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Sent via email: [alina.jardinegoad@caa.co.uk](mailto:alina.jardinegoad@caa.co.uk)

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Dear Alina,

**VIRGIN ATLANTIC'S RESPONSE ON THE PUBLICATION OF THE CIVIL AVIATION AUTHORITY'S INITIAL VIEWS ON MARKET POWER AT HEATHROW, GATWICK AND STANSTED**

Virgin Atlantic appreciates the opportunity to provide comments on the Civil Aviation Authority's (CAA's) initial views on market power at Heathrow, Gatwick and Stansted. We welcome the open and consultative approach that has been adopted by the CAA with this assessment given the impact the outcome will have on our commercial interests at both Heathrow and Gatwick airport.

**Virgin Atlantic's Overall View**

During the preliminary assessment period Virgin Atlantic has contributed to the CAA's process through engaging with and submitting formal evidence to the authority. Over this time we have continued to strongly argue that both Heathrow and Gatwick airport hold significant market power, and are pleased that this has been supported by the conclusions reached in the CAA's initial views.

This letter highlights our position on some of the high-level messages drawn out of the initial views. However, given the timescale (with the summary having been published on 31 January 2012 and the full initial assessment having been published on 24 February 2012) we have not had a considerable enough time to consider the full analysis in detail and welcome the opportunity to submit our full view at a later date.

**Heathrow - Initial Views on Market Power**

The CAA's view that there is consistent evidence to support the assessment that Heathrow airport enjoys a very strong market position, over a large proportion of the passengers, cargo shippers and airlines using the airport is one which we would wholly support.

Given that Heathrow is the only hub airport in the UK, we have specific requirements from the airport to support our operations which are not currently replicable at any other UK airport. For our operations Heathrow has the ability to sustain a high-level of connecting traffic and cargo operations in comparison to other UK airports. This therefore results in the number of airports with which Heathrow competes for airline business on a comparable basis as relatively limited.

We have continually made the point that we would face significant costs to relocate our business to alternative airports due to the adverse impact of switching (i.e. high sunk cost,

operational challenges..etc), on the quality of the network available at Heathrow and impact that this would have on our route yields.

The CAA comments that Heathrow competes for passengers in two distinct markets. For direct services, it competes with other airports in the South-East, although many passengers (particularly business travellers) appear to have a strong preference for using Heathrow. Given our operations from both Heathrow and Gatwick we would agree that there is a very strong preference for our passengers to utilise Heathrow over Gatwick on key business routes. For passengers connecting through Heathrow, we note the CAA's conclusion that Heathrow competes with other European hubs and in some cases hubs further afield.

However, on the airline market side, this is limited by the capacity available at the airport coinciding with the inability for incumbent airlines to switch away from Heathrow. While passengers do have the ability to utilise an alternative airport in prospect of higher charges (although this may not be a favourable option) we do not have the same flexibility to re-locate our operations. Therefore, we agree that this culminates in the airport sustaining a dominant market position, and retaining significant market power.

It is also noted that the CAA was unable to identify any factors which would indicate that Heathrow's market position would change significantly over the medium term. Although Heathrow stands to face increased challenge from Gatwick (and potentially Stansted) during this time, the impact of this competition in our opinion is unlikely to be offset by the market strength that comes from hub operations at the airport. This is particularly the case when combined with capacity constraints and growing demand also taking place at the airport.

#### **Gatwick - Initial Views on Market Power**

We welcome the initial view reached by the CAA that while there is a degree of competitive pressure at Gatwick airport, there are significant areas in which they continue to have SMP. We believe that given the current forecasts for demand growth and capacity constraints particularly during peak times, this position is likely to remain in the medium term. Furthermore, despite the recent change in ownership of the airport we do not believe that this has significantly impacted the degree of competition faced by Gatwick.

The analysis from the CAA notes the wide range and type of airlines who operate from Gatwick, and the specific requirements of long-haul operations from the airport which we welcome. We can of course see that competition for airlines can vary across market segments depending on the business model adopted. However, it would be beneficial to examine exactly how market power varies across different segments (i.e. charters, low-cost carriers and long-haul services) and parameters used for this. Whilst it is suggested that Gatwick appears to compete with Heathrow for long-haul leisure services, this competition will in reality be limited by the available capacity at Heathrow which acts as a barrier for entry, therefore constricting the market.

We note the suggestion that that the airport has a particularly strong market position in some segments through evidence that some passengers do not view Stansted as a particularly close alternative to Gatwick (despite their catchment overlaps). We continue to maintain the view that the higher yields achievable at Gatwick, the sunk-costs invested in the airport, the costs involved with switching operations and the lack of interlining carriers at Stansted all culminate in Gatwick having significant market power from our standpoint.

Although certain parties have provided evidence to the assessment that the current price controls keep its prices artificially low resulting in inflated airline route profitability, and therefore increase the apparent market power, we continue to dispute that this is the case.

Despite any changes in conduct since the airport was sold, we agree with the CAA that this does not constitute sufficient evidence to conclude that the airport no longer holds market power. Additionally, given how recent the change in ownership has taken place it is too soon to be able to draw any concrete conclusions that the airport no longer holds SMP. We believe that further evidence over a sustained period of time is necessary to illustrate any change in the level of competition at the airport.

### **Conclusion**

Overall, we welcome the initial conclusions that the CAA has reached in its assessment. From our perspective a pragmatic and consultative approach has been taken with the assessment, leading to well-rounded and evidenced conclusions being drawn.

We welcome the position taken in assessing the needs of a long-haul base carrier at both airports and the attempt to define the market within which they operate. Our continued opinion is that switching costs & substitutability, yield premiums and airport capacity all have a significant part to play in defining why both Heathrow and Gatwick continue to retain significant market power.

Virgin is available to elaborate on any of the comments made in this response in further detail. We would also welcome the opportunity to engage and submit further comments in the future on some of the details in this initial view.

Kind regards,



David Joseph  
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Virgin Atlantic Airways Limited