines two separate passenger markets: one for LCC and charter airlines and one for full service long haul carriers and their associated feeder traffic, the latter including Heathrow and Gatwick.

In relation to the first market we note that the CAA has not concluded firmly on the scope of the market as it possibly includes Gatwick (as well as Stansted, Luton and Southend). This is clearly problematic to the extent that the inclusion or exclusion of an airport affects the conclusion of the assessment of market power.

For the second market, the CAA does not conduct an assessment of market power, only stating that Stansted does not currently compete successfully in this market. We would have expected some analysis of evidence to support this conclusion, including an assessment of the prospects of an independent Stansted now free to compete in this market as the new owners have recently made clear.

#### Competitive price level

The CAA considers that its additional analysis, including the price benchmarking by LeighFisher, suggests that Stansted is pricing above the competitive level. In addition, the CAA considers that the evidence suggests that, if economic regulation is completely removed from Stansted, it could seek to increase prices further above the competitive level.

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<sup>15</sup> Ryanair press release <http://www.ryanair.com/en/news/ferrovial-baa-hikes-stansted-fees-by-6-percent-from-april-2013-in-a-parting-gift-to-manchester-airport-group-and-a-parting-slap-to-stansted-s-airlines-and-passengers>

From the analysis presented by the CAA, we are not clear how the CAA can substantiate this conclusion. We have previously submitted separate responses on the LeighFisher benchmarking analysis and Europe Economics analysis of forward looking costs. In our responses we set out our considerable reservations on the approaches used, and on the way in which the CAA seeks to use that analysis. In particular, the LeighFisher analysis is not a sound basis from which to estimate the competitive price level. We are also concerned that the CAA uses the analysis to develop a point estimate of the competitive price level. A more appropriate approach would be for the CAA to develop estimates of the range of prices that would be expected in a competitive market and then cross-check Stansted's prices to assess whether they are consistent with that range.

#### Application of Test A at Gatwick

As we have set out above, a number of areas of the CAA's analysis of Stansted's market power cause Gatwick concern. In particular, we are concerned that if the CAA does not correct for these in its consideration of Gatwick's market power it will reach an erroneous conclusion on the question of whether Gatwick has or can be expected to acquire SMP. We encourage the CAA to revise the approach to its analysis to address the concerns set out above.

## Test B – that competition law does not provide sufficient protection against the risk that Stansted may engage in conduct that amounts to an abuse of that SMP

#### Application of Test B at Gatwick

Before setting out our comments on the CAA's consideration of Test B, we would emphasise that Gatwick is in a wholly different position from Stansted because of the extent to which we have proposed, refined and detailed our airline commitments. We have made a number of previous submissions to the CAA explaining that we consider Test B is not passed at Gatwick. This view is further bolstered by our Commitments offer.

We are concerned with how the CAA appears to be interpreting the requirements of Test B. In particular, it appears as though, in the way that the CAA has formulated its assessment, that Test B will in all likelihood be passed whenever an airport is found to have SMP. We do not consider that this could have been the intention of the legislation, or of the will of Parliament, as such a formulation negates the need for a Test B. Therefore, the hurdle required to demonstrate that Test B is passed must be higher than that proposed by the CAA.

We also note that the CAA's current conclusion on Test B is different to that in its 2007 advice to the Secretary of State on the de-designation of Manchester and Stansted airports<sup>16</sup>.

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<sup>16</sup> We recognise that this advice was provided under a different regulatory framework than which the CAA is currently assessing airports' market power, but the question was very similar.

### Scope of the concept of abuse of market power

The CAA states that “the concept of the abuse of market power would therefore seem in principle to have a potentially wider scope than abuse defined under 18(2) of the CA98”<sup>17</sup>. We are aware of no valid grounds for such a conclusion.

### How the CAA will assess Test B

The CAA sets out the question it considers that it should seek to answer in applying Test B. This is:

*“Whether applying the legal tests required by competition law to the situations that might arise based on our assessment of market power in a given case, will ensure that the identified risk to the interest of users of airport operational services is addressed in a timely and comprehensive manner”*<sup>18</sup>

We are concerned that the CAA has misdirected itself in failing to concentrate on the interests of passengers and cargo shippers. Test B should focus on whether any risk of abuse would translate to harm to passengers and/or cargo shippers. This is narrower than that set out in the CAA’s formulation of the question above, which refers to “the interests of users of airport operational services”, which we read to include, additionally and erroneously, the interests of airlines. While such a distinction may not be important in some circumstances, it may be important in others.

### The aims of ex ante regulation versus the aims of ex post regulation

The CAA includes in its consideration of Test B, a discussion of the differences between ex ante and ex post regulation. In doing so, the CAA repeats some text from Ofcom, the communications regulator, which has explained its approach when deciding between ex post and ex ante regulation when regulating communications markets. Ofcom explains that regulation can be designed in a way to actively reduce market power and promote effective competition over the period in which the regulation is in place.

*“Ex-post competition law is [. . .] unlikely within itself to bring about effective competition, as it prohibits the abuse of dominance rather than the holding of a dominant position. In contrast, ex-ante regulation is normally needed to promote actively the development of competition. Ex-ante regulation attempts to reduce the level of market power in a market, thereby encouraging effective competition to become established”*

We are concerned that the CAA has not understood the context of this quote, characterising it as Ofcom using ex ante regulation to curtail the risks of abusive behaviour before the behaviour emerges, whereas what it is referring to is the fact that Ofcom designs its ex ante regulation in a way to encourage effective competition. The approach referred to in the quote is not about curtailing the risks of abuse before the behaviour emerges.

### The application of competition law to airports – exclusionary behaviour

We welcome the CAA’s assessment of the potential to use general competition law to address exclusionary behaviour at airports. In particular, we welcome the recognition of the low likelihood

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<sup>17</sup> Paragraph 8.7.

<sup>18</sup> Paragraph 8.18.



of there being incentives on an airport to participate in exclusionary conduct and the recognition that, where this may occur, competition law is likely to be an effective response. As acknowledged by the CAA, this has been demonstrated by the successful use of the Competition Act 1998 to address anti-competitive exclusionary behaviour by Heathrow Airport in terms of access to its forecourt<sup>19</sup>. Moreover, we would also highlight the recent successful use by the CAA of section 41 of the Airports Act 1986, which is in many respects very similar to general competition law, to assess separate complaints of discriminatory behaviour against Heathrow and Gatwick airports.

### The application of competition law to airports – exploitative behaviour

The CAA sets out a number of reasons why it is concerned about relying on competition law to address exploitative behaviour by an airport operator, such as excessive pricing. These include difficulties around estimating the total economic value of the product being offered, the difficulty in distinguishing between high prices as market signals and high prices which may be excessive and the reluctance by competition authorities to prescribe clear upper limits on market prices. The CAA also highlights what it refers to as “difficulties” associated with the tests that are derived from the United Brands ruling.

We are concerned that the CAA is taking an unduly negative view of the ability of competition law to address excessive pricing, particularly in view of more recent case law. Each of the issues identified by the CAA is in fact a reason why the CAA should be very cautious about deploying ex ante regulation in a market such as the South East airports market, where true competition is beginning to be a reality and where ex ante regulation has the very real ability to constrain the further development of competition in the future. Indeed, in such circumstances there is a strong argument that relying on ex post competition law would be much preferable to address any abuse that materialises, as such an approach would allow the market dynamics to affect outcomes, rather than over-intrusive regulatory interventions.

### Government intervention

We are concerned by the way that the CAA has interpreted government policy on airport capacity in the South East of England, and how it has linked this with its consideration of Test B at Stansted. There are a number of issues in this section which we find particularly troubling:

- **Government policy has changed since 2010** – There is no recognition by the CAA that policy has changed since the government ruled out, in 2010, any new runways in the South East.
- **The change in government policy in 2010 did not change the competitive benefits from separate ownership absent new runway capacity** – The CAA refers to the CC’s material change in circumstances decision in which the CC continued to require BAA to sell Stansted. The CAA quotes the report, which states “*government policy is also likely to delay the competitive benefits to be expected from a new runway...*” However, the CAA makes no reference to the fact that the CC’s view, confirmed by the CAT, was that the decision would not impact on the substantial benefits from competition that would arise from separate ownership absent the provision of new runway capacity.
- **Normal price signals will still emerge, absent new runway capacity** – The CAA argues that the absence of new runway capacity will “*interfere with the normal price signals expected within*

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<sup>19</sup> *Purple parking versus Heathrow Airport Limited EWHC 987, 2011*

*a competitive market*” and that “*in an unregulated market at an airport facing these constraints it would be expected that prices rise at these airports to better match demand with available supply*”. The implication is that these are inconsistent. However, they are wholly consistent and would be exactly what would be expected in a competitive market.

- **Competing airports have substantial incentives to increase capacity** – the CAA states that “*when restraints are lifted, absent regulation, an airport operator with substantial market power would face limited incentives to provide additional capacity as this would erode the rents available*”. This is directly contrary to the findings of the CC in the airports market investigation which found that separate ownership would create competition between the airports to provide additional capacity. An airport would have a substantial incentive to be first to market with new capacity, because if a competitor airport were to provide capacity, this would depress prices across the whole market, but the airport not providing the additional capacity would not benefit from any increase in volume, so its total revenues would decrease. The impact of this dynamic can be observed today, with the “race for runways” currently under way.

#### Government policy on regulators’ use of competition law

As the CAA will be aware, the government is currently looking at ways in which it can encourage and incentivise sectoral regulators to make more use of their competition law powers. The government is concerned that regulators rely too much on their sector specific powers in preference to general competition law.

The CAA’s thoughts on Test B appear to be going in the opposite direction.

## Test C – for users of air transport services, the benefits of regulating Stansted by means of a licence are likely to outweigh the adverse effects

#### Application of Test C at Gatwick

As mentioned above, Gatwick is in a very different position from Stansted. The combination of our Contracts and Commitments, the Airport Charges Regulations, the Ground Handling Directive and general competition law, together provide sufficient protection to the interests of end users. Moreover, the transition to commercial agreements outside of a licence-based regulatory regime will promote competition between airports which will allow greater ability for the airport and airlines to work together, innovate and better serve the needs, desires and interests of passengers.

#### Impact of licence regulation – excessive prices

We are concerned that the CAA underestimates the constraining effect of competition law on a firm’s pricing practices. In particular, we do not understand why the CAA considers that if an airport is pricing within the constraints of a price control, but at a level that would be excessive under competition law, that this makes it more difficult for a competition authority to make a case against excessive prices.

The CAA goes on to state:

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## *Gatwick*

*“If the price cap is set too low, then this could affect the prices of the airport’s competitors, reducing their operators’ incentive to invest or ability to make adequate returns. This may affect the development of the market over time, potentially to the detriment of consumers. It may also adversely affect airline locational decisions.”*

This statement demonstrates the possibility that the CAA, by setting price caps, is determining the market outcomes in the provision of airport services in the South East. Thus, the CAA should be very cautious about setting price caps at all three of the currently regulated airports.

The CAA seeks to explain why its view with regard to Test C has changed between its previous assessment of the costs and benefits of regulation of Stansted in its 2007 de-designation advice and its current assessment. In doing so the CAA lists a number of factors that have changed. However, the CAA fails to acknowledge the single most important development since 2007, namely the step change increase in competition from the break-up of BAA, or the substantial increase in spare capacity in the South East now, as compared to 2007.

### Impact of licence regulation – inefficiency

The manner in which the CAA presents its discussion of inefficiency is that there is an underlying expectation that the regulated airport should always be the most efficient in its benchmark group for each of the benchmarked activities. This is an extreme position and omits any recognition that even the most efficient firm in a sector will have scope to increase its efficiency against its peers in some areas of its operation. The CAA also omits any consideration of what would be a reasonable benchmark against which to measure an airport’s efficiency.

### Impact of licence regulation – investment incentives

We are concerned by the manner in which the CAA considers how regulation can be used to correct for the deficiencies and distortions to investment incentives created by the current regulatory framework, as identified by Stansted. Rather than assessing whether removing regulation would address concerns about distorted incentives, the CAA concludes that it can increase the regulatory oversight at Stansted to correct for the deficiencies created by the current regulatory approach.

This “perfected regulation” philosophy appears to be strongly at odds with how regulators have usually approached markets with regulation that have experienced an increase in competition.

### Indirect costs of licence regulation

The CAA acknowledges that, in addition to direct costs, the main costs of regulation are likely to be indirect. However, while the CAA lists some examples of what these indirect costs are likely to include, no attempt is made to estimate the magnitude of these costs. The CAA justifies this on the basis that the indirect costs are “difficult to quantify”, but we would encourage the CAA to carry out a full analysis of what we believe are very substantial indirect costs of regulation.