CAP 796

Flying on Business

a study of the UK business air travel market

Civil Aviation Authority

Regulatory Policy Group

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Flying on Business – a Study of the UK Business Air Travel Market

Part 1, May 2009
Traffic Trends and Characteristics

Part 2, December 2010
Analysis of the UK Business Air Travel Market

November 2011

ISBN 978 0 11792 405 5

First Edition November 2011

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Published by TSO (The Stationery Office) on behalf of the UK Civil Aviation Authority.

Printed copy available from:
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Telephone orders/General enquiries: 0844 477 7300
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Explanatory Note

This report on UK business air travel is made up of two separate studies by the CAA.

The first was published in May 2009 as *UK Business Air Travel: Traffic Trends and Characteristics*.[1] This examined how UK business traffic has changed by sector (long haul, short haul and domestic) between 1996 and 2007, and the characteristics of business passengers. It also looked at the expansion of the Business Aviation sector, which provides on-demand air services using small business aircraft, typically with fewer than 15 seats.

The second was published in December 2010 as *Flying on Business: a study of the UK business air travel market*,[2] and it further develops the analysis from the first study. It examines the drivers of UK business air travel and how they have been affected by the recent recession. It also looks at how companies manage their business travel, the changing role of travel management companies, how airlines compete for business travellers, and what may affect the demand for business air travel to and from the UK in the future.

Because the two studies are largely complementary, they have been combined into a single document for ease of reference. The first study forms Part 1, and the second study forms Part 2.

The content of each study is essentially unchanged, except where the first study referred to the CAA's intention to carry out a second study, where appropriate references to Part 2 have been substituted. Also, some material has been removed from the Introduction to Part 2 where this duplicates or sits better in the Introduction to Part 1. Although the second study refers to the first and second studies as Part 1 and Part 2 respectively, it should be noted that, with a few exceptions, the second study does *not* attempt to update the analysis in Part 1.

In preparing the combined document for publication some editorial changes have inevitably been necessary to keep a uniform phraseology, format and style wherever possible throughout the document. Any typographical errors have been corrected.

For continuity reasons the numbering of chapters, paragraphs, tables and figures has been retained from the original studies, but annexes have been prefixed with a 1 or 2 as appropriate. Page numbering and footnote numbering run consecutively through the document and do not correspond with the original publications.

Definition of business passengers

This report defines business passengers as those passengers whose air journey is undertaken for business purposes, as distinguished from a journey for the purpose of visiting friends and relatives or for other leisure activities.

Although the majority of passengers in premium cabins are travelling for business purposes, the majority of business travellers travel in economy class. Thus, the report considers all business passengers irrespective of the type of airline, ticket or cabin that they use for their travel.

Where the report refers to 'UK business passengers' or uses similar terms, this means passengers travelling for business purposes to and from UK airports, irrespective of whether they are resident in the UK.

Part 1 of the report also looks at the small but significant proportion of business travel carried out using business aircraft, typically with fewer than 15 seats, and often operating from smaller airfields. Some of this travel – such as businesses using their own aircraft to transport

1. Originally published at www.caa.co.uk/docs/5/ergdocs/20090515BusinessTravel.pdf.
2. Originally published at www.caa.co.uk/docs/589/ERG_FlyingOnBusiness_AStudyOfTheUKBusinessTravelMarket.pdf.

employees – will include non-commercial air transport. The report seeks to capture and present information available on this business aviation traffic. However, data is less readily available than for larger commercial operators. This is because a significant proportion of business aviation flights are to/from smaller airfields which are outside the scope of the CAA's collection of traffic statistics and survey data, and also because there is no requirement for some air-taxi operators and all private operators to report traffic data to the CAA. Consequently this report relies on flight data provided by Eurocontrol.

Acknowledgements

The CAA spoke to a wide range of organisations (businesses, travel management companies, airlines, airports, analysts and others) in the production of each of the two studies making up this report. Much of the source information has been drawn from these interviews, backed up by the CAA's traffic data and published survey evidence from a variety of sources. The provision of flight data by Eurocontrol is also greatly appreciated. The CAA would like to thank all those who contributed their time and information to help inform the content of this report.

Civil Aviation Authority

November 2011

Part 1 May 2009 – Traffic Trends and Characteristics

Executive Summary of Part 1

Introduction

1 Business air travel is an important aspect of international trade and economic development. Changes in the international business environment, particularly the move away from inward-looking trade regimes to more outward-oriented trade policies by many countries have led to rapid increases in the flow of goods, services and capital (both human and physical) between nations. With an increasingly globalised and financially integrated world economy, air transport services are necessary for moving people and goods swiftly within and between nations, and the increased liberalisation and deregulation of international air transport markets has facilitated this.

2 Between 1996 and 2007, the number of passengers travelling for business purposes to and from UK airports rose by nearly 20 million, while the proportion of business passengers using London airports remained at around two-thirds. The main growth in business travel was in passengers travelling in economy cabins, often to short-haul destinations and using no-frills carriers (NFCs).[3] Although Heathrow captured virtually all of the growth in passengers to long-haul destinations, its share of the London market for business travel fell. The use of business aviation – on-demand, non-scheduled services, often provided using small aircraft and uncongested airports – grew significantly between 1996 and 2007 and, despite accounting for only a relatively small proportion of all passengers travelling for business purposes, probably attracted passengers that would otherwise have used scheduled airlines' higher-yielding, premium classes.

3 CAA Passenger Survey data for 2008 suggests that, following the onset of the economic downturn, travel for business purposes declined at a faster rate than leisure travel in the latter part of the year. The number of business aviation flights fell particularly sharply in late 2008 and early 2009.

4 This study considers business passengers as those passengers whose air journey is undertaken for business purposes, irrespective of the cabin in which they are travelling (although the majority of passengers in premium cabins are travelling for business purposes, around 70% of long-haul and 90% of short-haul business travellers in 2007 used economy class). It considers the growth in business traffic in the last ten years, how this breaks down between routes and airlines, and the socio-economic characteristics of business passengers. It also considers the sub-sector of business aviation, which provides personalised on-demand services to business travellers.

Impact of the recent economic downturn on business travel

5 Given the close relationship between economic growth, trade and international business travel, it is unsurprising that the recent worldwide economic recession, along with the slump in consumer confidence and business investment, is having a significant impact on business air travel, particularly premium passengers. The rapidly

3. See Annex 1.A for a list of carriers serving UK airports which are categorised as 'no-frills' for the purpose of this study.

deteriorating economic and trading conditions are highlighted by the sharp falls in premium traffic flows within and across different world regions. According to IATA, international premium traffic began to fall in July 2008 and the monthly traffic decline has been particularly steep since November 2008, leading to a 21% fall in premium passengers worldwide in February 2009 compared with February 2008. British Airways (BA) also reported an average decline of around 12.5% in its premium traffic between September 2008 and February 2009 compared with the previous year.

6 The CAA Passenger Survey shows that UK scheduled business travel has suffered more than leisure traffic as the economic crisis continues, with the largest fall seen in the final quarter of 2008. Table 1 shows that, while leisure travel on all international scheduled flights from the four major London airports only grew marginally by 0.4% in 2008, international business travel fell by 6.3%.[4] Business passengers on long-haul and short-haul[5] routes have been particularly impacted since the second half of 2008, with falls of 8% and 22% respectively in the final quarter of 2008 compared with a year earlier following respective declines of 4% and 5% in Q3 2008.

Table 1 Growth of scheduled international business and leisure travellers at Heathrow, Gatwick, Stansted and Luton between 2007 and 2008

	Business	**Leisure**
Short haul	-8.0%	0.7%
Long haul	-3.0%	0.1%
Total international	**-6.3%**	**0.4%**

Source: CAA Passenger Survey, 2007 and 2008.

7 The latest Eurocontrol data suggest that the economic downturn has had a significant impact on business aviation, with the number of UK business flights falling by over 20% year on year in the fourth quarter of 2008 and early 2009. In part, this is likely to be due to business aviation being an on-demand service. A downturn in demand is therefore likely to result in an immediate decline in movements, whereas for commercial air transport, weakening demand may be reflected first in lower seat factors and yield reductions and only later in fewer flights.

8 Although the current worldwide economic downturn has had a significant effect on business travel demand particularly in the last quarter of 2008, it is still too early to assess the extent and likely duration of the impact that the current recession might have on business travel. Future work will look at these effects more closely when more data become available, although any impact of the current recession needs to be seen in the context of a longer term pattern of growth, described below.

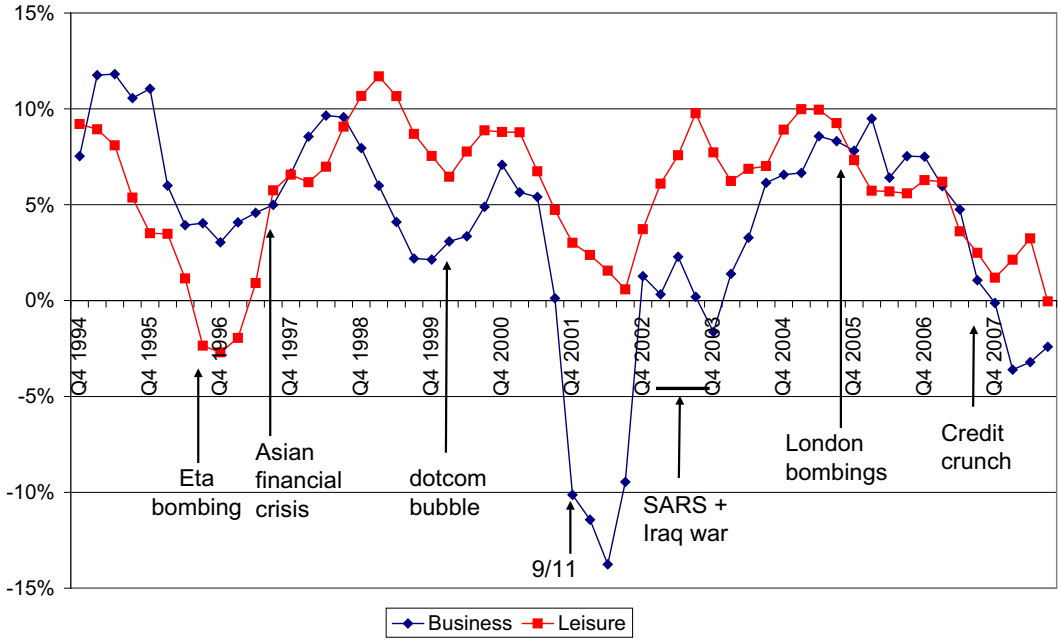
Growth in business travellers from UK airports between 1996 and 2007

9 Despite a number of adverse shocks between 1996 and 2007 that had a varying degree of impact on business and leisure traffic (Figure 1), business passengers on scheduled flights to/from UK had increased from around 43 million in 1996 to almost 63 million in 2007, representing an average annual growth rate of about 3.4% per

4. These figures from the four major London airports compare with a fall of 1.9% of all passengers (including scheduled and charter passengers travelling on domestic and international flights) handled by UK airports in 2008 compared with 2007.
5. For the purposes of this study, long-haul is defined as all those destinations outside geographical Europe and North Africa (Morocco, Algeria, Tunisia, Libya and Egypt), but where, for convenience, all destinations in both Russia and Turkey are defined as short-haul.

annum.[6] However, the growth of leisure passengers on scheduled flights over the same period was even stronger, with an average annual growth rate of more than 8% per annum. Consequently, business passengers as a proportion of total UK scheduled traffic have fallen from 41% in 1996 to 30% in 2007.

Figure 1 Rolling annual growth of international business and leisure passengers at all UK airports, 1994–2008



Source: *International Passenger Survey (MQ6), ONS.*

Note: *Data exclude domestic and international-to-international connectors. Q1–Q3 2008 figures are provisional only.*

10 Table 2 shows that the growth in business traffic since 1996 has varied considerably by airport. The share of business passengers at regional airports has increased only modestly from 35% to 38% over the period. However, despite Heathrow's continued strong position in business traffic, growth in business traffic since 1996 has been spread fairly evenly between the four major London airports with each seeing an increase of over 2 million. London City has also grown considerably over the period, by 1.4 million business passengers, from under half a million in 1996.

6. Based on CAA Passenger Survey data which include domestic and international-to-international connectors. Some airports' data are scaled up from the nearest survey year or, where no survey data exists, modelled on data from similar surveyed airports.

Table 2 Volume and growth of scheduled business passengers between 1996 and 2007

Airport	Business passengers (m)					
	1996	**2007**	**Passengers gained**	**Average growth p.a.**	**% share in 1996**	**% share in 2007**
Heathrow	22.0	24.3	2.3	0.9%	51%	39%
Gatwick	4.0	6.2	2.3	4.2%	9%	10%
London City	0.4	1.9	1.4	13.8%	1%	3%
Luton+Stansted	1.6	6.5	4.9	13.5%	4%	10%
London total	***28.0***	***38.9***	***10.8***	***3.0%***	***65%***	***62%***
Manchester	3.0	4.4	1.4	3.5%	7%	7%
Birmingham	1.8	2.1	0.3	1.4%	4%	3%
Glasgow	2.0	2.8	0.7	2.8%	5%	4%
Edinburgh	2.0	3.9	1.9	6.4%	5%	6%
Belfast	1.4	2.4	1.0	5.2%	3%	4%
Other UK regions	5.1	8.3	3.2	4.5%	12%	13%
Regional total	***15.3***	***23.8***	***8.5***	***4.1%***	***35%***	***38%***
UK total	**43.3**	**62.7**	**19.4**	**3.4%**	**100%**	**100%**

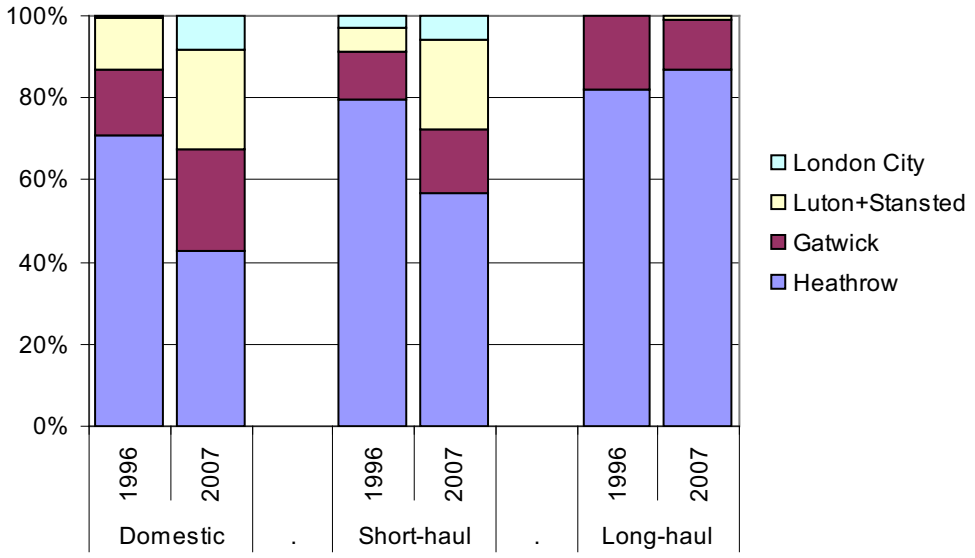
Source: CAA Passenger Survey, 1994–1996, 2005–2007.

Note: Data include domestic and international-to-international connectors.
Belfast includes Belfast City and Belfast International airports.
Airports not surveyed in 1996 and/or 2007 have been scaled up from the nearest survey year or, where no survey data exists, modelled on data from similar surveyed airports.

11 However, the increase of almost 11 million business passengers using the London airports was distributed differently for domestic, short- and long-haul sectors. In particular, the number of domestic and short-haul business travellers at Heathrow has not increased over this period, while the airport has captured virtually all the growth in long-haul business passengers (three million in total) at London airports. This was in part due to BA's network restructuring that has seen a substantial portion of its long-haul traffic transferred from Gatwick to Heathrow since 2001.

12 Figure 2 shows the change in share of business passengers among the London airports between 1996 and 2007. The notable gain in domestic and short-haul business passengers by Stansted, Luton and London City airports probably reflects a combination of factors: the capacity constraint at Heathrow, which has tended to displace domestic and shorter haul services in favour of longer haul flights; the growing success of London City; and the ability of NFCs at Luton and Stansted to attract business travellers for whom these airports are more convenient.

Figure 2 Percentage share of business passengers at London airports in 1996 and 2007



Source: CAA Passenger Survey, 1996 and 2007.

Note: 2007 London City figures have been scaled up from 2006 (its latest survey year).

Where do business passengers fly to/from?

13 The UK's overall origin/destination (O/D) international business traffic[7] is dominated by North American and European countries, which are also the most significant in terms of volume of trade with the UK. Table 3 shows that the top five business destinations in 2007 together accounted for 46% of UK's total O/D international business passengers and 44% of total volume of trade with the UK.

14 However, emerging markets such as United Arab Emirates, India and China have had the largest growth rates between 1996 and 2007, albeit from a relatively low base in 1996.

7. UK O/D international traffic is those passengers whose full journey begins or ends in the UK. It therefore excludes passengers connecting between international flights at a UK airport and domestic passengers.

Table 3 Country origins/destinations with most international business passengers and growth, 2007

COUNTRY	Business Passengers (m)	% of total international business passengers	% passenger growth over 1996	Share of total UK trade
Top 5 destinations:				
Germany	4.0	11.9%	45%	11.8%
United States	3.7	11.1%	36%	13.9%
Irish Republic	3.1	9.4%	128%	3.8%
Netherlands	2.3	7.0%	58%	6.7%
France	2.2	6.6%	17%	7.8%
Emerging markets:				
India	0.5	1.5%	151%	1.3%
United Arab Emirates	0.4	1.1%	155%	0.6%
China	0.3	0.9%	521%	3.4%
Total international	**33.3**	**100%**	**61%**	**100%**

Source: CAA Passenger Survey, 1994–1996, 2005–2007, excluding international-to-international connectors; ONS Exports and Imports of Goods and Services by Country.

Note: Tables includes only airports surveyed by the CAA. Airports not surveyed in 1996 and/or 2007 have been scaled up from the nearest survey year.

Long-haul

15 Long-haul scheduled business travel[8] at UK airports has grown from 8 million passengers in 1996 to 11 million in 2007. It is still very much dominated by North Atlantic destinations (constituting more than 40% of total UK long-haul business passengers), particularly to/from New York City. However, there was faster growth in business passengers between 1996 and 2007 to cities (for example, Shanghai, Beijing, Mumbai, Bangalore, Chennai, Dubai, Abu Dhabi and Doha) in emerging markets such as China, India and Middle Eastern countries.

16 For scheduled business passengers travelling on long-haul routes, just over 50% of passengers used either BA or Virgin Atlantic in 2007, a figure which had remained unchanged from 1996[9]. Less than 7% of business travellers to long-haul destinations used UK regional airports in 2007, only slightly up from the proportion in 1996.

8. This includes business passengers travelling to a short-haul hub, such as Amsterdam, to connect to a long-haul fight.
9. Interpretation of airlines' shares of business passengers should be cautious as airports not surveyed in 1996 or 2007 have been scaled up from their nearest survey years. As some of the routes served by individual airlines might have come in and out of operation at an airport between its survey year and the target year, this must be taken into account when interpreting the results.

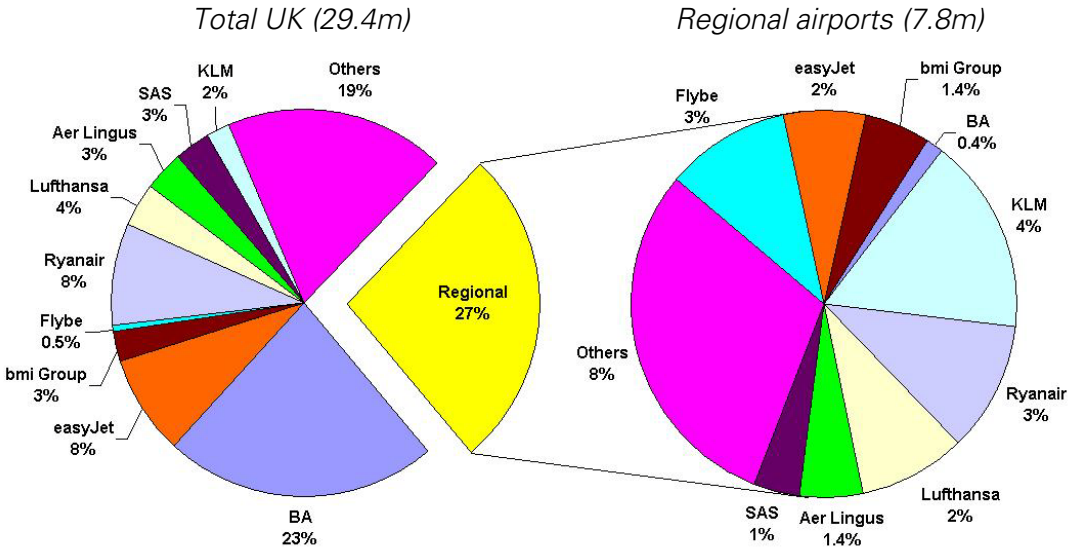
Short-haul

17 UK short-haul travel is the largest segment of scheduled business traffic in terms of passenger numbers, and grew from 19 million passengers in 1996 to 29 million in 2007. A high proportion is to and from the main financial centres or capital cities of Europe such as Dublin, Amsterdam, Paris, Frankfurt and Brussels. However, secondary cities such as Barcelona, Cork, Nice and Prague have also registered strong business traffic growth. Both leisure and business passengers (in particular business passengers from small and medium sized enterprises in the regions) will have benefited from increased flight frequency, lower fares and a wider range of originating airports providing a credible business offer from both London and the regions following the growth of NFCs.

18 Paris and Brussels were still in the top five short-haul city destinations for business passengers travelling by air in 2007, with 1.2 million and 0.7 million passengers respectively. However, while overall short-haul business travel had grown by 69% since 1996, these markets had seen falls of 11% and 9% respectively over the same period, indicating the effect of increased competition from Eurostar services.

19 NFCs now carry a significant proportion of short-haul international business passengers, from 3% in 1996 to around 30% in 2007. Figure 3 shows the proportion of passengers on short-haul routes by airline in 2007 at London and regional airports. The number of business passengers carried at regional airports doubled (from around four million to almost eight million) between 1996 and 2007.

Figure 3 Share of business passengers on short-haul scheduled flights by carrier at London and regional airports, 2007



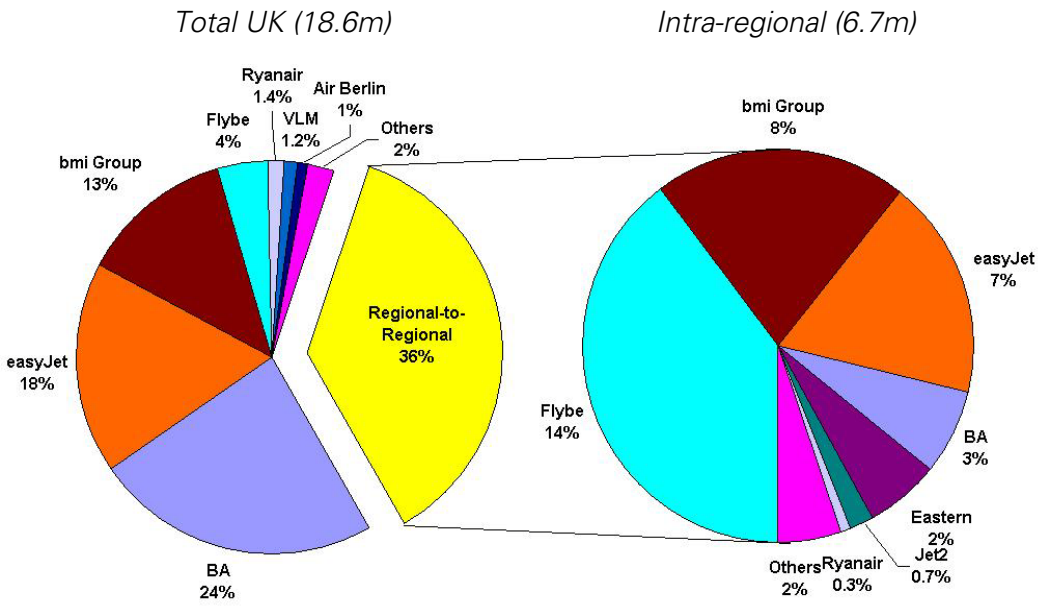
Source: CAA Passenger Survey, 2005–2007.

Note: Figure includes only airports surveyed by the CAA. Airports not surveyed in 2007 have been scaled up from the nearest survey year. BA figures include passengers carried by its franchisees. bmi Group includes bmi Regional and bmibaby. Flybe figures in 2007 include passengers carried by BA Connect.

Domestic

20 Domestic scheduled business traffic at UK airports grew from 15 million passengers in 1996 to 19 million in 2007,[10] the great majority of which has been on routes between regional airports. Nevertheless, as Figure 4 shows, domestic business travel is still dominated by London–regional traffic, albeit the market share of London as a business destination has diminished from 32% to 27% between 1996 and 2007.

Figure 4 Share of business passengers on domestic scheduled flights by carrier between London and regional airports 2007



Source: CAA Passenger Survey, 2005–2007.

Note: Figure includes only airports surveyed by the CAA. Airports not surveyed in 2007 have been scaled up from the nearest survey year. BA figures include passengers carried by its franchisees. bmi Group includes bmi Regional and bmibaby. Flybe figures in 2007 include passengers carried by BA Connect.

Characteristics of business travellers

21 In recent years the proportion of business passengers who travel in premium classes has declined across all sectors, particularly in the short-haul market. The average 3.4% per annum growth rate of business passengers between 1996 and 2007 has masked a downward trend in airline average yields since the late 1990s and a shift of business passengers from premium cabins to economy class. The last two columns of Table 4 show that the proportion of long-haul business passengers travelling in the First/Business Classes fell from 34% in 1996 to 23% in 2007 while the short-haul international market saw an even bigger decline (more than 30 percentage points) over the period.

10. Domestic passengers are counted twice as the same passenger is registered at both the departure and arrival domestic airports.

Table 4 Proportion of business passengers travelling in different cabin classes

	How much of each cabin is filled by business passengers?		Which cabin do business passengers use?	
Ticket Type	*1996*	*2007*	*1996*	*2007*
Long-haul destinations				
First/Business/Club	79%	73%	34%	23%
Premium Economy	n/a	56%	n/a	9%
Economy	28%	20%	66%	69%
Total long haul	36%	25%	100%	100%
Short-haul int'l destinations				
Business/Club	93%	81%	40%	9%
Economy	39%	26%	60%	91%
Total short haul	50%	28%	100%	100%

Source: CAA Passenger Survey, 1994–1996, 2005–2007.

Note: Airports not surveyed in 1996 and/or 2007 have been scaled up from the nearest survey year.

22 Passenger surveys reveal that a greater proportion of business passengers at the London airports in 2006[11] earned less than £46,000 per annum (in real terms) than in 1996, that the proportion of female business travellers has remained at around 20% since 1996, and that over two–thirds of business passengers describe the reason for their trip as either 'attending internal company business' or 'meeting external clients'.

23 Table 5 shows the professions of business passengers at the London airports in 2006. It indicates that 'City' occupations[12] such as banking and legal feature highly among business passengers and, in particular, London City has the highest proportion (48%) of business passengers from this industry group, probably due to its close proximity to the financial centre[13] of London; the range of business oriented destinations served; level of frequency offered and the speed of transit through its terminal building. The table also shows that the distribution of professions at London City differs from that at the other airports. However, there is little difference in distribution between full-service (FSCs) and no-frills carriers at Gatwick, Stansted and Luton.[14]

11. 2006 survey data is used in this example, as this is the most recent survey data available for London City (other London airports are surveyed continuously).
12. For brevity, the banking, financial, insurance and legal professions are referred to in this report as 'City' occupations, however this does not necessarily refer to their geographical location.
13. For the purposes of this report, the 'financial centre' refers to that area of London where the majority of the capital's workers employed in 'City' occupations are based. This comprises two main locations – the City of London (the 'Square Mile') and Canary Wharf. Both are located to the east of the capital, and are approximately five miles apart. Transport links and geographical proximity mean that Stansted and London City are well-placed to serve this area. The opening of the DLR station at London City in 2005 improved accessibility further, from both Bank station in the City of London and from Canary Wharf itself.
14. There were no NFCs serving Heathrow or London City in 2006.

Table 5 Distribution of business passengers by industry group at London airports in 2006

Industry Group	London City	Heathrow	Gatwick + Stansted + Luton	
			NFCs	FSCs
Banking/Finance/Insurance/Legal	48%	20%	16%	18%
Health/Education/Public Services	11%	14%	16%	16%
Transport & Communications	8%	14%	13%	14%
Engineering/IT Consulting/Electrical Supplies	7%	12%	12%	10%
Catering, Retail, Wholesale and Hotel	4%	6%	10%	6%
Energy & Water Supply Industries	5%	5%	3%	9%
Mining & Manufacturing Industries	4%	9%	5%	6%
Other Business	13%	20%	25%	20%
Total business passengers (m)	1.5 (100%)	24.2 (100%)	7.7 (100%)	3.9 (100%)

Source: CAA Passenger Survey, 2006.

Business aviation

24 Although the bulk of business travel takes place on commercial scheduled airlines at major airports, there is a small but significant proportion of UK business travel using small business aircraft, typically with less than 15 seats, based on ad hoc services operating from smaller and less congested airfields. Business aviation is commonly regarded as the use of any general aviation aircraft for a business purpose. This includes non-commercial operation of an aircraft owned by a company or individuals or commercial operation by an operator (such as air taxi and fractional operators)[15] having a commercial operating certificate.[16]

15. Fractional ownership means having a share of a business aircraft which normally involves owning block(s) of flying time of 100 hours or more per year (broadly equivalent to 1/8th shares of an aircraft) although it is also possible to own smaller shares of an aircraft.
16. Since most UK business aviation traffic is outside the scope of CAA traffic statistics and survey data, and information on the number of business passengers using business aviation services is not readily available, the analysis of business aviation traffic hereafter is based on available flight data of certain types of small aircraft from Eurocontrol which are considered to be most likely used for business aviation services. (See Annex A of More to the Point: Business Aviation in Europe in 2007, Eurocontrol, 2008.)

25 Between 2003 and 2007, business aviation movements to/from the UK grew by an average of 13.7% per annum. In 2007, business aviation accounted for 7.3% of all UK movements (excluding overflights) operated under 'instrument flight rules' (IFR), although this figure has dropped to 6.9% in 2008.[17] There are no figures for the number of passengers carried by business aviation, but it may be less than 1.5% of the business passengers carried by scheduled services[18] (although this would represent a much higher proportion of those travelling in premium cabins).

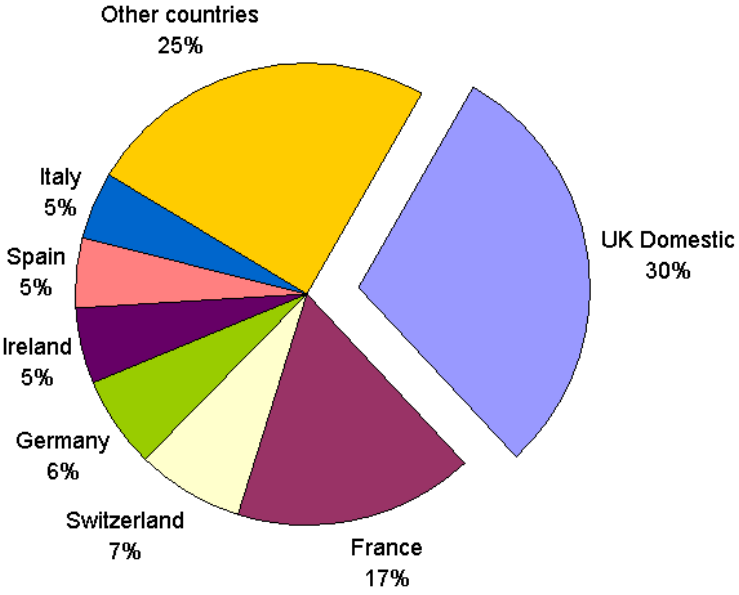
26 The rising popularity of business aviation in recent years has been driven by a range of factors. While some of these are general drivers (such as increasing globalisation and economic growth) that affect all air travel segments, others are more specific for business aviation. For example, the use of smaller and less congested airports of a client's choice to avoid delays at some major airports, and the ability to choose to fly to specific destinations at the most convenient times (which scheduled flights may not be able to provide) are some of the factors which make use of business aviation an attractive alternative for premium travel for some time-sensitive business travellers.

27 Business aviation has a very different business model and operational characteristics from scheduled carriers. The UK business aviation market is served by a few big operators along with many small operators which have a fleet size of less than five aircraft. Business aviation serves a wide network that spreads small volumes of air traffic among a large number of small and medium sized airports – only around 7% of the more than 14,000 UK–international airport pairs used by business aviation services had alternative scheduled services (i.e. with at least one scheduled departure per working day). Business aviation operations have more peaky demand patterns (especially for hourly traffic) than scheduled traffic, and the volume and direction of traffic flows can be highly variable.

28 Figure 5 shows the destinations served by UK business aviation in 2008. Domestic flights made up the largest segment (30%),[19] while for international traffic to and from the UK, France accounted for almost 17% of all UK business movements – more than double that of any other country. The six major international destination countries, all European, combined with domestic traffic, made up three-quarters of all UK business aviation movements in 2008.

17. Flights are generally referred to as operating under 'IFR' when they are operating within the en-route air traffic control structure for some or all of the journey.
18. Typically, business aircraft might have a configuration seating between four and twelve persons. Assuming there are, on average, five business travellers per flight, and given that a high proportion of these are air taxi and fractional positioning flights, the estimated number of passengers carried by business aviation would be well under one million as compared with the 63 million passengers travelling for business purposes or 240 million total UK passengers on commercial flights in 2007.
19. Domestic movements are only counted once here to aid comparison.

Figure 5 Business aviation movements to/from the UK (2008)



Source: Eurocontrol.

Note: Domestic movements are only counted once to aid comparison.

29 Because of the ad hoc nature of many business aviation services, business aviation has increasing difficulty in gaining access to major congested airports such as Heathrow and Gatwick which are slot-coordinated. Consequently, business aviation traffic in the London area has spread among secondary and less congested airports around London such as Luton, Biggin Hill, Farnborough, London City and Northolt.[20]

30 The UK airport with the most business aviation departures in 2008, an average of 38 per day, was Luton. Farnborough averaged 29 departures per day, Biggin Hill 17 departures and London City 13 departures. All other UK airports averaged less than 10 business aviation departures per day in 2008.

20. Business aviation operators using Luton and London City, which have a significant proportion of business aviation traffic (around 25% and 15% respectively of each airport's total movements in 2007), also face potential pressure from scheduled carriers in obtaining regular and sustained runway access as these airports become more congested.

Part 1 Chapter 1 Introduction to Part 1

1.1 International trade in goods and services has been an important driver of regional and global economic growth and rising prosperity in recent decades. With deregulation and liberalisation of air transport markets in various parts of the world, and an increasingly globalised and competitive economy, the air transport industry has been an important facilitator of the rapid movement of people and goods across national borders and within countries. On the demand side, passenger air services are vital for international trade, with recent surveys suggesting that around two-thirds of companies consider business air travel to be vital or very important for sales and marketing, enabling them to meet potential customers face-to-face and to keep in touch with existing clients, suppliers and staff across the world.[21]

1.2 On the supply side, passengers travelling in premium cabins (first/business/premium economy) are particularly important for the financial health and viability of, in particular, the network scheduled airline industry, contributing significantly to airlines' revenues and profits. For example, British Airways (BA) derived around 50% of its total revenue from premium travellers in 2007/08[22] even though they made up less than 15% of its total passengers carried.[23]

1.3 In 2007, 240 million passengers travelled through UK airports,[24] of which 87% travelled on scheduled services, while the remaining 13% used charter services, representing a growth of 2.3% over 2006 and an average annual growth of 5.3% since 1996. Over the same period, passengers travelling for business purposes[25] on all carriers have been growing at a lower average annual rate of 3.4% per annum, making up around a quarter of all UK air traffic in 2007. Short-haul[26] destinations remain by far the most significant segment of the business market in terms of passenger numbers.

1.4 However, total UK traffic declined by nearly 2% to 235 million in 2008 as the impact of the financial crisis began to spread to the real economy in the UK and across most countries. This fall in travel demand affected both UK scheduled and charter services, although there were variations across airports and traffic segments. Recent evidence suggests that premium passenger numbers (especially demand for business aviation services)[27] are declining more than leisure passenger numbers in the global economic downturn, highlighting the importance of international trade and finance in driving business travel. For example, IATA reported a marked decline in total premium traffic since July 2008 as a result of the ongoing financial and economic crises. The monthly reductions compared with a year earlier have been particularly steep in the latest four months of available data, showing an accelerated fall in premium traffic from 11.5% in November 2008 to 21.1% in February 2009 compared with a corresponding drop of around 4%-8% in economy travel. BA's premium traffic also dropped by 14% on average between November 2008 and March 2009 while non-

21. IATA: The Economic and Social Benefits of Air Transport (2008).
22. BA presentation to analysts, Preliminary Full-Year Results 2007/08, 16 May 2008.
23. Based on CAA Passenger Survey 2007.
24. These 240m passengers include international-to-international connecting passengers at UK airports and domestic passengers are being counted both at the airport of arrival and at the airport of departure.
25. The definition of business passengers used for the purposes of this study appears in the Explanatory Note at the beginning of the document.
26. For the purposes of this study, long-haul is defined as all those destinations outside geographical Europe and North Africa (Morocco, Algeria, Tunisia, Libya and Egypt), but where, for convenience, all destinations in both Russia and Turkey are defined as short-haul.
27. Business aviation is commonly regarded as the use of air taxis or any general aviation aircraft for a business purpose (see Chapter 4 for further details on this sub-sector of business travel).

premium traffic fell by only about 4% over the same period.[28] Since business travel is one of the major variable cost items for many companies, corporate expenditure on travel is likely to be scrutinised more than ever in an economic slowdown. As companies feel the economic pinch and seek value for money from their business trips, recent surveys by Association of Corporate Travel Executives (ACTE), Travelodge and others have indicated that a significant number have introduced travel cutbacks (for example, trading down cabin class and cutting back hotel spending) and/or imposed a ban on non-core business travel such as trips for internal meetings.[29]

1.5 Because of the importance of passengers travelling for business purposes for airline revenue[30] and their differing demand characteristics from other type of passengers,[31] a change in the mix of business and leisure passengers could affect operational and strategic decisions of airlines, such as scheduling, aircraft size and configuration, code sharing or alliance decisions, and network and pricing strategies.

1.6 This study focuses on the recent trends and characteristics of business travel to/from UK airports, in respect of both commercial scheduled[32] air transport and on-demand business aviation services. It complements other previous air passenger studies by the CAA such as those on UK leisure outbound traffic[33] and passengers visiting friends or relatives,[34] each representing other segments of the UK air passenger market.

Structure of Part 1 of this study

1.7 Due to the scope of topics related to business air travel, this study was carried out in two parts.

1.8 **Part 1** examines recent trends of air passengers travelling on business purposes and their socio-economic characteristics. It considers the growth in business travel in the last ten years and seeks to discern any emerging trends from this important and high-yielding passenger segment by route and by airline. The analysis is extended to include a relatively small but fast-growing sub-sector of business travel in recent times – business aviation – which provides personalised on-demand services, primarily to time-sensitive business travellers.

1.9 Chapter 2 looks at the historic and recent trends of UK business and leisure traffic at various airports and discusses the disparity in traffic growth rates between London and regional airports.

1.10 Chapter 3 presents a more detailed analysis of business passenger growth on long-haul, short-haul and domestic routes and how this varies by London and regional airport and by carrier. The competitive pressures from rail on short-haul routes are illustrated by a case study on travel to/from Paris and Brussels. The routeings taken by business passengers to long-haul destinations are also discussed.

28. BA's premium and non-premium traffic fell by 20% and 5.5% respectively in February, although this was distorted by the Leap Year in 2008 and by a number of flight cancellations due to the heavy snowfall in the South East of England during the first week of February 2009.
29. According to the travel consultant company Edgar, Dunn and Company, some companies may spend up to 40% of their total travel budget on internal meetings.
30. On full-service carriers, business passengers are more likely than leisure passengers to travel in premium cabins and use fully-flexible tickets; on no-frills carriers, they are more likely to book later (paying higher fares) and provide more ancillary revenue than leisure passengers.
31. For example, business passengers tend to be more time sensitive but less price elastic than leisure travellers.
32. This study focuses on scheduled passengers only. The proportion of business passengers using charter services is typically less than 0.5% of the total passengers at an airport.
33. Demand for outbound leisure air travel and its key drivers, CAA (December 2005).
34. *CAP 787 International relations: the growth in air travel to visit friends or relatives*, CAA (March 2009). www.caa.co.uk/cap787

1.11 Chapter 4 examines the socio-economic characteristics of business passengers and their professions. It also examines the use of premium cabins by business passengers and the catchment areas from which Heathrow and London City airports – the two London airports with the highest proportion of business passengers – draw their short-haul business passengers.

1.12 Chapter 5 studies the fast growing but relatively small (in terms of both the number of flights and passengers carried) business aviation sector in recent years, its unique demand and supply characteristics, and early indications of how this sector has been impacted by the worldwide recession.

1.13 While Part 1 of this study aims to set the scene by presenting background information on business air travel, **Part 2**[35] considers some of the demand and supply-side factors that have facilitated the growth of business travel in recent years and influenced the operational and strategic decisions made by carriers regarding their network scheduling and development; aircraft size and configuration; code sharing or alliance decisions; and pricing strategies. In particular, Part 2 discusses the potential demand drivers for business travel at both macro and micro levels along with the impact of the recent global economic downturn on this traffic segment.[36] Given the importance of premium-class passengers for the profitability of full-service scheduled carriers, Part 2 also discusses how airlines respond to changes in this market and compete for this higher-yield passenger segment.

35. Part 2 was published later, in December 2010, and now forms part of this combined document (see the earlier Explanatory).
36. When Part 1 was published in May 2009, it was still too early to assess the extent of the impact of the downturn and how long it might last. Furthermore, at that time, 2008 survey data was still provisional and therefore subject to revisions.

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Part 1 Chapter 2 Business travel since 1996

Chapter summary

Between 1996 and 2007:

- Business passengers as a proportion of total UK scheduled traffic have fallen from around 42% to 30%; the domestic sector had the largest presence of business passengers (45%) in 2007, followed by the short-haul (27%) and long-haul (24%) sectors.
- The business element of air travel has appeared to be reasonably resilient to external shocks in the past, although the 11 September 2001 terrorist attacks had a notable impact on international business travel (especially to/from North America) and the current economic downturn is taking a heavier toll on business (and particularly premium-class) passengers than leisure traffic.
- Business traffic has grown far less strongly than leisure traffic in both London and the regions (London City is the only exception, where business traffic grew marginally faster than leisure traffic).
- The share of total UK business traffic at regional airports only increased moderately from 35% to 38%, although the share of total scheduled leisure traffic at regional airports increased by 15 percentage points to 38% over the same period.
- The proportion of total business passengers using Heathrow among the London airports has fallen, since the rate of growth of business traffic has been higher at the other London airports. However, Heathrow has captured virtually all the growth in long-haul business passengers while the numbers of domestic and short-haul business travellers there have either declined or remained flat over this period.

2.1 This chapter examines trends in business travel to and from the UK since 1996 across different airports. It begins by presenting a brief overview of the growth trends of UK business and leisure traffic and how they have been affected since 1996 by some external events such as the bombing incidents in Spain and in London, the Asian financial crisis, the IT bubble, 11 September (9/11) attacks, SARS and the Iraq War. It also discusses the rapid expansion of NFCs[37] that underpins much of the observed change since 1996 in the mix of business and leisure passengers at London and regional airports.

37. See Annex 1.A for a list of carriers serving UK airports which are categorised as 'no-frills' for the purpose of this study.

Historic and recent traffic trends

2.2 Business passengers on scheduled flights have increased from around 43 million in 1996 to almost 63 million in 2007.[38] This represents an average annual growth rate of 3.4% between 1996 and 2007 or an increase of 45% over the period. However, the growth of leisure passengers on scheduled flights over the same period was even stronger, with an average annual growth rate of more than 8% per annum. As a result, business passengers constituted around 30% of all scheduled passengers in 2007, compared with 41% in 1996.

2.3 CAA analysis[39] from 2003 found that passenger traffic at UK airports enjoyed relatively robust growth and was markedly resilient, with the growth rate of passenger demand tending to recover quickly from external shocks. The only exception, perhaps, was the 1970s oil crisis and the subsequent economic recession, which appeared to change permanently the underlying trend of UK passenger demand. Table 2.1 shows that, over the last decade or so, despite numerous adverse external events, UK international passenger traffic experienced robust growth of, on average, 5.8% per annum between 1996 and 2007. However, there was evidence of traffic growth slowing in recent years, affecting domestic and UK outbound leisure traffic more than other segments.[40]

Table 2.1 Average annual growth of UK international traffic by passenger journey purpose 1996–2007

	Business	Leisure	Total
1996–2005	2.9%	7.1%	6.2%
2005–2007	3.6%	3.7%	3.7%
1996–2007	3.0%	6.5%	5.8%

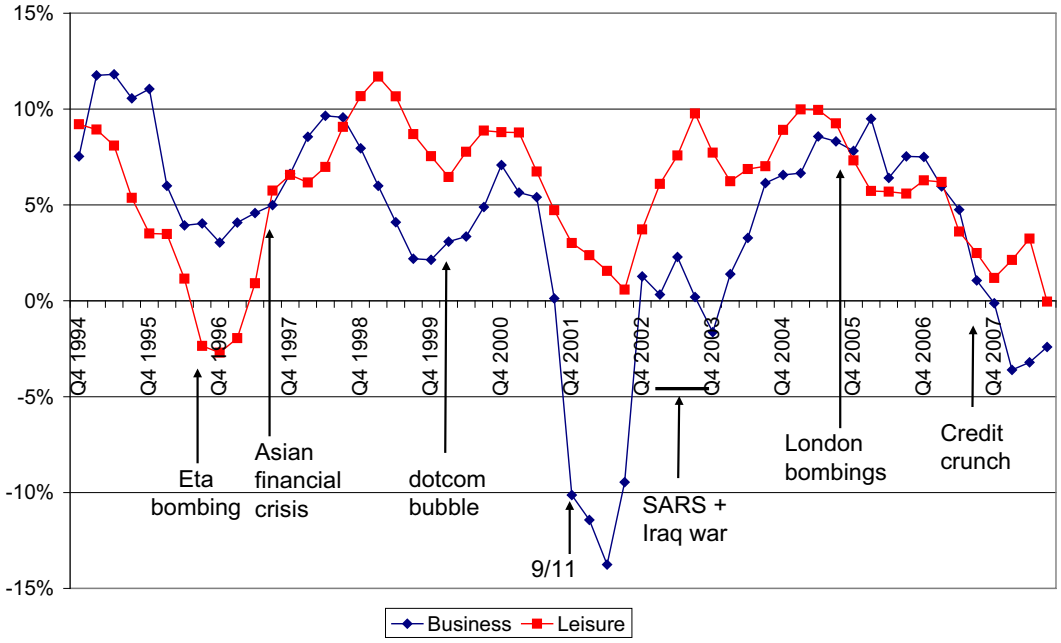
Source: International Passenger Survey (MQ6), ONS.

Note: Data exclude international-to-international connectors.

2.4 Notwithstanding this resilience, Figure 2.1 illustrates that there were notable differences between leisure and business passengers in terms of the impact of, and subsequent recovery from, these adverse shocks. In contrast to those who travelled internationally for leisure purposes, business passengers travelling on international flights were particularly affected by the 9/11 terrorist attacks in 2001. Full recovery from the incidents was delayed by the Iraq War and SARS in 2003. Other events did not appear to have as significant or long lasting an impact on business passengers as the 9/11 attacks. Early indications from the current economic downturn, which started in the US in the second half of 2007 and has subsequently developed into a global financial and economic crisis, suggest that it is initially taking its toll more on business than on leisure travel according to the latest International Passenger Survey (MQ6) data published by the UK Office of National Statistics (ONS).

38. Based on data from the 20-plus airports surveyed by CAA between 1994–96 and 2005–07. These airports represented almost 95% of all UK scheduled passengers in 2007, including domestic and international-to-international connectors. Since not all airports are surveyed by the CAA each year, data from airports not surveyed in 1996 and 2007 have been scaled up from the nearest survey year (or, where no survey data exists, modelled on data from similar surveyed airports) to each airport's total terminal passenger figure in 1996 or 2007. This study focuses on scheduled passengers only. The proportion of business passengers using charter services is typically less than 0.5% of the total passengers at an airport.
39. *Air passenger growth and airport capacity*, CAA *(July 2003)* http://webarchive.nationalarchives.gov.uk/20040104234901/http://dft.gov.uk/aviation/whitepaper/supporting/pdf/air_passenger_growth_and_airport_capacity_caa_report.pdf.
40. *Recent trends in growth of UK air passenger demand*, CAA (January 2008) www.caa.co.uk/docs/589/erg_recent_trends_final_v2.pdf.

Figure 2.1 Rolling annual growth of international business and leisure passengers at all UK airports, 1994–2008

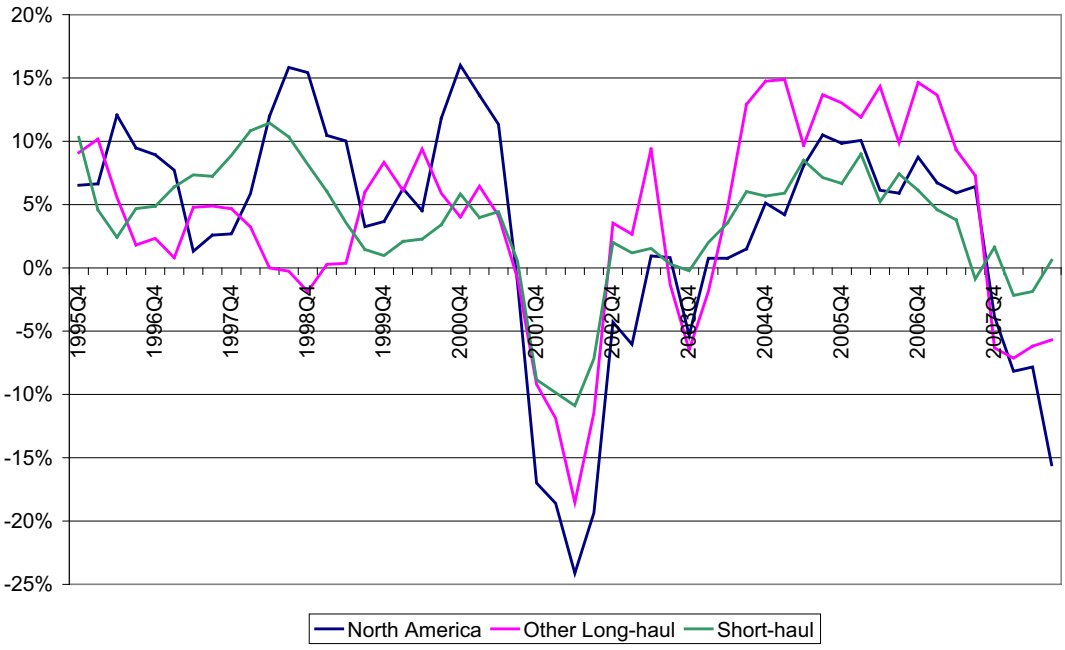


Source: International Passenger Survey (MQ6), ONS.

Note: Data exclude international-to-international connectors. Q1–Q3 2008 figures are provisional only.

2.5 A further disaggregated analysis of the International Passenger Survey (MQ6) data published by ONS (see Figure 2.2 below) reveals that, while the 9/11 attacks affected all business routes, particularly to/from North America, the impact of the Asian financial crisis that began in mid-1997 seemed to be limited to business travel to/from Asian countries only.

Figure 2.2 Rolling annual growth of international business passengers at UK airports by destination, 1995–2008



Source: International Passenger Survey (MQ6), ONS.

Note: Data exclude international-to-international connectors. Q1–Q3 2008 figures are provisional only.

2.6 Figure 2.3 shows that, although leisure traffic to North America and other long-haul destinations was affected by 9/11, the decline was less steep than that of business traffic.[41] On the other hand, a series of bombing incidents by Eta at a number of Spanish tourist destinations in 1996 had a notable impact on short-haul leisure traffic,[42] with an immediate drop in Q3 1996 of more than 20% of leisure passengers to Spain alone. Spain made up around one third of all short-haul leisure traffic to/from UK airports in 1996.

Figure 2.3 Rolling annual growth of international leisure passengers at UK airports by destination, 1995–2008

Source: International Passenger Survey (MQ6), ONS.

Note: Data exclude international-to-international connectors. Q1–Q3 2008 figures are provisional only.

Impact of the recent economic downturn

2.7 The sub-prime mortgage problem in the US that began in the summer of 2007 has since become a global financial crisis, and what looks like being the most severe world recession since the 1930s. The economic downturn intensified following the collapse of the Wall Street investment bank Lehman Brothers in September 2008. Falling stock markets and house prices, along with rising unemployment, levels of household and corporate indebtedness and economic uncertainty, have taken a toll on both consumer spending and business confidence. According to the World Trade Organisation, the slump in global demand led to a significant slowdown in the growth of world trade in volume terms from 6% in 2007 to 2% during 2008, with a sharp decline of roughly 9% forecast for 2009, the biggest drop since the Second World War.[43]

41. North America leisure traffic had been slowing down since the beginning of 2001. The 9/11 events further exacerbated this declining trend.
42. Eta is an armed Basque nationalist and separatist organisation in Spain. Forty-five British holidaymakers were injured in a bomb explosion at Reus Airport in July 1996. Shortly afterwards, the Eta group planted more bombs in hotels in the Spanish coastal resorts of Cambrils and Salou.
43. World Trade Organisation Press release, 24 March 2009.

2.8 Given that business air travel is closely related to economic growth and developments in international trade and investment, it is unsurprising that the recent synchronised global contraction in economic output and trade, along with the slump in consumer confidence and business investment, is having a significant impact on business air travel, particularly for premium-class cabins. The rapidly deteriorating economic and trading conditions are mirrored in marked falls in premium traffic flows within and across different world regions, particularly since September 2008, leading IATA, in March 2009, to revise its projection of net losses for the global aviation industry in 2009 to US$4.7bn – almost doubling its December 2008 forecast of a US$2.5bn loss – as network carriers are affected by the steeply falling demand from premium passengers and air cargo traffic.[44]

2.9 CAA Passenger Survey data show that the current economic crisis so far has had a greater impact on UK scheduled business than on leisure travel. Table 2.2 shows that, while leisure travel on all scheduled international flights from the four major London airports only grew marginally by 0.4% in 2008, international business travel fell by 6.3%. The survey data also reveal that the reduction in international scheduled traffic has intensified in the final quarter of 2008 with respective decline of 18% and 2% in business and leisure travellers.[45]

Table 2.2 Growth of scheduled business and leisure travellers at Heathrow, Gatwick, Stansted and Luton between 2007 and 2008

	Business	**Leisure**
Short haul	-8.0%	0.7%
Long haul	-3.0%	0.1%
Total international	**-6.3%**	**0.4%**

Source: CAA Passenger Survey, 2007 and 2008.

2.10 Business passengers have been particularly affected since the second half of 2008, with falls of 8% on long-haul routes and 22% on short-haul routes in the final quarter of 2008, following declines of 4% and 5% respectively in Q3 2008 as compared with a year earlier. Nevertheless, it is still too soon to be able to assess the full extent of the impact that the current economic crisis might have on business travel and how long it might last. A subsequent paper[46] will look at the effect of this further when more data become available.

Difference in growth rates at UK airports

2.11 Notwithstanding a number of adverse shocks, the robust passenger growth seen in the last decade or so has been driven predominantly by leisure passengers, particularly at regional airports, where the average annual growth rate of leisure traffic as a whole was more than three times that of business traffic, as shown by Table 2.3 below.[47] London City appears to be the only exception to this trend: business passengers grew marginally faster than leisure passengers over the period shown. Due to its proximity to London's financial centre and increasing congestion at the

44. IATA Press release, 24 March 2009.
45. Data by quarter is obtained by re-weighting the CAA annual survey to ensure that the weights exactly reflect the actual passengers flown in each quarter and at each airport.
46. Published in December 2010 and now forming Part 2 of this document.
47. For more information on trends at regional airports, see *CAP 775 Air Services at UK Regional Airports*, CAA (November 2007). www.caa.co.uk/cap775

other London airports, London City has managed to grow its position with financial sector employees taking business trips to domestic and international short-haul destinations.

2.12 However, growth rates vary significantly between London and regional airports and between airports within each region. Table 2.3 highlights the disparity in growth rates between business and leisure passengers for all domestic and international scheduled traffic (including connecting passengers) across the various UK airports. The average growth rate for all passengers on scheduled flights across all UK airports for the time period shown (1996–2007) was 6.5% per annum.

Table 2.3 Volume and growth of scheduled business and leisure passengers between 1996 and 2007

	Business (m)			Leisure (m)		
Airport	**1996**	**2007**	**Average growth p.a.**	**1996**	**2007**	**Average growth p.a.**
Heathrow	22.0	24.3	0.9%	33.6	43.5	2.4%
Gatwick	4.0	6.2	4.2%	10.3	20.5	6.4%
London City	0.4	1.9	13.8%	0.3	1.1	12.9%
Luton+Stansted	1.6	6.5	13.5%	3.2	25.6	20.8%
London total	*28.0*	*38.9*	*3.0%*	*47.4*	*90.7*	*6.1%*
Manchester	3.0	4.4	3.5%	3.7	9.5	9.0%
Birmingham	1.8	2.1	1.4%	1.5	4.6	10.7%
Glasgow	2.0	2.8	2.8%	1.7	4.1	8.3%
Edinburgh	2.0	3.9	6.4%	1.5	4.8	11.0%
Belfast	1.4	2.4	5.2%	1.8	4.3	8.4%
Other UK regions	5.1	8.3	4.5%	3.8	27.8	19.9%
Regional total	*15.3*	*23.8*	*4.1%*	*14.0*	*55.1*	*13.3%*
UK total	**43.3**	**62.7**	**3.4%**	**61.4**	**145.8**	**8.2%**

Source: CAA Passenger Survey, 1994–1996, 2005–2007.

Note: Data include domestic and international-to-international connectors.

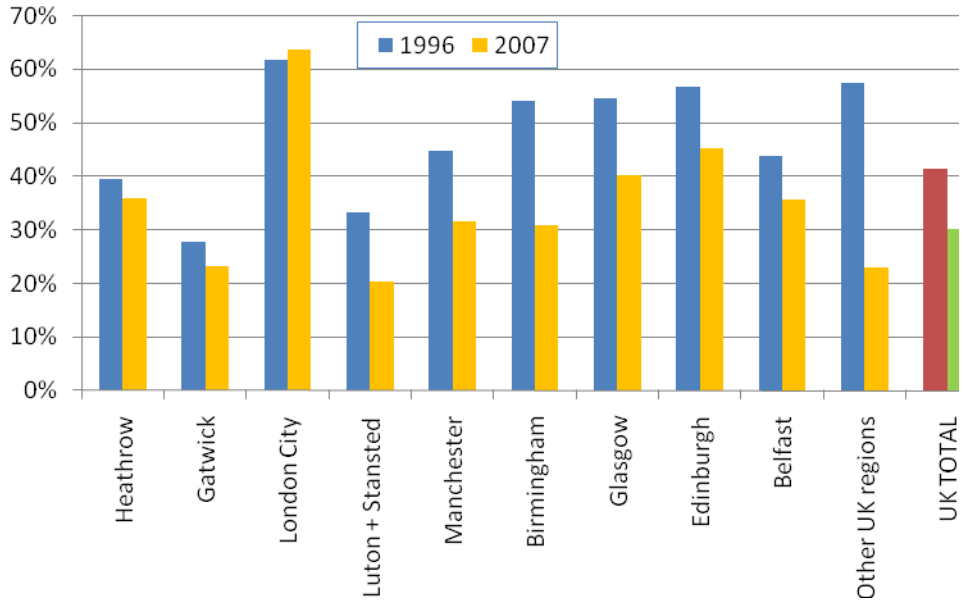
Belfast includes Belfast City and Belfast International airports.

Airports not surveyed in 1996 or 2007 have been scaled up from the nearest survey year or, where no survey data exists, modelled on data from similar surveyed airports.

2.13 As a consequence of greater growth rate in leisure relative to business traffic, the proportion of total UK scheduled passengers travelling for business purposes has declined from over 40% in 1996 to around 30% in 2007. The reduction in proportion of business passengers was most significant for the smaller regional airports (from 57% in 1996 to 23% in 2007), which saw rapid growth in services by NFCs. Although regional airports represented a smaller proportion of all traffic at UK airports in 1996 (29 million out of the total of 105 million), Figure 2.4 shows that they had a higher percentage of business passengers than Heathrow. This was due to a large proportion of traffic at regional airports in 1996 being domestic travel served by traditional full-service carriers (FSCs) with a large business component. The

subsequent development of NFCs and consequent increase in international services to leisure destinations at regional airports has changed this outlook considerably, with Heathrow having a higher percentage of business passengers than most regional airports (Edinburgh and Glasgow are notable exceptions) in 2007.

Figure 2.4 Proportion of scheduled passengers travelling for business purposes from various UK airports in 1996 and 2007



Source: CAA Passenger Survey, 1994–1996, 2005–2007.

Note: Data include domestic and international-to-international connectors.

Belfast includes Belfast City and International airports.

Airports not surveyed in 1996 and/or 2007 have been scaled up from the nearest survey year or, where no survey data exists, modelled on data from similar surveyed airports.

2.14 Table 2.4 indicates that the rapid expansion of NFCs, particularly in the regions, has had a greater impact on the share of total leisure passengers carried than on business travellers. Regional airports as a whole saw significant gains in scheduled leisure traffic (an increase of 41 million leisure passengers to 55 million between 1996 and 2007 which represents a 15 percentage point rise in market share to 38% in 2007), while their share of total UK business traffic increased only modestly from 35% to 38% over the same period.

Table 2.4 Airport percentage share of total UK business and leisure passengers in 1996 and 2007

	Business		Leisure	
Airport	**1996**	**2007**	**1996**	**2007**
Heathrow	51%	39%	55%	30%
Gatwick	9%	10%	17%	14%
London City	1%	3%	0%	1%
Luton+Stansted	4%	10%	5%	18%
London total	***65%***	***62%***	***77%***	***62%***
Manchester	7%	7%	6%	7%
Birmingham	4%	3%	2%	3%
Glasgow	5%	4%	3%	3%
Edinburgh	5%	6%	2%	3%
Belfast	3%	4%	3%	3%
Other UK regions	12%	13%	6%	19%
Regional total	***35%***	***38%***	***23%***	***38%***
UK total	100%	100%	100%	100%

Source: CAA Passenger Survey, 1994–1996, 2005–2007.

Note: Data include domestic and international-to-international connectors.

Belfast includes City and International airports.

Airports not surveyed in 1996 and/or 2007 have been scaled up from the nearest survey year or, where no survey data exists, modelled on data from similar surveyed airports.

2.15 While the growth in business traffic has been relatively evenly distributed between regional airports, there has been a more notable redistribution between London airports. Table 2.4 shows that Stansted, Luton and London City airports have gained market share as Heathrow's share of total UK business passengers fell from 51% in 1996 to 39% in 2007. This probably reflects a combination of factors: the capacity constraint at Heathrow, which has tended to displace domestic and shorter haul services in favour of longer haul flights (which tend on average to have a smaller proportion of business passengers on board);[48] the growing success of London City; and the ability of low-fare carriers at Luton and Stansted airports to attract business travellers.

48. See Figure 2.8.

2.16 The redistribution of business passengers among the London airports also appears to have occurred in a different way for the domestic, short-haul and long-haul sectors, as shown in Table 2.5.

Table 2.5 Volume of business passengers by sector at London airports in 1996 and 2007

	1996				2007			
Passengers (m)	**Domestic**	**Short haul**	**Long haul**	**Total**	**Domestic**	**Short haul**	**Long haul**	**Total**
Heathrow	3.8	12.1	6.1	22.0	2.8	12.5	9.0	24.3
Gatwick	0.9	1.8	1.3	3.9	1.6	3.3	1.3	6.2
Luton + Stansted	0.7	0.9	0.0	1.6	1.6	4.8	0.1	6.5
London City	0.01	0.4	0.0	0.4	0.6	1.3	0.0	1.9
London total	**5.3**	**15.2**	**7.4**	**27.9**	**6.6**	**21.9**	**10.4**	**38.9**

Source: CAA Passenger Survey, 1996 and 2007.

Note: 2007 London City figures have been scaled up from its 2006 latest survey year.
Traffic sector is defined by the final destination of a flight.

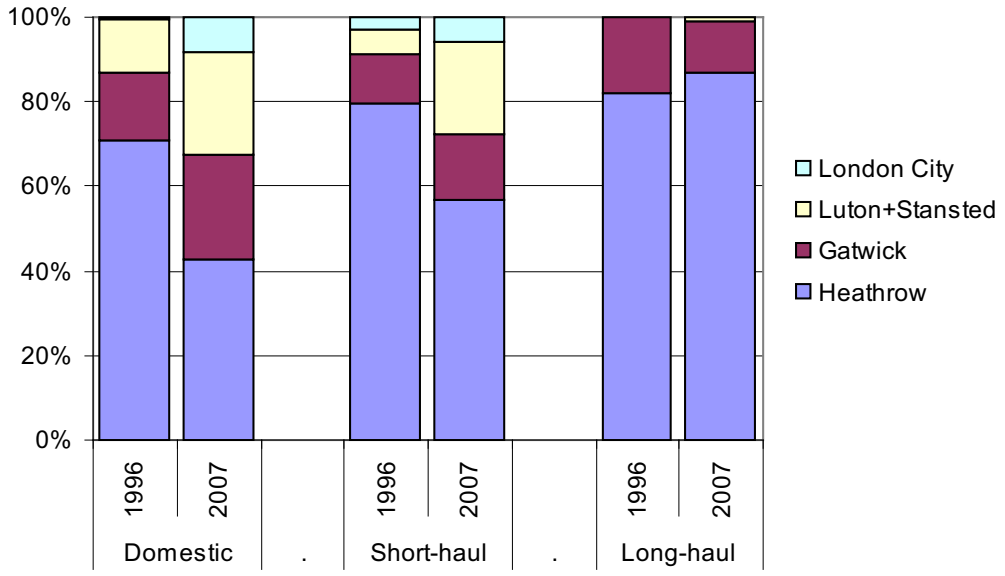
2.17 Although the proportion of business passengers at Heathrow (Figure 2.4) and its market share of total UK business traffic (Table 2.4) have decreased over time, Heathrow has attracted all the long-haul business growth (three million passengers) at London airports, increasing its market share of long-haul business traffic from 82% in 1996 to 87% in 2007. This in part was due to BA's network restructuring that has seen a substantial portion of its long-haul routes being transferred from Gatwick to Heathrow since early 2001.[49]

2.18 Faced with increasing competitive pressure from NFCs, some network airlines (such as BA) or alliances at Heathrow have either cut back their domestic and/or short-haul operations or replaced some of them with long-haul services to capture the higher-yield business passengers (compared with shorter haul business passengers) with greater frequency of services. However, this also attracts more leisure passengers onto these flights as the airlines seek to fill up the back cabin with discounted economy fares. As mentioned before, since long-haul flights have, on average, the lowest proportion of business passengers compared with domestic and short-haul flights, this shift towards longer haul services has altered the mix of business and leisure passengers at the airport over time, resulting in a lower concentration of business passengers than before.

2.19 This trend of Heathrow becoming a more long-haul dominated airport is reflected in its capturing almost all of the three million additional long-haul business passengers in and out of the London airports between 1996 and 2007 (Table 2.5), while its share of domestic and short-haul business passengers has decreased sharply as Luton, Stansted and London City have established an increasingly significant presence in these markets, as Figure 2.5 indicates.

49. The implementation of the EU-US 'Open Skies' agreement from March 2008 has led to further transfer of North Atlantic routes from Gatwick to Heathrow by BA and other carriers such as Continental, Delta and Northwest.

Figure 2.5 Percentage share of business passengers at London airports in 1996 and 2007



Source: CAA Passenger Survey, 1996 and 2007.

Note: 2007 London City figures have been scaled up from its 2006 latest survey year.

Passengers carried by carrier type

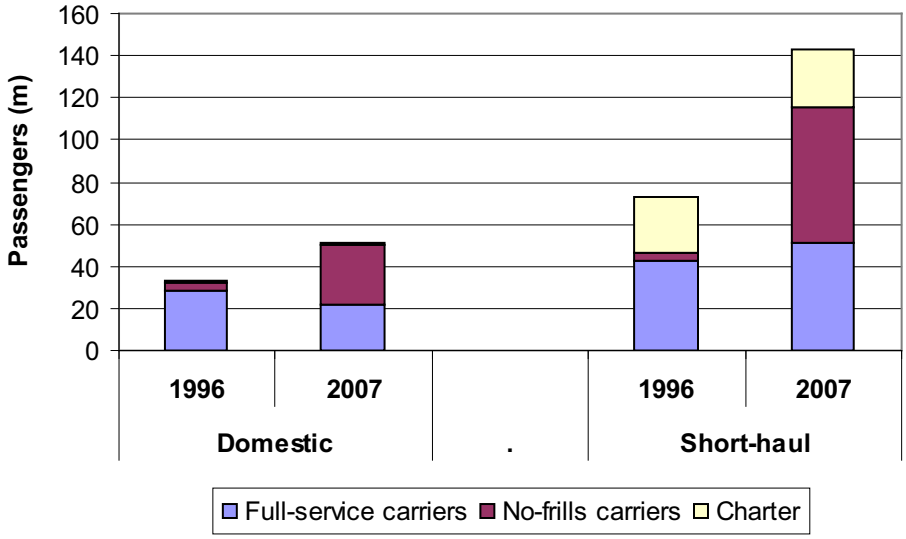
2.20 The emergence and development of NFCs has brought a number of innovations and increased competition to the airline industry, particularly in the domestic and short-haul markets. In 2007, NFCs carried about 57% of all passengers on domestic routes and 45% on short-haul routes. Furthermore, of those business passengers who travelled from the London airports in 2006,[50] more than 20% travelled with NFCs – a significant increase from less than 5% in 1996.

2.21 In contrast to traditional FSCs, the no-frills operating model tends to have a greater use of secondary and less congested airports that allow quick turnaround times (hence enabling higher aircraft utilisation), the provision of a single class of travel with high-density seating and a range of optional 'frills' available for purchase. Furthermore, NFCs generally have a more simplified fleet structure, a focus on point-to-point service to short-haul destinations, a simpler fare model built around one-way ticket pricing and the use of direct ticket sales that bypass the traditional reservations systems. All of these factors enable NFCs to offer a basic service at a low fare.[51]

2.22 The rapid growth of NFCs in the UK has not only altered the dynamics of competition between NFCs, FSCs and charter carriers, but also the level and mix of passengers across London and regional UK airports. Figure 2.6 shows that, by 2007, NFCs had become the dominant group in both the domestic and short-haul sectors, with growth in passenger numbers of almost eight and fifteen times respectively over 1996 levels. Consequently, NFCs' market shares of all passengers in the domestic and short-haul sectors have increased considerably from 10% and 6% in 1996 to around 57% and 45% respectively in 2007.

50. The latest year that all five London airports were surveyed by CAA was 2006.
51. *CAP 770 No-frills carriers: revolution or evolution?* CAA (November 2006). www.caa.co.uk/cap770

Figure 2.6 Domestic and short-haul passengers at UK airports by carrier type and by route type

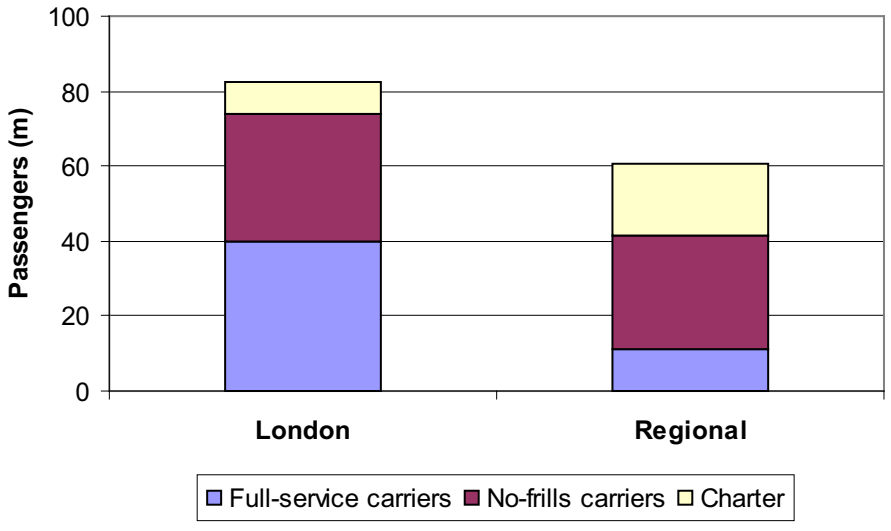


Source: CAA Airport Statistics.

Note: Domestic passengers are counted twice as the same passenger is registered at both the departure and arrival domestic airports.

2.23 Figure 2.7 sets out the proportion of traffic from London and regional airports by carrier type for the short-haul market in 2007. As well as showing the strong position of London airports for short-haul services, it also indicates that FSCs as a whole have a much stronger presence at London airports than at regional airports (and vice versa for charter airlines), while NFCs carry a more even volume of traffic across London and regional airports.

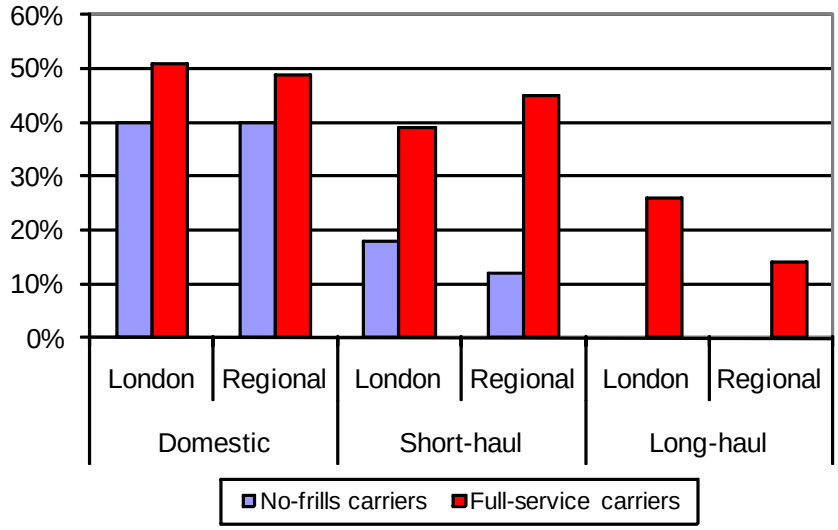
Figure 2.7 Volume of short-haul passenger traffic by carrier type from London and regional airports in 2007



Source: CAA Airport Statistics.

2.24 Historically, in terms of the proportion of passengers carried on a route, business passengers have the most significant presence in the domestic sector, followed by the short-haul and long-haul sectors. In terms of the proportion of business passengers carried by airline, Figure 2.8 shows that there is only a relatively small divergence between NFCs and FSCs on domestic routes with 40% to 50% of the traffic being business. However, there is a more significant difference on short-haul routes where 40% of passengers travelling on FSCs were on business compared with around 18% and 12% on NFCs at London and regional airports respectively. This, in part, may be due to a wider use of 'non-primary' airports by NFCs to predominantly leisure destinations, although level of frequency and timing of the flights would also have significant impact on business travel demand (see paragraphs 3.20 to 3.23 for further discussion of different types of airport pairs and distribution of business passengers on short-haul international routes served by BA, easyJet and Ryanair from London airports).

Figure 2.8 Proportion of business passengers by carrier type and by sector in 2007



Source: CAA Passenger Survey, 2005–2007.

Note: Figure includes only airports surveyed by the CAA. Airports not surveyed in 2007 have been scaled up from the nearest survey year.

2.25 The next chapter looks in more detail at where business passengers travelled from, which were the most popular destinations for business travel, and how these have changed between 1996 and 2007 at London and regional airports and by carrier.

Part 1 Chapter 3 Business passenger growth by route and by carrier

Chapter summary

- In terms of business passenger numbers, business travel to international short-haul destinations remained by far the most significant segment (50%) in 2007, followed by domestic business travel (33%).

Long haul

- Business passengers on long-haul services are mainly London (and predominantly Heathrow) based. The market is roughly split 50:50 between UK and foreign airlines, with BA and Virgin being the major players from London airports.
- The number of business passengers carried by sixth-freedom operators[52] such as Emirates, Qatar and Etihad Airways is growing, but still only represents a small percentage share (less than 10%) of total long-haul business traffic.

Short haul

- On international short-haul routes, the proportion of business passengers travelling from London airports (as opposed to travelling from the regions) has decreased from 80% in 1996 to 73% in 2007 and no-frills carriers now have a greater share of these passengers at London airports (from around 2% in 1996 to more than 18% in 2007).
- The most popular short-haul origins/destinations for business travel are Dublin and Amsterdam. There has also been strong growth in business traffic to and from secondary cities such as Barcelona, Cork, Nice and Prague, while the Channel Tunnel has had a noticeable effect on Paris and Brussels routes.

Domestic

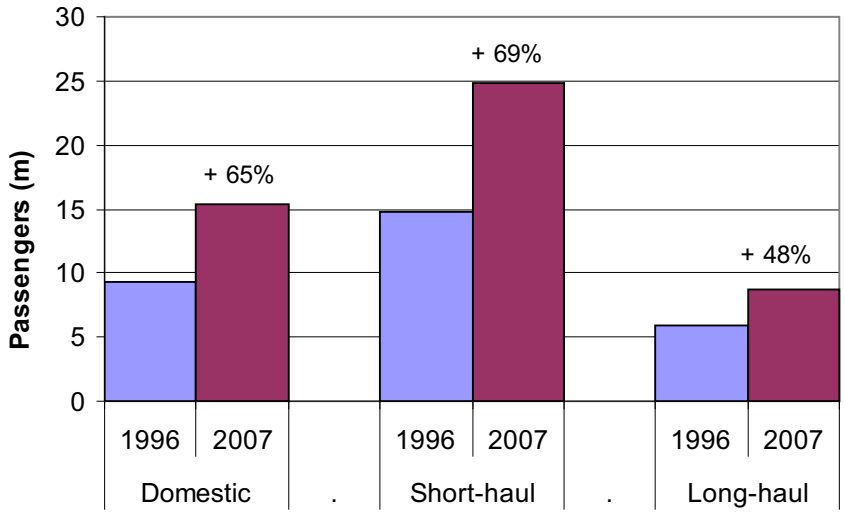
- Domestic business traffic to/from London declined between 2004 and 2007, although the number of links between London and the regions changed little.
- No-frills carriers have had a significant impact on domestic business travel in the regions as they expand their networks at regional airports.
- The share of total UK domestic business traffic represented by flights between regional airports has increased from 28% in 1996 to 36% in 2007.

3.1 The previous chapter considered all terminating and connecting business passengers[53] who use either London or regional airports – indicating the relative significance of business traffic for various airports and by carrier type. This chapter also considers terminating business passengers, who either start or end their journeys at a UK airport, and examines which origins and destinations have the most business travellers to and from the UK. The relative significance of different carriers serving long-haul, short-haul and domestic routes at London and UK regional airports is discussed, and the effect of competition from rail on traffic to/from Paris and Brussels is presented as a case study.

52. Sixth-freedom traffic is that carried between two foreign points via an intermediate point in the carrier's home country.
53. Connecting passengers are those passengers at an airport whose sole purpose is to transfer from one flight to another, within 24 hours of arrival at the airport.

3.2 While domestic travel has the highest proportion of business passengers per flight (as indicated in Figure 2.8), Figure 3.1 shows that, in terms of passenger numbers, travel to international short-haul destinations remains by far the most significant segment of business travel, accounting for almost 50% of the total UK origin/destination (O/D) business traffic in 2007 and demonstrating a growth of almost 70% since 1996.

Figure 3.1 Volume and percentage growth of terminating business passengers by origin/destination



Source: CAA Passenger Survey, 1994–1996, 2005–2007.

Note: Data exclude international-to-international connectors. Domestic passengers are counted twice as the same passenger is registered at both the departure and arrival domestic airports.

Figure includes only airports surveyed by the CAA. Airports not surveyed in 1996 and/or 2007 have been scaled up from the nearest survey year.

3.3 Drilling down from overall sector-level traffic, Table 3.1, Table 3.2, Table 3.3 and Table 3.6 list the top business destinations by country and by sector[54] in 2007 and their respective growth in business passenger numbers from the 1996 level.

3.4 Table 3.1 shows the 25 origin and destination countries with the largest volume of business travellers who either originated or ended their journeys within the UK in 2007, and their respective percentage growth from 1996 to 2007. The list shows that business destinations are dominated by North American and European countries, which are also most significant in terms of volume of trade with the UK. While the CAA survey data suggest that these 25 countries represent around 87% of the UK's total origin and destination international business traffic, Table 3.1 indicates that they also account for about 82% of UK's total trade in 2007/08 according to ONS data.[55]

54. Traffic sector is defined by the final destination of a flight.
55. The extent of this relationship is further explored in Part 2 of this study.

Table 3.1 Top 25 origin/destination countries for UK business travel, 2007

Country	Business passengers in 2007 (m)	% of total international passengers	Business passenger growth over 1996	Share of total UK trade
Germany	4.0	11.9%	45%	11.8%
United States	3.7	11.1%	36%	13.9%
Irish Republic	3.1	9.4%	128%	3.8%
Netherlands	2.3	7.0%	58%	6.7%
France	2.2	6.6%	17%	7.8%
Spain	2.0	6.1%	176%	4.8%
Italy	1.9	5.7%	91%	4.2%
Switzerland	1.4	4.3%	56%	2.2%
Denmark	0.8	2.5%	79%	1.2%
Belgium	0.8	2.5%	-6%	4.5%
Sweden	0.8	2.5%	43%	1.9%
Norway	0.8	2.4%	99%	2.7%
Poland	0.6	1.8%	292%	1.0%
India	0.5	1.5%	151%	1.3%
Portugal	0.4	1.2%	67%	0.7%
Czech Republic	0.4	1.2%	188%	0.7%
Canada	0.4	1.2%	48%	1.7%
Austria	0.4	1.2%	51%	0.7%
United Arab Emirates	0.4	1.1%	155%	0.6%
Greece	0.4	1.1%	143%	0.3%
Russia	0.3	1.0%	46%	1.1%
Japan	0.3	0.9%	15%	2.5%
Hungary	0.3	0.9%	106%	0.6%
China	0.3	0.9%	521%	3.4%
Hong Kong	0.3	0.9%	29%	1.6%
Total international	**33.3**	**100%**	**61%**	**100%**

Source: CAA Passenger Survey, 1994–1996, 2005–2007; ONS Exports and Imports of Goods and Services by Country.

Note: Data exclude international-to-international connectors. Table includes only airports surveyed by the CAA. Airports not surveyed in 1996 and/or 2007 have been scaled up from the nearest survey year.

3.5 The largest growth in business passengers between 1996 and 2007 is seen for Spain, Poland, Czech Republic, and the emerging markets of United Arab Emirates, India and China, albeit growth for most of these countries was from a relatively low base in 1996. While Poland and the Czech Republic appear to have increased their UK business traffic generally since joining the European Union, much of the increase in business passengers in the Spanish market has been driven by traffic to and from Barcelona, Malaga and Alicante which have benefited from the growth of NFCs at both London and regional airports.

3.6 In contrast, France and Belgium are the only European countries that exhibit either fairly low or negative growth in business passengers over the period. A further disaggregated analysis of these countries reveals sharp reductions in business travel between UK and Paris/Brussels between 1996 and 2007, suggesting strong competition from cross-channel rail services on these routes (see Table 3.3 and the case study below on modal competition).

Long-haul

3.7 Table 3.2 sets out the top 20 long-haul city destinations for UK O/D business passengers in 2007. It shows that long-haul business travel was still very much dominated by North America destinations (constituting more than 40% of total UK long-haul business passengers), particularly to/from New York City.

Table 3.2 Top 20 long-haul origin/destination cities for UK business travel, 2007

City	Business passengers in 2007 (m)	% of total long-haul passengers	Business passenger growth over 1996
New York (JFK)	0.72	8.2%	36%
Newark	0.28	3.3%	71%
Hong Kong	0.28	3.2%	29%
Dubai	0.27	3.2%	149%
Boston	0.25	2.9%	41%
Tokyo	0.23	2.7%	16%
Washington	0.23	2.6%	41%
San Francisco	0.20	2.4%	23%
Chicago	0.20	2.3%	34%
Singapore	0.20	2.3%	50%
Mumbai	0.18	2.0%	125%
Houston	0.16	1.9%	139%
Toronto	0.15	1.8%	50%
Tel Aviv	0.15	1.8%	59%
Los Angeles	0.15	1.7%	6%
Shanghai	0.14	1.6%	2752%
Johannesburg	0.14	1.6%	11%
Delhi	0.12	1.4%	55%
Lagos	0.11	1.3%	68%
Philadelphia	0.11	1.2%	32%
Total long haul	**8.75**	**100%**	**48%**

Source: CAA Passenger Survey, 1994–1996, 2005–2007.

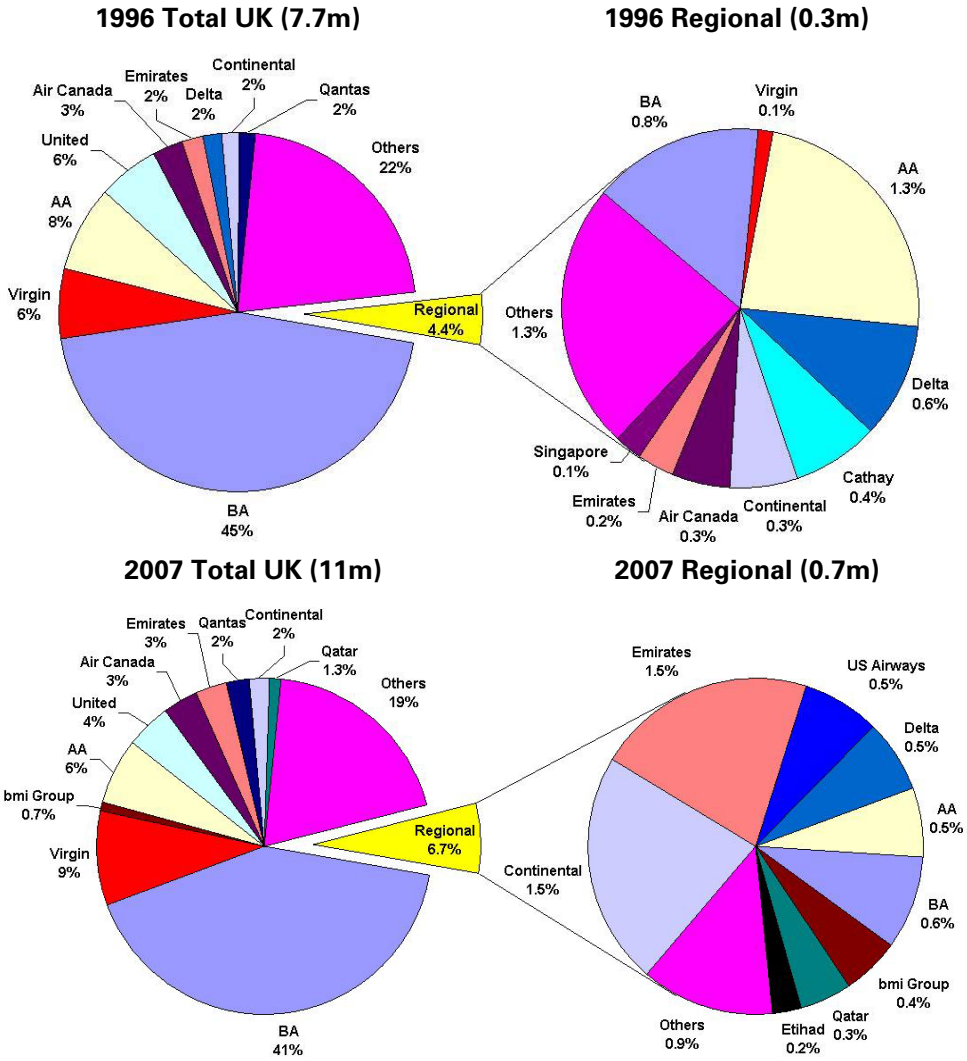
Note: Data exclude international-to-international connectors. Table includes only airports surveyed by the CAA. Airports not surveyed in 1996 and/or 2007 have been scaled up from the nearest survey year.

3.8 Restrictions on airlines operating UK–US routes were relaxed following the advent of the EU–US Open Skies agreement in March 2008, leading to more frequency of services and reported fare reductions. The initial impact of the liberalised transatlantic market was reflected in a net increase of 9% and 7% in the number of scheduled flights and seats respectively on UK–US routes between the last month of the Winter 2007/08 season and the first month of the Summer 2008 season. However, Table 3.2 also shows that the fastest growth of business passengers was to/from cities in emerging markets such as China, India and the Middle East. In particular, routes between the UK and Shanghai, Beijing, Mumbai, Bangalore, Chennai, Dubai, Abu Dhabi and Doha all experienced rapid expansion between 1996 and 2007, albeit from a relatively low base in 1996.

3.9 Figure 3.2 shows how airlines' shares of business passengers on long-haul flights out of London and the regions changed between 1996 and 2007.[56] It is clear that the majority of UK long-haul business travel remained London (and mainly Heathrow) based.

3.10 While the proportion of UK scheduled long-haul flights represented by services to/from regional airports had doubled from 7% in 1996 to around 14% in 2007 according to CAA Airport Statistics, Figure 3.2 shows that regional airports' share of UK long-haul business passengers, predominantly carried by non-UK airlines, had increased only moderately from 4.4% to 6.7% over the same period. This is because scheduled long-haul services out of the regions are more leisure dominated compared with Heathrow.

Figure 3.2 Share of business passengers on long-haul scheduled flights by carrier at London and regional airports



Source: CAA Passenger Survey, 1994–1996, 2005–2007.

Note: Data include international-to-international connectors. BA figures include all of its franchisees. bmi Group includes bmi Regional and bmibaby. Figures for Flybe in 2007 include passengers carried by BA Connect. Figures include only airports surveyed by the CAA. Airports not surveyed in 1996 and/or 2007 have been scaled up from the nearest survey year.

56. Airlines' shares of business passengers hereafter in this chapter should be treated with caution as airports not surveyed in 1996 or 2007 have been scaled up from their nearest survey years. As some of the routes served by individual airlines may have come in and out of operation at an airport between its survey year and the target year, this must be taken into account when interpreting the results.

3.11 The proportion of business passengers on long-haul flights carried by UK airlines (slightly above 50% in 2007) remained relatively unchanged between 1996 and 2007; BA (41% in 2007) remained the most significant carrier in and out of the London airports in the UK long-haul market, as shown in Figure 3.2.

3.12 However, the combined London market share of the American airlines[57] fell from about 18% in 1996 to 15% in 2007, amid rapid expansion by some Middle East sixth-freedom carriers such as Emirates, Qatar and Etihad Airways at both London and regional airports. The combined share of total UK long-haul business passengers carried by these Middle East sixth-freedom carriers rose from 2% in 1996 to more than 7% in 2007. Emirates and Continental are the most significant carriers in the regions, each carrying 1.5% of total long-haul business passengers in 2007.

Short-haul

3.13 A high proportion of UK short-haul origin/destination business traffic is to and from the main financial centres or capital cities of Europe, as illustrated in Table 3.3. While Dublin and Amsterdam are the top two destinations for short-haul business travel, strong growth to secondary cities such as Barcelona, Cork, Nice and Prague is observable.

Table 3.3 Top 20 short-haul origin/destination cities for UK business travel, 2007

City	Business passengers in 2007 (m)	% of total short-haul passengers	Business passenger growth over 1996
Dublin	2.4	9.6%	106%
Amsterdam	2.0	8.1%	69%
Paris	1.2	4.8%	-11%
Frankfurt	1.0	4.0%	22%
Brussels	0.7	3.0%	-9%
Copenhagen	0.7	2.7%	89%
Milan	0.6	1.3%	39%
Geneva	0.6	2.5%	75%
Dusseldorf	0.6	2.4%	23%
Zurich	0.6	2.4%	46%
Barcelona	0.6	2.4%	225%
Munich	0.6	2.3%	43%
Madrid	0.5	2.2%	79%
Stockholm	0.5	2.1%	49%
Cork	0.4	1.7%	271%
Oslo	0.4	1.5%	66%
Berlin	0.4	1.5%	154%
Nice	0.3	1.4%	129%
Hamburg	0.3	1.3%	32%
Prague	0.3	1.3%	143%
Total short haul	**24.9**	**100%**	**69%**

Source: CAA Passenger Survey, 1994–1996, 2005–2007.

Note: Data exclude international-to-international connectors. Table includes only airports surveyed by the CAA. Airports not surveyed in 1996 and/or 2007 have been scaled up from the nearest survey year.

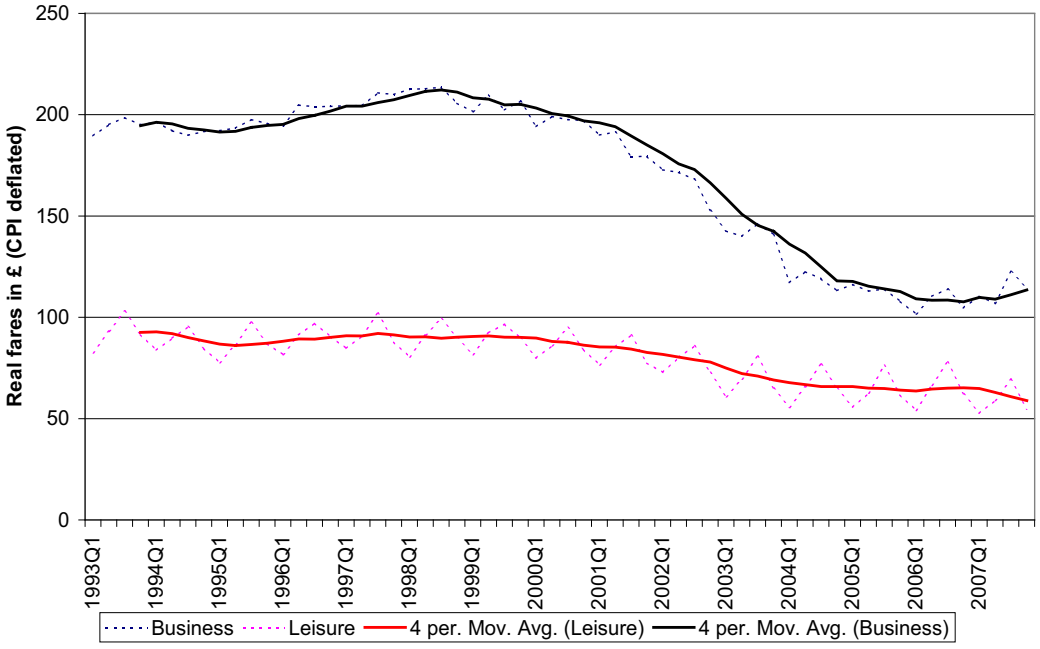
57. The American airlines operating from London are American, United, Continental, Delta, Northwest and US Airways.

3.14 These routes have benefited from increased flight frequency from both London and regional airports following the growth of NFCs. The fall in business passengers to and from Paris and Brussels is most likely due to a combination of the impact of Eurostar (see case study below) and the demise of the Belgian flag-carrier Sabena which carried significant numbers of connecting passengers via its hub at Brussels Airport.

3.15 The impact of NFCs on short-haul travel has been widely documented, especially their success in drawing passengers from traditional full service and charter carriers, increasing the range of routes offered from the UK (particularly from regional airports), and providing lower and/or more flexible fare options.[58] Growth in short-haul international passenger numbers between 1996 and 2007 was greater for leisure traffic, which increased by about 250%, than for business traffic, which only grew by around 70% (Table 3.3) – a growth not much higher than that of long-haul O/D business travel (48%) as shown in Table 3.2 above.

3.16 Short-haul business traffic has been growing more slowly than short-haul leisure traffic, despite the larger absolute and proportionate decline in average real UK–EU fares paid by business passengers compared with leisure since the late 1990s, as illustrated in Figure 3.3. The decline in the average real business fares over time reflects both a continuing trend of 'trading down' to economy class by some short-haul business passengers and an absolute reduction in fares available for a business trip. The data also seem to suggest that business passengers may be less price sensitive than leisure travellers and demand may be driven more by volume of trade and/or level of economic activity than by price (see paragraph 3.4). The effect of price on business travel and other potential demand drivers are further examined in Part 2 of this study.

Figure 3.3 Average one-way fares paid by UK passengers (UK–EU25) in 2005 prices

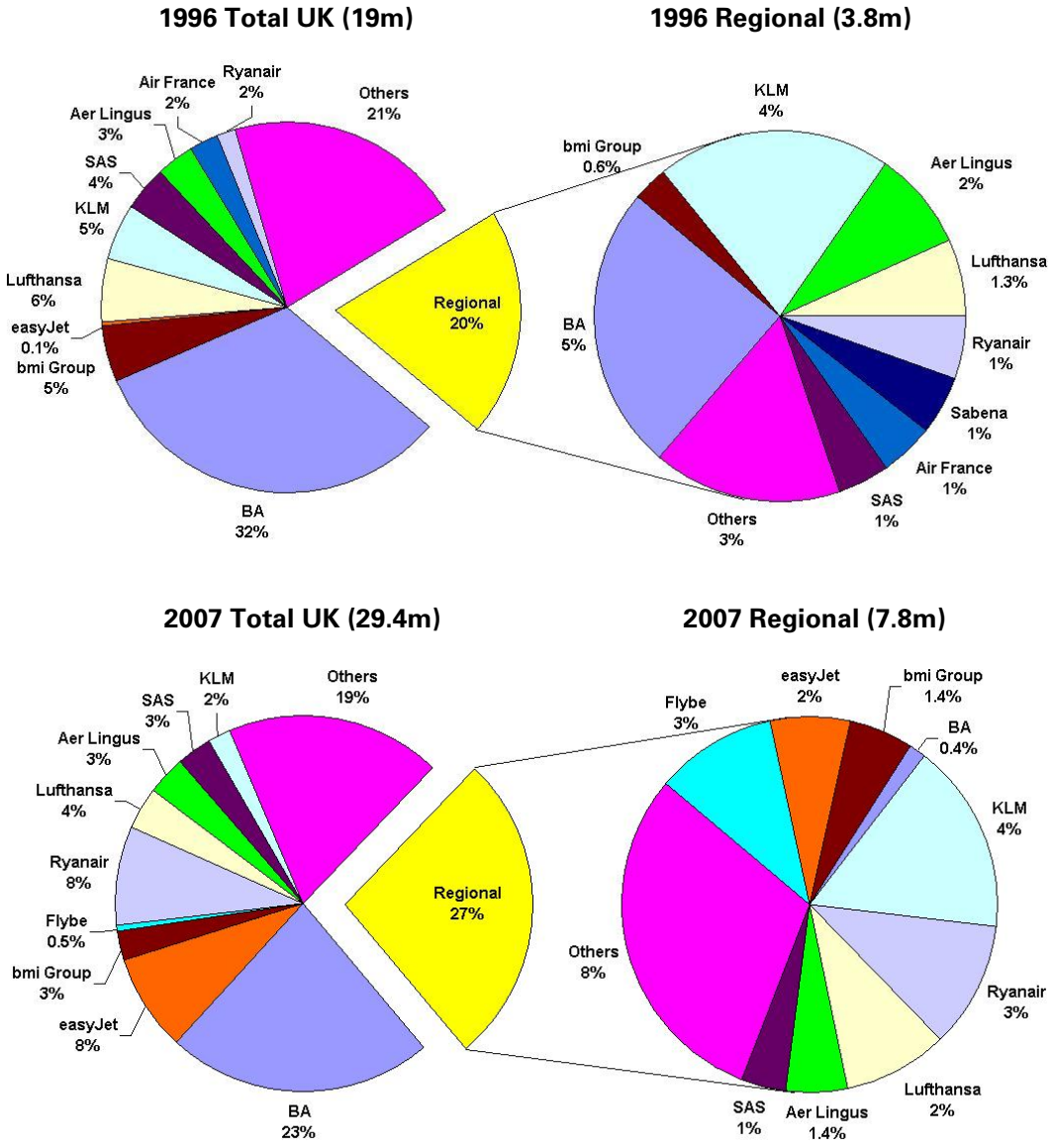


Source: International Passenger Survey, ONS.

58. See, for example, *CAP 770 No-frills carriers: revolution or evolution?*, CAA (November 2006). www.caa.co.uk/cap770

3.17 Within the business segment, Figure 3.4 shows that NFCs have taken substantial market shares from the traditional full-service legacy carriers in the international short-haul business market, especially from the London airports.

Figure 3.4 Share of business passengers on short-haul scheduled flights by carrier at London and regional airports



Source: CAA Passenger Survey, 1994–1996, 2005–2007.

Note: Data include international-to-international connectors. BA figures include all of its franchisees. bmi Group includes bmi Regional and bmibaby. Figures for Flybe in 2007 include passengers carried by BA Connect. Figures include only airports surveyed by the CAA. Airports not surveyed in 1996 and/or 2007 have been scaled up from the nearest survey year.

3.18 Figure 3.4 shows that:

- The London airports' share of the short-haul business market has decreased from 80% in 1996 to 73% in 2007.
- As in the long-haul sector, short-haul business travel from the regions shows a significant presence of non-UK airlines, representing almost 20 percentage points of the 27% regional share in 2007.
- NFCs have increased their share of business passengers, particularly at the London airports; the combined share of Ryanair and easyJet at the London airports increased markedly from 2% to 17% between 1996 and 2007 while that of BA and bmi fell from 37% to 26%.

3.19 Although the proportion of short-haul passengers on NFCs who are travelling for business purposes is still relatively low (on average 16% across London and regional airports) compared with FSCs (40%), there is a considerable and growing volume of business passengers carried by NFCs, as shown in Figure 3.4 above. Previous CAA analysis[59] suggested that the range of destinations served (particularly from the regions), the frequency of services and the lower prices offered by NFCs have particularly benefited business passengers from smaller firms and those in the regions, as suggested by the increase in the proportion of business travellers from lower income groups over the past decade or so.

3.20 However, although easyJet and Ryanair have similar market shares of business passengers at both London and regional airports, they differ significantly in terms of which cities/airports they fly from and to and in their relative appeal to business travellers. For example, although the number of international routes served and passengers carried by Ryanair at London airports in 2007 were, respectively, 24% and 35% higher than easyJet, a much larger proportion of Ryanair's London route network is linked to 'non-primary' airports[60] or leisure destinations than easyJet's. Table 3.4 shows that 93% of the routes served by Ryanair from London are to a 'non-primary' airport, whereas more than one-third of easyJet's short-haul routes (or 46% of its total short-haul passengers carried) from London in 2007 were linked to a 'primary' airport. This contrasts with BA where half of its short-haul international routes (or three quarters of its total short-haul passengers carried) were linked to a 'primary' airport at one end or the other.

59. *CAP 770 No-frills carriers: revolution or evolution?*, CAA (November 2006). www.caa.co.uk/cap770

60. For the purpose of this study, 'primary' airports are defined as the 40 airports with the highest passenger throughputs within each of the 40 largest urban zones (LUZ) as classified by Eurostat (Urban Audit), based on resident population in 2004 in the EU-27 countries plus Turkey, Norway and Switzerland. The largest airport in each of the capital cities of these EU-27 plus three countries is also considered as 'primary' airport (if it is not in the group of the 40 largest LUZ). Thus, Heathrow is considered as the 'primary' airport within the London area while Gatwick, Stansted, Luton and London City are classified as 'non-primary' airports (see Annex 1.B for a list of 'primary' airports considered in this study).

Table 3.4 Type of airport pairs served by BA, easyJet and Ryanair on short-haul international routes from London in 2007

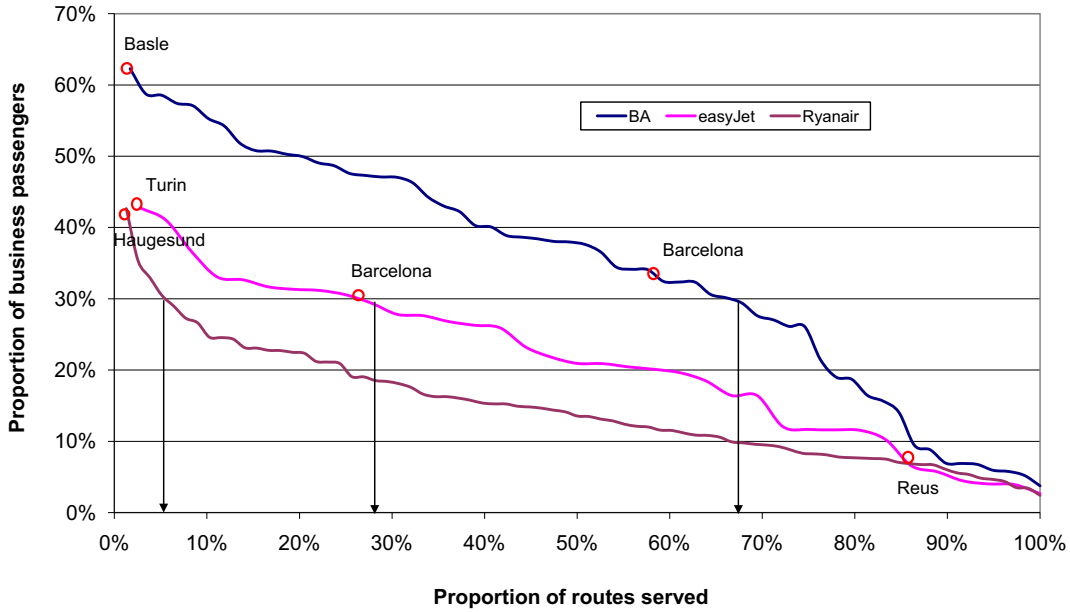
Airport pair	Route share by airport pair			Passenger share by airport pair		
	BA	easyJet	Ryanair	BA	easyJet	Ryanair
Primary / Primary	23%	0%	0%	49%	0%	0%
Primary / Non-Primary	29%	36%	7%	27%	46%	18%
Non-Primary / Non-Primary	48%	64%	93%	24%	54%	82%
Airport pairs served	123	91	113	--	--	--
Passengers carried (m)	--	--	--	19.2	12.3	16.6

Source: CAA Airport Statistics.

Note: Only Heathrow is considered as the 'primary' airport in the London area.
BA figures include GB Airways, BA Cityflyer, BMed and Loganair. easyJet figures include easyJet Switzerland.
Routes with fewer than 10 flights in 2007 have been excluded from the data.

3.21 Figure 3.5 shows the distribution of business passengers on short-haul routes served by BA, Ryanair and easyJet from London airports (excluding London City) in 2007. Of the 100 or so routes served by Ryanair, only about 5% of the routes carried 30% or more business passengers on average. By comparison, 27% of the short-haul routes served by easyJet from London and 67% by BA had 30% or more business passengers on board.

Figure 3.5 Distribution of business passengers on short-haul routes from London airports (except London City) in 2007



Source: CAA Passenger Survey, 2007.

Note: London City is not included as it was not sampled by the CAA in 2007. Routes with fewer than 50 interview records have been excluded from the data to minimize sampling errors.

3.22 BA has a larger proportion of routes that link to a primary airport and generally carries a higher proportion of business passengers than NFCs. However, on routes where NFCs offer a competitive frequency, NFCs are capable of attracting a similar (and in some cases higher) proportion of business passengers than FSCs. The London–Barcelona route is a case in point: BA, Iberia and easyJet fly to Barcelona from London while Ryanair serves the neighbouring airports at Girona and Reus – Ryanair markets these as Barcelona (Girona) and Barcelona (Reus) although both are about 50 miles from the city centre of Barcelona. Table 3.5 shows that in 2007 easyJet offered a frequency of service which was competitive with BA and Iberia. While easyJet's Luton service carried a similar proportion of business passengers to Iberia's Heathrow flights, its Gatwick service attracted a higher proportion of business passengers than both BA's Gatwick and Heathrow services.

Table 3.5 Proportion of business passengers by carrier and by airport in 2007

Airline	London airport	Airport / daily frequency	% business
BA	Gatwick	Barcelona (3)	30%
	Heathrow	Barcelona (5)	36%
Iberia	Heathrow	Barcelona (4)	28%
easyJet	Gatwick	Barcelona (4)	38%
	Luton	Barcelona (5)	28%
	Stansted	Barcelona (3)	20%
Ryanair	Luton	Girona (2)	2%
		Reus (1)	6%
	Stansted	Girona (4)	7%
		Reus (2)	8%

Source: CAA Passenger Survey, 2007, and Microsoft Mappoint.

Note: Daily frequency of return flights during weekdays in Summer 2007.

3.23 In contrast, Ryanair's services carried fewer than 10% business passengers in 2007. Ryanair had only one daily flight from Luton to Reus and two daily services from Stansted to Reus and from Luton to Girona in summer 2007. However, it offered four daily flights from Stansted to Girona, which suggests that frequency alone is insufficient to attract business passengers – they are also likely to prefer primary airports nearer to city centres. The timings of the outbound and return flights are also likely to be a significant factor for business travel.

3.24 As well as competition from other airlines, there may be significant competitive pressures from high-speed train services for short distance domestic and international travel. The section below examines how such inter-modal competition has developed on travel between the UK and Paris/Brussels.

Case Study: Modal competition from Eurostar on short-haul routes

Eurostar moved its London operations from Waterloo to the newly restored St Pancras International rail station on 14 November 2007 and started to use the dedicated high-speed line connecting central London to the Channel Tunnel. With this move, it became possible to reach Brussels and Paris from London in 1h 55m and 2h 15m respectively, representing a reduction in journey time of 20 minutes compared with Eurostar's Waterloo service.

The use of St Pancras station enabled Eurostar to offer connections to nine northern rail services that terminate at St Pancras or the neighbouring stations of Kings Cross and Euston, and it also began offering 'through fares' to the Continent, a single fare from any of 130 UK towns and cities to a Eurostar destination across the Channel.[1]

Figure 3.6 shows the extent of the rail network served by such 'through fares' to the Continent. Eurostar reported[2] large increases in travellers from UK regions after the first year at St Pancras International, with passenger numbers increasing by up to 150% from Derbyshire and more than 100% from the East Midlands, Yorkshire and the North East (albeit from a low base level). The slowest growth in Eurostar passengers was from Scotland: Edinburgh 38%, Glasgow 29% and Aberdeen 41%, where travelling by rail is disadvantaged by the relatively long journey time compared with travelling by air.

In 2007, 6.2 million passengers flew between Paris or Brussels and the UK, while 8.3 million passengers used Eurostar to cross the Channel. However, in 2008, only 5.7 million passengers flew on these routes, in contrast to Eurostar, which carried 9.1 million passengers (up 10.3% on 2007) despite a fire incident on board a freight shuttle on 11 September 2008 which caused significant service reductions and longer journey times.[3]

Analysis of CAA Airport Statistics shows that air passengers between all UK airports and Paris or Brussels declined by 6% between 2004 and 2007, while passengers travelling on Eurostar across the Channel increased by 15% over the same period. However, the impact of Eurostar on air travel to Paris/Brussels appears to differ significantly between London and regional airports, with some variation among the regional airports (Figure 3.7). Air passengers to Paris/Brussels from London and from regional airports that serve geographical areas with rail links to St Pancras, Kings Cross and Euston stations[4] were adversely affected by Eurostar competition (a decline of 17% from London and 6% from regional airports between 2004 and 2007). On the other hand, air passenger traffic to Paris/Brussels from other regional airports without effective rail links to London increased significantly (+33%). This suggests significant substitution from air to rail on travel to Paris/Brussels, especially for passengers originating from areas with effective rail links to St Pancras and its nearby rail stations.

This trend continued in 2008 – passenger numbers from London and from regional airports with effective rail links fell by 15% and 8% respectively compared with the same three quarters in 2007, whereas passenger numbers from the other regional airports increased by 11%. Figure 3.8 compares the passenger growth rates of Eurostar with air traffic to/from London and regional airports. It highlights the increasing modal shift on the Paris and Brussels routes, particularly after the move by Eurostar to St Pancras International station in late 2007.

1 *Eurostar offers through fares (including transfers on the London Underground) to the Continent with First Great Western, National Express East Anglia, First Capital Connect, Virgin Trains, National Express East Coast, East Midlands Trains, London Midland, Chiltern Railways and Hull Trains.*

2 *Eurostar press release, 12 November 2008.*

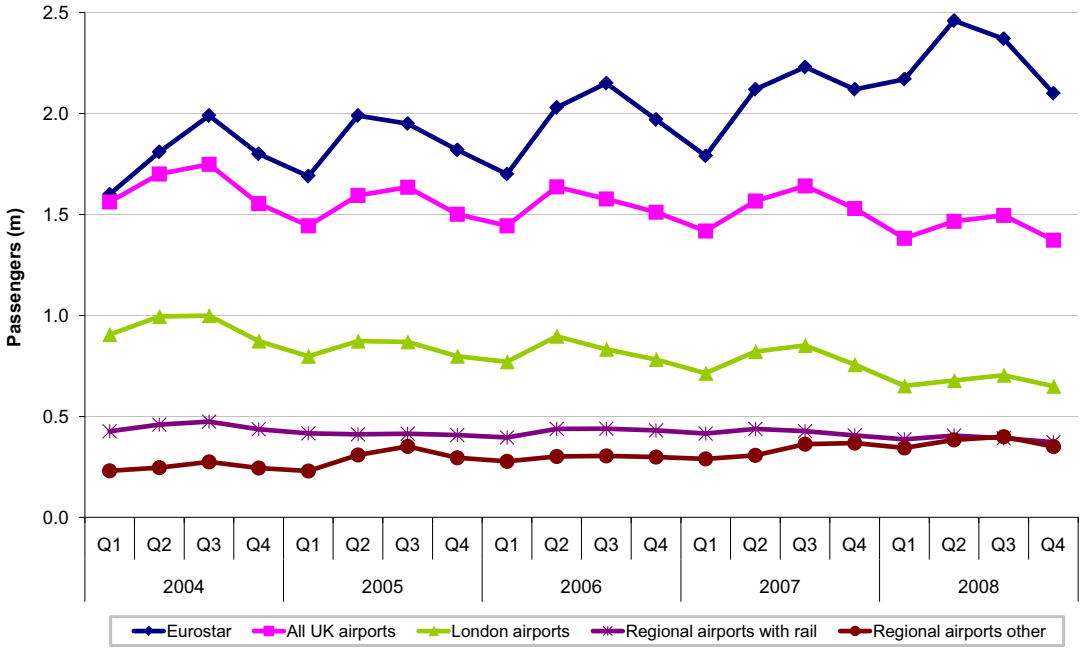
3 *Normal Eurostar services were restored on 23 February 2009 with further capacity added. There are now up to 19 trains per day from London to Paris and up to 10 per day to Brussels.*

4 *Airports that have rail links to St Pancras, Kings Cross and Euston stations are Birmingham, Cambridge, Coventry, East Midlands, Liverpool, Manchester and Norwich airports.*

Figure 3.6 Rail stations with through fares to the Continent

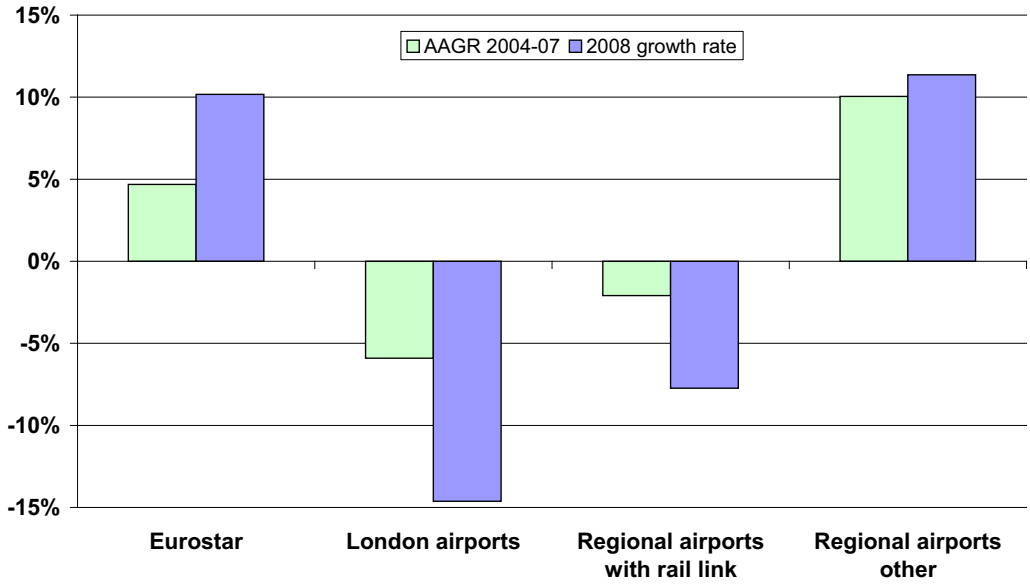
Source: Eurostar website.

Figure 3.7 Number of passengers between UK and Paris/Brussels by air and by Eurostar, 2004-2008



Source: CAA Airport Statistics and Eurostar.

Figure 3.8 Passenger growth between UK and Paris/Brussels by air and by Eurostar



Source: CAA Airport Statistics and Eurostar.

Note: AAGR = average annual growth rate.

Domestic

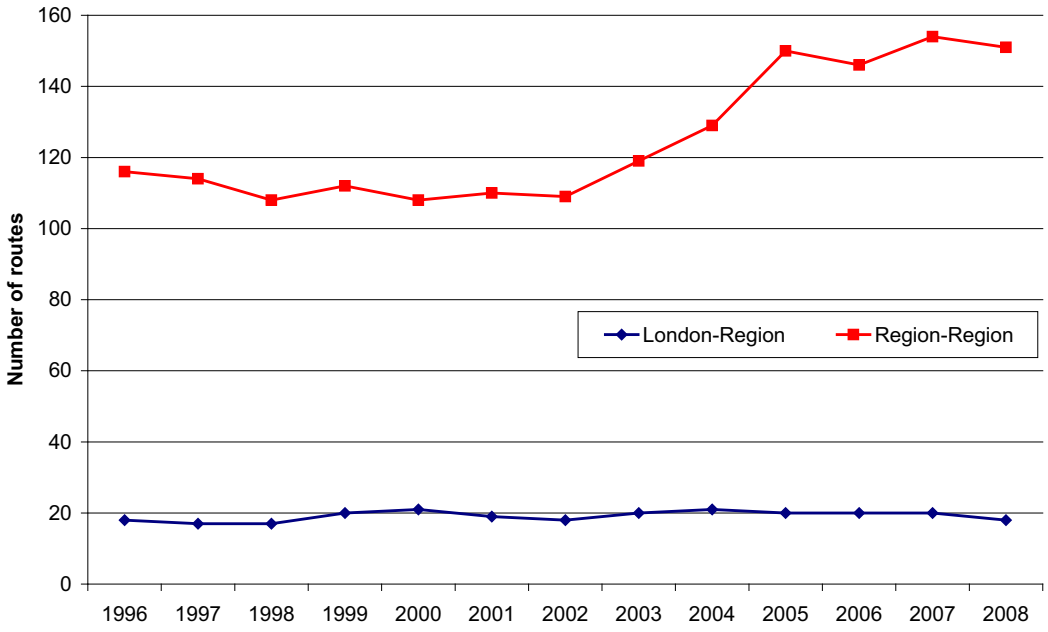
3.25 UK domestic traffic has been in decline since 2005 after steady growth averaging 5.2% per annum in the preceding decade. Consequently, domestic travel accounted for 21% of total UK traffic in 2007, compared with 24% in 1996.[61]

3.26 This recent reduction was largely driven by the decline of domestic traffic to/from London airports, especially Heathrow, where domestic traffic has fallen by an average of 6% per annum since 2004. However, traffic growth between UK regional airports also slowed to 4% in 2006 and -1% in 2007, following a period of strong growth averaging 12% per annum between 2000 and 2005.

3.27 A previous study by the CAA[62] suggested that contributing factors to this recent decline in domestic traffic could include: improved rail services; the deterrent effect of airport security restrictions and their contribution to increased journey time; fewer passengers to/from regional airports using Heathrow as a connecting point as alternative hub options outside the UK have developed; the increasing liberalisation of long-haul services and slots scarcity at Heathrow; and, to a lesser extent, the increases in Air Passenger Duty (although the declining traffic trend predates the February 2007 increase in Air Passenger Duty).

3.28 Although the number of links between London and UK regional airports has changed little in recent years, as shown in Figure 3.9, there has been a notable increase in links between UK regional airports since 2003.

Figure 3.9 Number of domestic routes by city pair, 1996–2008



Source: *CAA Airport Statistics.*

Note: *Routes are defined as services averaging at least five round trips per week. Data includes Channel Islands and Isle of Man.*

61. Domestic passengers are counted twice as the same passenger is registered at both the departure and arrival domestic airports.
62. *Recent trends in growth of UK air passenger demand*, CAA (January 2008). www.caa.co.uk/docs/589/erg_recent_trends_final_v2.pdf.

3.29 Domestic business travel by air within the UK is still dominated by London routes, although the London airports' market share of such traffic has diminished from 32% to 27% between 1996 and 2007, as shown in Table 3.6.[63] Manchester and Aberdeen as business destinations had well below average growth rates of domestic business travel, while there were significant increases at other regional airports, particularly Bristol and Southampton, where NFCs have established a base to cater for both leisure and business traffic.[64]

Table 3.6 Top 12 domestic destinations for business travel, 2007

City	Business passengers (m)	% of total domestic business passengers	% growth over 1996
London	4.2	27.1%	38%
Edinburgh	2.0	12.9%	74%
Glasgow	1.8	11.8%	64%
Manchester	1.0	6.3%	29%
Belfast Int'l	0.9	6.0%	79%
Belfast City	0.8	5.1%	100%
Birmingham	0.7	4.4%	79%
Aberdeen	0.6	3.7%	20%
Bristol	0.5	3.4%	417%
Newcastle	0.5	3.1%	75%
Southampton	0.4	2.6%	358%
East Midlands	0.3	2.0%	146%
Total domestic	**15.4**	**100%**	**65%**

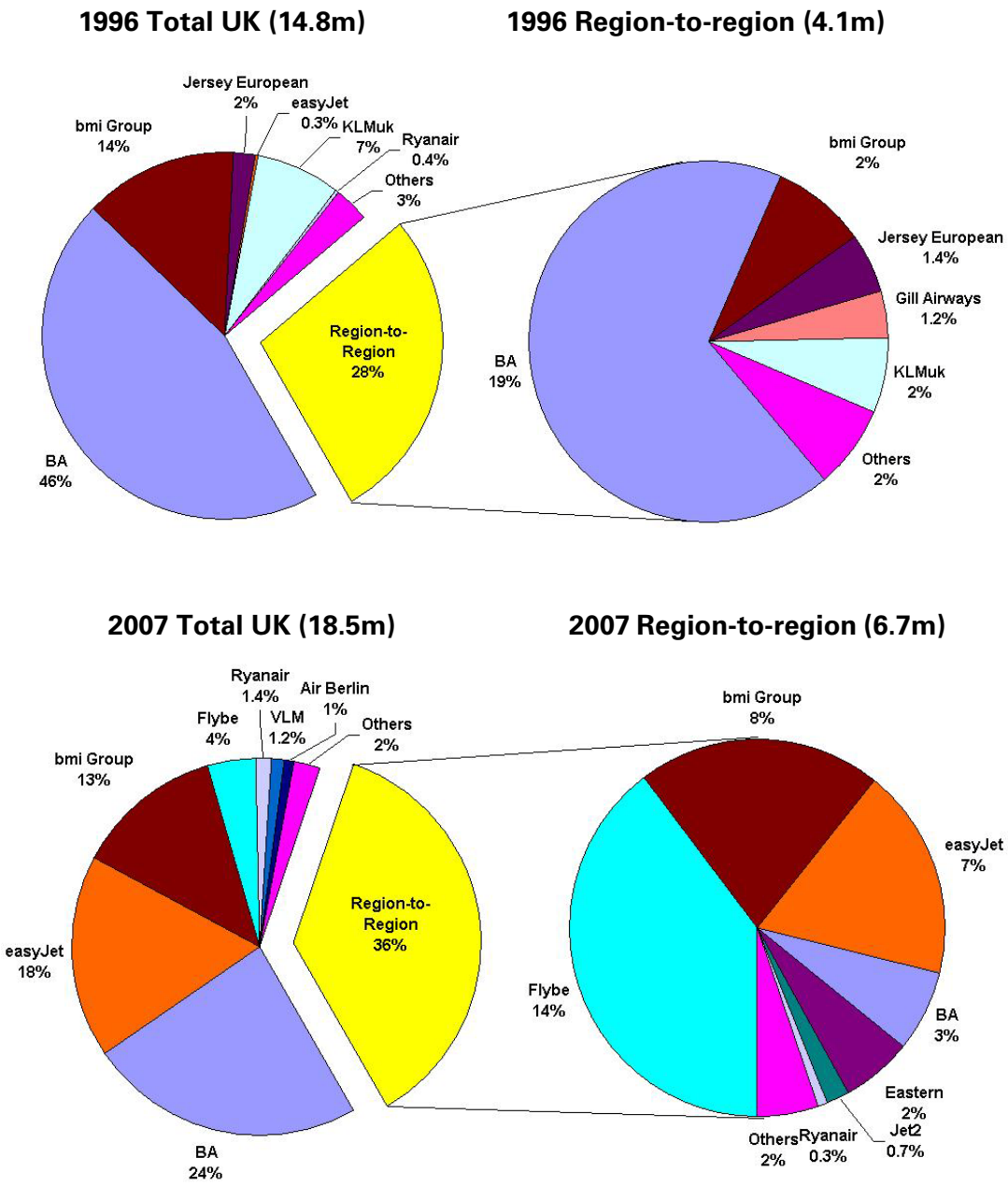
Source: CAA Passenger Survey, 1994–1996, 2005–2007.

Note: Data exclude international-to-international connectors. Table includes only airports surveyed by the CAA. Airports not surveyed in 1996 and/or 2007 have been scaled up from the nearest survey year.

3.30 In contrast to the long-haul and short-haul segments, several major UK airlines had significant shares in the domestic business market in 2007: BA, easyJet, bmi group and Flybe. Figure 3.10 shows the breakdown of domestic business traffic between London–Regional and Regional–Regional routes and by airline. It also shows that traffic between regional airports has increased from 28% of the UK total in 1996 to 36% in 2007, while BA's presence in the domestic market has been strongly challenged by the expansion of NFCs, especially on intra-regional routes, where BA has recently stopped offering services itself and through its franchisees.[65]

63. Domestic passengers are double counted as the same passenger is registered at both the departure and arrival domestic airports.
64. It is possible that some of this increased domestic business traffic has switched from road or rail travel.
65. BA's franchise agreement with the Scottish regional airline, Loganair, for connecting journeys within Scotland ended on 25 October 2008. Instead, Loganair began a franchise agreement with Flybe from the start of the 2008/09 Winter season.

Figure 3.10 Share of business passengers on domestic scheduled flights by carrier between London and regional airports



Source: CAA Passenger Survey, 1994–1996, 2005–2007.

Note: Data include international-to-international connectors. BA figures include all of its franchisees. bmi Group includes bmi Regional and bmibaby. Figures for Flybe in 2007 include passengers carried by BA Connect. Figure includes only airports surveyed by the CAA. Airports not surveyed in 1996 and/or 2007 have been scaled up from the nearest survey year.

3.31 Flybe (formerly known as Jersey European) intra-regional services have significantly increased their share of domestic business passengers from 1.4% in 1996 to 14% in 2007. Flybe became Europe's largest regional airline by acquiring BA Connect from BA in March 2007[66] and has had a franchise agreement with Loganair since October 2008.

3.32 Since 1996 the bmi Group has commenced long-haul services at London airports (see Figure 3.2 above), but its share of business passengers in the short-haul and domestic markets from London has fallen.[67] However, for domestic operations between regional airports, the bmi Group's market share of region-to-region business traffic has increased by more than five percentage points to 8% between 1996 and 2007.

66. For a more detailed study of Flybe's acquisition of BA Connect, see *CAP 775 Air services at UK regional airports*, CAA (November 2007). www.caa.co.uk/cap775

67. bmi recently announced the withdrawal of services from Heathrow to Leeds-Bradford and Durham Tees Valley as of 29 March 2009.

Part 1 Chapter 4 Socio-economic characteristics of and source of demand for business passengers

Chapter summary

Passenger characteristics and ticket type

- Business passengers have a similar median age to those travelling for leisure, but are much more 'clustered' in the 25 to 54 age bracket.
- The proportion of women business passengers has not changed much in the last 10 years; a larger proportion come from lower income groups than men.
- No-frills carriers (NFCs), which carry more than 20% of business passengers from London airports, carry a larger proportion of passengers from lower income groups than full-service carriers (FSCs).
- There has been a significant decline in the proportion of business passengers travelling in First or Business/Club cabins, especially in the short-haul market (from 40% in 1996 to less than 10% in 2007).

Purpose of business travel

- Attending internal meetings or meetings with external clients remained the main purposes of business travel between 2001 and 2007, representing around two-thirds of all business travel. There is also little difference in terms of trip purpose between those travelling on NFCs and FSCs over the same period.
- Around half (48%) of London City's business passengers in 2006 were from banking/finance-related industries.
- Heathrow's mix of business passengers' occupations in 2006 was not dissimilar to other large London airports - what might be seen as 'City' occupations did not predominate.
- Stansted had fewer business passengers from the 'City' occupations despite its relatively good transport links with the City of London (the 'Square Mile'), but attracted disproportionately more passengers from the health/public sectors, catering/retail/wholesale and construction industries.

Catchment area

- While Heathrow's catchment area in respect of short-haul business passengers has not changed much between 2000 and 2006, London City's catchment area has expanded significantly as the airport has grown in size and in the number of routes served. The majority of London City's increase in passenger shares appear to originate from areas in north-east and south-east London.

4.1 This chapter examines some of the socio-economic characteristics of business passengers and whether these have changed over time. It looks at elements such as carrier type, the proportion of business passengers travelling in different classes, the main purpose of their business trip and their profession.

4.2 The chapter concludes with an examination of the catchment area in respect of short-haul business passengers for Heathrow and London City – the two London airports with the highest proportion of business passengers.[68]

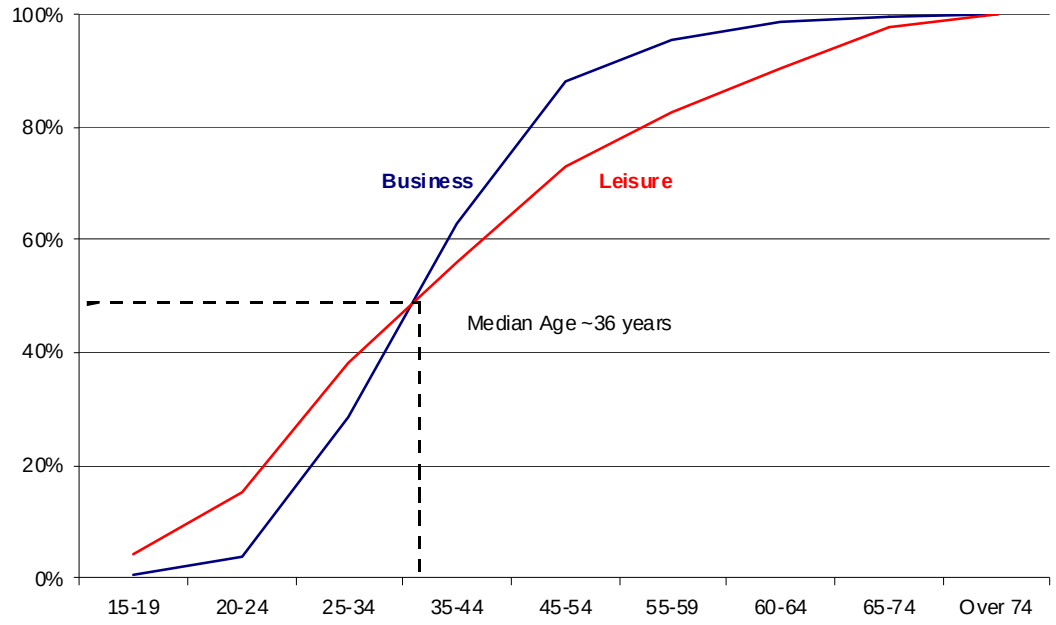
Business passenger characteristics

4.3 This section looks at some socio-economic characteristics of UK business passengers, the main purpose of their business trips and the industry group they fall into, as well as the proportion of these business passengers choosing to travel in business versus economy class.

Age distribution

4.4 Figure 4.1 shows that business passengers predominantly lied within a narrower age band than leisure passengers, with 31% belonging to the 35 to 44 age group and 84% in total falling into the wider 25 to 54 age bracket. This compares with leisure passengers, whose largest segment (22%) came from the younger 25 to 34 age group with only 58% in total falling into the wider 25 to 54 age bracket. However, both business and leisure passenger groups had a similar median age of around 36 years.

Figure 4.1 Age distribution by journey purpose in 2006



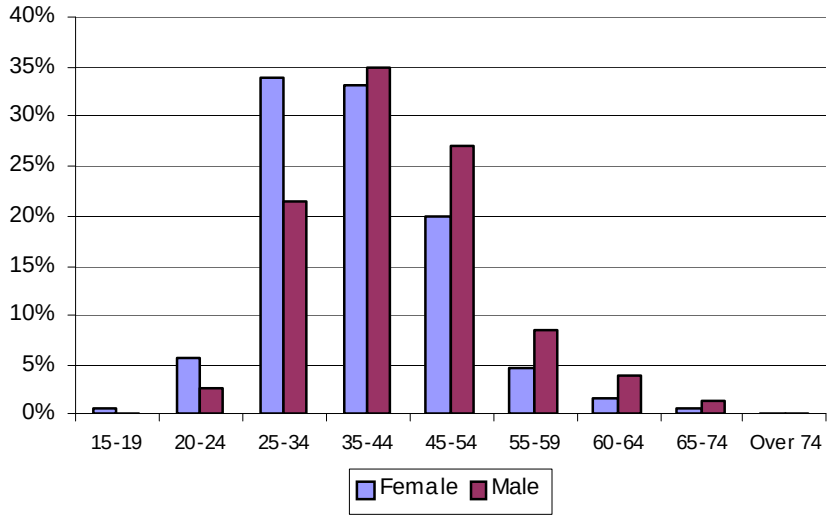
Source: CAA Passenger Survey, 2006.

Note: The 11 surveyed airports in 2006 were Belfast City, Belfast International, Birmingham, East Midlands, City of Derry, Gatwick, Heathrow, Luton, Manchester and Stansted.

4.5 When looked at by gender, there was a notable difference in the age distribution of business passengers. Figure 4.2 shows that, in 2006, more male business passengers belonged to the older age groups than female passengers. While almost 40% of male business passengers were aged between 45 and 64, only 26% of female business passengers fell within this older age band.

68. CAA Passenger Survey 2006 is used since London City, which has a high proportion of passengers travelling for business purposes, was not surveyed in 2007.

Figure 4.2 Age distribution of business passengers by gender in 2006



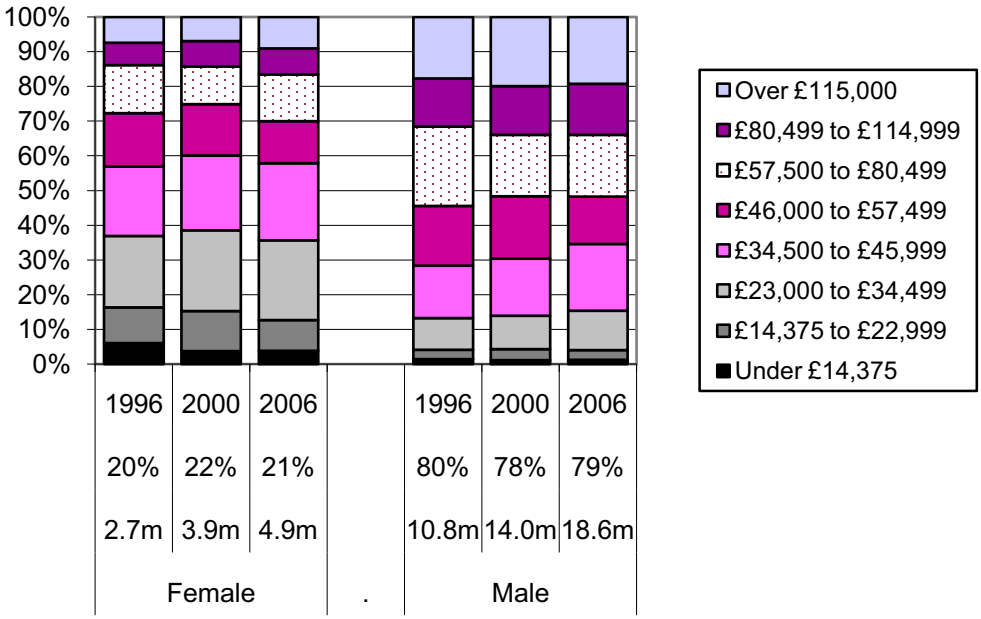
Source: CAA Passenger Survey, 2006.

Note: The 11 surveyed airports in 2006 were Belfast City, Belfast International, Birmingham, East Midlands, City of Derry, Gatwick, Heathrow, Luton, Manchester and Stansted.

Income distribution by gender

4.6 Figure 4.3 shows that around one in five business passengers at London airports in 2006 were female. Although this percentage has not changed significantly since 1996, there is a striking difference between the genders in terms of their income distribution. It appears that a significantly larger proportion of female business passengers come from lower income groups – a pattern which has not significantly changed over the period.

Figure 4.3 Income distribution of UK residents by gender at London airports 1996 to 2006, 2006 prices



Source: CAA Passenger Survey, 1996, 2000 and 2006.

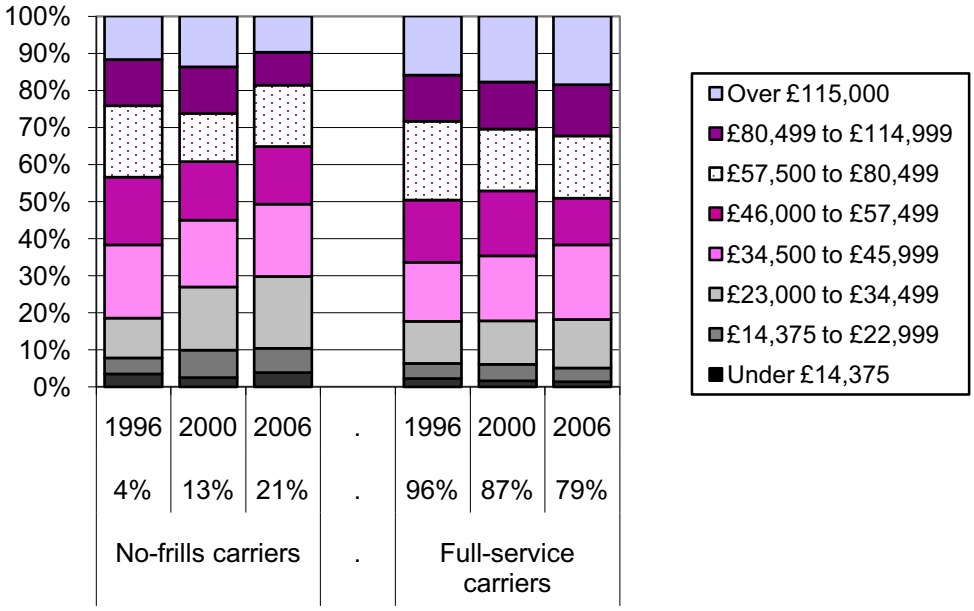
Note: All incomes have been converted to 2006 prices.

Income distribution by carrier type

4.7 The income distribution of UK business passengers using the London airports shows more marked changes over time when looked at by carrier type than by gender. Figure 4.4 shows that the proportion of business passengers travelling on NFCs at the London airports has increased rapidly from less than 5% in 1996 to over 20% in 2006. There is a significant increase in the proportion of business passengers with lower incomes travelling on NFCs, although the same trend is present, albeit to a much lesser extent, for FSCs. This trend, combined with the increased proportion of business passengers travelling on NFCs, means that the overall average income of business passengers fell in real terms between 1996 and 2007.

4.8 This is most likely due to a combination of the increasingly international nature of the UK's businesses (including small and medium sized enterprises) and the greater range of destinations and lower fares available at London and regional airports, both of which could make air travel viable for smaller companies and more junior staff from larger companies.

Figure 4.4 Income distribution of UK business passengers using London airports 1996 to 2006, 2006 prices



Source: CAA Passenger Survey, 1996, 2000 and 2006.

Note: All incomes have been converted to 2006 prices.

Business passengers travelling in different classes

4.9 The full-service scheduled airline industry has long relied on a combination of high-yield business travellers and a large number of low-fare-paying economy passengers to maximize revenues and profits.

4.10 The business travel market has, in recent years, seen the proportion of business passengers who travel in premium classes declining across all sectors, particularly the short-haul market, as more travellers question the value of premium class products or are attracted away by cheaper alternatives.[69] The average 3.4% per annum growth rate of international business passengers between 1996 and 2007 documented in

69. Business passengers in 1996 sometimes had no real choice as there was only very small presence of NFCs. The 'Saturday night stay' rule existed on all but the highest economy fare, and fully flexible tickets were generally only available in the Business Class cabin.

Chapter 2 has been accompanied by a downward trend in airline average yields since the late 1990s and the shift of business passengers from travelling in premium cabins to economy seats.

4.11 Table 4.1 shows the proportion of business passengers in different cabin classes and the percentage of business passengers who travel in the premium classes as opposed to travelling on economy tickets.

Table 4.1 Proportion of business passengers travelling in different cabin classes

	How much of each cabin is filled by business passengers?		Which cabin do business passengers use?	
Ticket Type	*1996*	*2007*	*1996*	*2007*
Long-haul destinations				
First/Business/Club	79%	73%	34%	23%
Premium Economy	n/a	56%	n/a	9%
Economy	28%	20%	66%	69%
Total long haul	36%	25%	100%	100%
Short-haul destinations				
Business/Club	93%	81%	40%	9%
Economy	39%	26%	60%	91%
Total short haul	50%	28%	100%	100%
Domestic destinations				
Business/Club	91%	93%	22%	8%
Economy	51%	46%	78%	92%
Total domestic	56%	48%	100%	100%

Source: CAA Passenger Survey, 1994–1996, 2005–2007.

Note: Airports not surveyed in 1996 and/or 2007 have been scaled up from the nearest survey year.

4.12 While the proportion of domestic passengers in business class who are travelling on business has remained broadly the same over the years, there has been a reduction in the long-haul (79% to 73%) and short-haul (93% to 81%) markets compared with 1996. In addition, the proportion of business passengers who opt to travel in premium classes has declined across all three markets, particularly for the short-haul routes.

4.13 This change in the pattern of business passengers travelling in different classes reflects the underlying changes in, among other things, the aviation environment, the fare structures and the level of fares in both long- and short-haul markets in recent years. Enhanced competition in Europe and elsewhere has increased the choice of airlines, range of destinations, level of frequency and ticket flexibility and reduced average fare levels. For example, the introduction of premium economy class on long-haul routes by some airlines to further price discriminate passengers has led to 'trading down' by some first/club class business passengers[70] and 'trading up' by economy passengers who are travelling for leisure purposes but want to pay for extra comfort. Table 4.1 shows that, of the 32% of long-haul business passengers travelling in the premium class in 2007, more than one quarter are travelling on a premium economy ticket.[71] The table also indicates that within this premium economy class, 44% are leisure travellers.

70. Premium Economy Class also appeals to small and medium-sized enterprises that do not have a corporate contract with an airline or alliance because they are unlikely to be able to negotiate Business Class discounts based on buyer power.

4.14 On domestic and short-haul routes, NFCs have made inroads into the market share of FSCs for leisure, and, to a lesser extent, business passengers. They were able to achieve this by significantly reducing the level, as well as changing the structure of fares (such as removal of 'Saturday night stay' rule) and instead, offering an increasingly wider choice of on-demand 'frills' such as priority boarding and lounge access which might attract business passengers. Furthermore, the point-to-point operating model, the use of less congested airports, and the consequent high number of rotations that can be achieved, all serve to allow NFCs to offer a wide range of choices to passengers in terms of destinations and flight frequency (increasing the likelihood of a daily/near daily service) on some less dense routes.

Purpose of business travel

4.15 When looking at the types of employment among business passengers, banking and finance-related industries feature highly. This section looks at the main purpose of business travel and the proportion of business passengers from various industry groups, by carrier type and airport respectively.

4.16 Table 4.2 shows that attending internal meetings or meetings with external clients were the main purposes of business travel in 2001 and 2007. There is little difference in terms of trip purpose between those travelling on NFCs and FSCs over time, although the proportion of total UK business passengers carried by NFCs has more than doubled since 2001.

Table 4.2 Main purpose of business travel by carrier type

Main business purpose	No-frills carriers		Full-service carriers		% share of no-frills carriers	
	2001	2007	2001	2007	2001	2007
Attending internal business	34%	35%	35%	36%	12%	27%
Meetings with customers	34%	34%	30%	30%	14%	30%
Conference/congress	7%	8%	8%	10%	11%	24%
Overseas employment	2%	2%	3%	4%	10%	20%
Trade fair/exhibition	3%	4%	2%	3%	19%	35%
Contract home leave	1%	1%	2%	2%	5%	11%
Au pair/studies paid by employer	1%	1%	1%	1%	12%	29%
General business	16%	13%	15%	11%	13%	32%
Airline staff/armed services	2%	2%	3%	2%	8%	26%
Total	**100%**	**100%**	**100%**	**100%**	**13%**	**28%**

Source: CAA Passenger Survey, 1999-2001, 2005-2007.

71. The flexible Premium Economy (W2) product was first introduced by Virgin in the 90s and followed by BA in 2000 which was initially rolled out as a supplement (c20%) over the flexible Economy (Y2) fare. While the relativities in fare levels between the different classes have evolved over time, the current Premium Economy fare on BA flights is typically about 35%–45% of the fully flexible Business (J2) fare and c35%–55% above the flexible Economy (Y2) fare on most dense long-haul routes, although the increment over the Y2 fare could be as high as 70% or more on some thicker routes such as New York and Los Angeles. However, the spread between different classes is generally much smaller on thinner routes.

4.17 There is a noticeable difference across London airports in terms of the industry group from which business passengers originate. This variation appears to be attributable more to airport location than to the carrier type. Table 4.3 shows that the largest sector using London City has been the 'City' occupations[72], with 48% of all business passengers, compared with 20% or less from this group using Heathrow and the other London airports. Due to its close proximity to the financial centre[73] of London, London City has been able to attract a disproportionately high volume of this element of business traffic (9% of the total as indicated in Table 4.4 below), even though it only has 4% of the total business passengers at the five London airports.

Table 4.3 Distribution of business passengers by industry group at London airports in 2006

Industry group	London City	Heathrow	Gatwick + Stansted + Luton	
			No-frills carriers	Full-svc carriers
Banking/finance/insurance/legal	48%	20%	16%	18%
Health/education/public services	11%	14%	16%	16%
Transport & communications	8%	14%	13%	14%
Engineering/IT consulting/electrical supplies	7%	12%	12%	10%
Catering, retail, wholesale and hotel	4%	6%	10%	6%
Energy & water supply industries	5%	5%	3%	9%
Mining & manufacturing industries	4%	9%	5%	6%
Construction	4%	4%	10%	6%
Food/agriculture/forestry/fisheries etc.	2%	5%	5%	4%
Recreational & entertainment industries	2%	3%	4%	3%
Other business	4%	8%	7%	7%
Total business passengers (m)	**1.5**	**24.2**	**7.7**	**3.9**
	100%	**100%**	**100%**	**100%**

Source: CAA Passenger Survey, 2006.

4.18 By contrast, Stansted appears to be under-represented in this industry group and in the energy/water supply industries with market shares of only 7% and 5% respectively, despite handling 11% of total business passengers at London airports and having relatively good transport links with the City of London (the 'Square Mile'). Instead, Stansted appears to attract business passengers disproportionately from the health/public sectors, catering/retail/wholesale and construction industries. On the other hand, Gatwick appears to have a more-than-proportionate share of business passengers from the energy/water supply industries, unlike Luton or Stansted, where the opposite is true.

72. For brevity, the banking, financial, insurance and legal professions are referred to in this report as 'City' occupations, but this does not necessarily refer to their geographical location.
73. For the purposes of this report, the 'financial centre' refers to that area of London where the majority of the capital's workers employed in 'City' occupations are based. This comprises two main locations – the City of London (the 'Square Mile') and Canary Wharf. Both are located to the east of the capital, and are approximately five miles apart. Transport links and geographical proximity mean that Stansted and London City are well-placed to serve this area. The opening of the DLR station at London City in 2005 improved accessibility further, from both Bank station in the City of London and from Canary Wharf itself.

Table 4.4 Proportion of total London business passengers by airport and by industry group in 2006

Industry Group	London City	Gatwick	Heathrow	Luton	Stansted	Total	Total Pax (m)
Banking/finance/ insurance/legal	9%	14%	65%	4%	7%	100%	7.5
Health/education/ public services	3%	15%	61%	5%	15%	100%	5.4
Transport & communications	2%	14%	67%	5%	11%	100%	5.1
Engineering/IT cons./ electrical supplies	3%	13%	68%	6%	12%	100%	4.3
Catering, retail, wholesale and hotel	2%	15%	59%	7%	16%	100%	2.5
Energy & water supply industries	4%	24%	66%	1%	5%	100%	1.9
Mining & manufacturing	2%	11%	74%	4%	8%	100%	2.8
Construction	3%	20%	51%	8%	18%	100%	2.1
Food/agriculture/ forestry/fisheries etc.	2%	12%	66%	6%	14%	100%	1.7
Recreational & entertainment	3%	13%	63%	8%	13%	100%	1.1
Other business	2%	15%	69%	5%	9%	100%	2.8
% of total London business passengers	**4%**	**15%**	**65%**	**5%**	**11%**	**100%**	**37.3**

Source: CAA Passenger Survey, 2006.

Airport catchment area

4.19 The catchment area from which an airport draws its passengers can be defined in a number of different ways. The 'relevant' geographical market for different types of passengers for an individual airport is likely to be affected by a number of factors including surface access journey times to and from the airport, the spatial distribution (in relation to their residential or work location) of outbound passengers around the airport and the intended final destination of inbound passengers.[74]

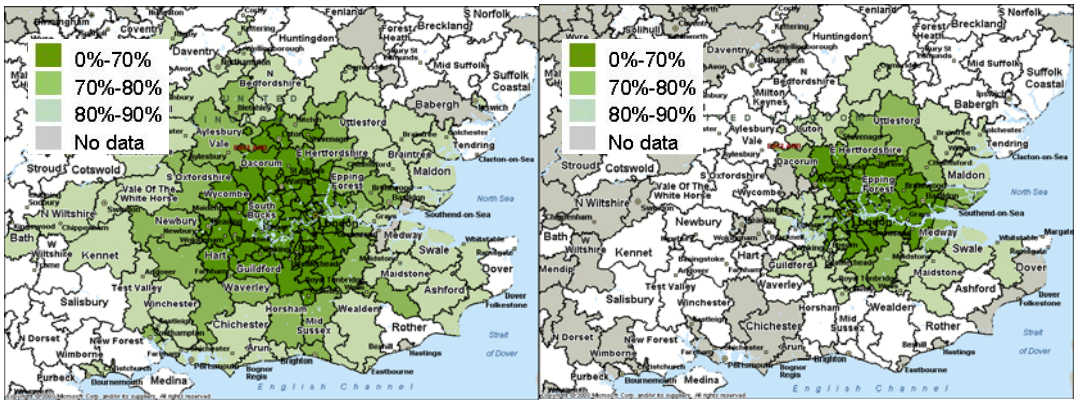
4.20 One way to analyse the relative concentration of passengers around an airport is to map out the actual distribution of passengers by average time spent travelling to an airport in order to catch a flight or (on arrival) travelling from an airport to their ultimate destination. Heathrow and London City are the two London airports with the highest proportion of business passengers. For each of these two airports in 2006, Figure 4.5 shows, in the darkest green shade, the origin of the 70% of scheduled short-haul international business passengers with the shortest journey times.[75] The middle

74. See, for example, Initial price control proposals for Heathrow, Gatwick and Stansted airports: Supporting paper II, CAA (December 2006).
75. Only short-haul passengers were considered since London City had no long-haul routes at that time.

shade shows the area in which the next-closest 10% of short-haul business passengers are located, with the lightest shade showing a further 10%. Thus, the combined green shaded areas represent the origin of travel for 90% of the short-haul business passengers at Heathrow and London City airports.

Figure 4.5 Distribution of surface origin/destination for short-haul international business passengers at Heathrow and London City, 2006

Heathrow ***London City***



Source: CAA Passenger Survey, 2006, using Microfit Mappoint.

4.21 Figure 4.5 shows that Heathrow draws its short-haul business passengers from a wide area of South East England and that the proportion from Greater London greatly exceeds that of any other individual county. The distribution has not changed much between 2000 and 2006, although there was a slight expansion in the 70% area (darkest shade).

4.22 By comparison, London City's catchment area appears to be much more local – 90% of its business passengers had an airport access time of less than 90 minutes (compared with almost 115 minutes for Heathrow) in 2006. Nevertheless, this represents a noticeable increase from 72 minutes for the corresponding 90% of passengers in 2000, indicating that its catchment area has expanded as the airport has grown in size and in number of destinations served. Other transport developments in the Dockland area surrounding London City have also helped to improve the accessibility of the airport.[76]

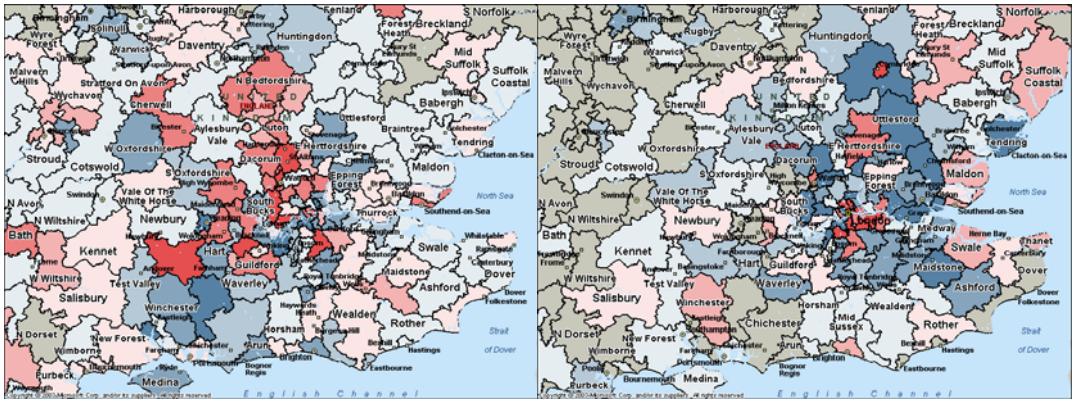
4.23 The change in the geographical distribution of short-haul international business passengers using these airports between 2000 and 2006 is shown in Figure 4.6. Dark blue shading indicates where the percentage has increased by more than 0.4 of a percentage point,[77] while dark red shading indicates a reduction of more than 0.4 of a percentage point.

4.24 Although the change in catchment area is rather complex for both airports, it appears that there is a relative concentration of increasing shares for London City in the north-east and south-east of London while, for Heathrow, the areas of increasing and reducing shares are more evenly distributed.

76. Passenger numbers at London City have grown rapidly since its opening in 1987. This has happened alongside the regeneration of the area over the last 20 years, overseen by the London Docklands Development Corporation (LDDC). Over this period and subsequently, Canary Wharf has grown in size, alongside other transport developments including the opening of the DLR and the Jubilee extension to the London Underground (completed in 1999). By 2007, the working population of Canary Wharf was estimated (by the Canary Wharf Group plc) to be 93,000 (compared with 14,000 in 1996).
77. For example, from 3.0% of passengers to 3.5%.

Figure 4.6 Changes in point of origin of Heathrow and London City short-haul international business passengers, between 2000 and 2006

Heathrow ***London City***



Source: CAA Passenger Survey, 2000 and 2006, using Microfit Mappoint.

Part 1 Chapter 5 Business aviation

Chapter summary

Traffic

- Business aviation grew significantly between 2003 and 2007, but remained a relatively small sector in terms of movements (around 7% of all UK movements) and passengers carried (likely to be less than 1.5% of the business passengers carried by scheduled services) in 2008.
- However, against the backdrop of a declining proportion of business passengers travelling in premium classes (especially in the short-haul market) on scheduled airlines, it is likely that some premium passengers have shifted from scheduled carriers to business aviation in the last five years.
- Business aviation in the UK is primarily a domestic or short-haul phenomenon. Domestic flights accounted for 30% of all business aviation movements in 2008. The most international business movements at UK airports in 2008 were to/from France (17%) – more than double that of any other country – but the Russian Federation saw the highest average growth rate of 30% per annum between 2004 and 2007.

Route network

- By comparison to commercial scheduled services, business aviation has a much wider network linking airport pairs that are either not served regularly, or not served at all by scheduled carriers.[78] Only around 7% of the 14,000 UK–International airport pairs used by business aviation services in 2008 had scheduled services (i.e. with at least one scheduled departure per working day or 260 annual departures).

UK airports

- On-demand business aviation services in the London area have spread among less congested non-primary airports such as Luton, Farnborough, London City, Biggin Hill and Northolt around London due to increasing difficulty in securing runway access to slot-coordinated airports such as Heathrow and Gatwick.
- Luton (38 departures/day) and Farnborough (29 departures/day) remained the top two airports with the most business aviation traffic in 2008, accounting for 25% of total UK business aviation departures. Northolt, Biggin Hill and Farnborough are the UK airports where business aviation forms the highest proportion of total traffic (more than 85% at each airport).
- As a result of its ad hoc demand, business aviation might be more responsive to changes in economic and business conditions than scheduled services. This seems to be borne out by the more pronounced decline of business aviation activities (a drop of more than 20% year on year) than other traffic (around 10% fall) in the second half of 2008 and early 2009 as a result of the recent economic downturn.

78. This includes some small airports which cannot be used by commercial scheduled carriers except for small business aircraft, because of short runway length.

5.1 Although the majority of business travel uses commercial scheduled services at medium and large airports, there is a small but significant proportion of UK business travel (in terms of number of movements) using ad hoc business aviation services based on small business aircraft, typically with less than 15 seats, and usually operating from less congested airports. In 2008, business aviation accounted for almost 7% of all UK movements operated under 'instrument flight rules' (IFR).[79]

5.2 Business aviation provides regular and ad hoc charter services for business travellers, as well as for overnight mail and freight. In terms of annual gross value added, the business aviation sector is said to have made notable contributions to the general economy.[80] However, business aviation also absorbs capacity and resources in terms of infrastructure, including airport and air traffic management, because of its unique demand characteristics and pattern of traffic flow.

5.3 This chapter looks at the development and characteristics of this fast-growing sub-sector of business travel in the UK in recent years, and how the services provided by business aviation differ from commercial scheduled services. It also considers the impacts of business aviation demand on UK air traffic management and airspace planning.

Definition of business aviation

5.4 Although there is no single best definition of 'business aviation', it is commonly regarded as the use of any general aviation aircraft for a business purpose.[81] This includes both commercial and non-commercial operations of an aircraft, and can be divided into three categories:

- Commercial – aircraft flown for ad hoc business purposes by an operator having a commercial operating certificate. These include air taxi and fractional operators.[82]
- Corporate – non-commercial operations in which a company owns and operates its own aircraft for the carriage of employees.
- Owner operated – non-commercial operation for business purposes by an individual as owner of the aircraft.

5.5 However, most UK business aviation traffic is outside the scope of CAA traffic statistics and survey data, and information on the number of business passengers using business aviation services is not readily available. Therefore, the analysis of business aviation traffic hereafter is based on Eurocontrol data showing IFR flights by types of aircraft which are considered to be most likely used for business aviation services.[83]

79. Flights are generally referred to as operating under 'IFR' when they are operating within the en-route air traffic control structure for some or all of their journeys. Data on the alternative 'visual flight rules' (VFR) flights are not readily available and, in any case, VFR is generally not a viable option for business aviation as it is difficult to operate with any degree of predictability in poor weather conditions.
80. For example, according to a recent study by PWC Economics, The Economic Impact of Business Aviation in Europe (December 2008), business aviation was estimated to have contributed directly and indirectly a total of up to €20bn to the European economy in 2007.
81. A definition adopted by the International Business Aviation Council in 1998 and subsequently referenced by ICAO is "that sector of aviation which concerns the operation or use of aircraft by companies for the carriage of passengers or goods as an aid to the conduct of their business, flown for purposes generally considered not for public hire and piloted by individuals having, at the minimum, a valid commercial pilot licence with an instrument rating".
82. Fractional ownership means having a share of a business aircraft which normally involves owning block(s) of flying time of 100 hours or more per year flying (broadly equivalent to 1/8th shares of an aircraft) although it is also possible to own smaller shares of an aircraft.
83. The list of aircraft that are considered as business aircraft can be found in Annex A of More to the Point: Business Aviation in Europe in 2007, Eurocontrol (2008).

5.6 One problem of defining business aviation based on aircraft type alone is that the same aircraft type may also be used for non-business purposes, such as leisure charter flights to sporting events, pilot training, medical evacuation flights, military and state flights – all are encapsulated in the Eurocontrol data set. On the other hand, large business jets (such as Boeing Business Jets) and helicopters are not included in this list of business aircraft. This limitation of the data set should be kept in mind when interpreting results presented in this chapter labelled as business aviation.

UK business aviation traffic growth in recent years

5.7 Business aviation traffic expanded rapidly in the UK between 2003 and 2007, with business aviation movements to/from the UK growing by an average of 13.7% per annum compared with 3.4% per annum for other flights (Table 5.1 and Figure 5.1).[84] In 2007, business aviation movements accounted for 7.3% of all UK movements (excluding overflights) operated under IFR, although this figure had dropped to 6.9% in 2008.

Table 5.1 Volume and growth of UK business and other movements (daily average)

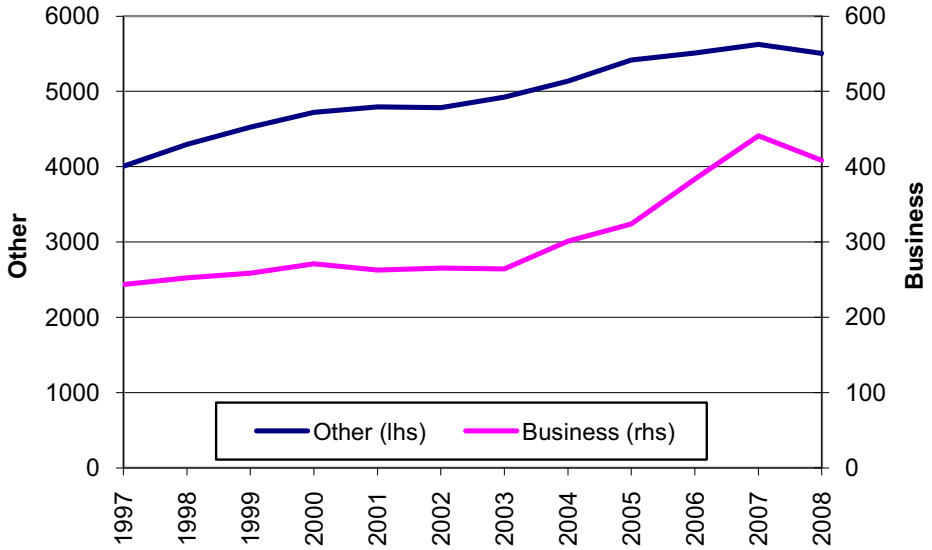
	Other movements/day		Business movements/day		Total movements/day		Proportion of business movements
Year	volume	growth	volume	growth	volume	growth	
1997	4009		244		4253		
1998	4299	7.2%	252	3.6%	4551	7.0%	5.5%
1999	4526	5.3%	259	2.6%	4784	5.1%	5.4%
2000	4720	4.3%	271	4.8%	4991	4.3%	5.4%
2001	4797	1.6%	263	-3.1%	5060	1.4%	5.2%
2002	4783	-0.3%	265	1.1%	5048	-0.2%	5.3%
2003	4923	2.9%	264	-0.5%	5187	2.7%	5.1%
2004	5136	4.3%	301	14.0%	5437	4.8%	5.5%
2005	5418	5.5%	324	7.6%	5742	5.6%	5.6%
2006	5512	1.7%	383	18.3%	5896	2.7%	6.5%
2007	5626	2.1%	441	15.0%	6067	2.9%	7.3%
2008	5508	-2.1%	409	-7.3%	5916	-2.5%	6.9%

Source: Eurocontrol.

Note: Domestic movements are only counted once to aid comparison.

84. 'Other' flights include all other movements that are not business aviation as defined by the list of business aircraft.

Figure 5.1 UK business and other movements per day, 1997–2008

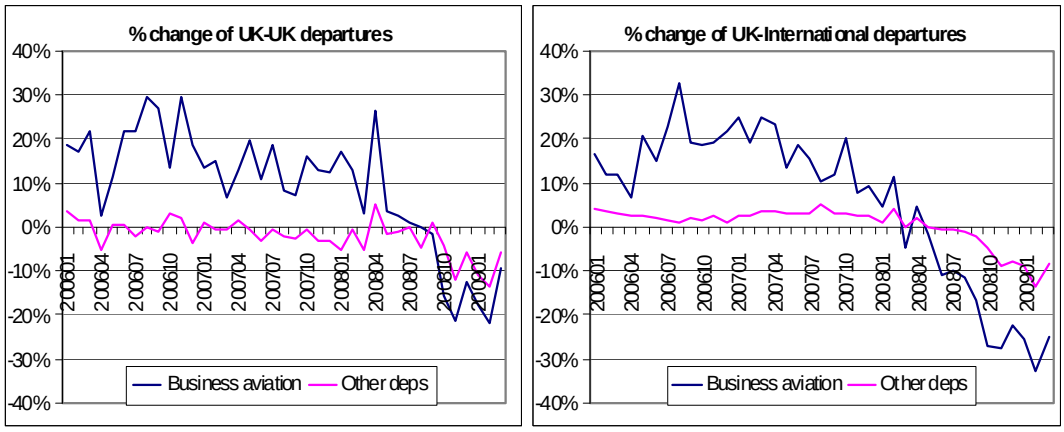


Source: Eurocontrol.

Note: Domestic movements are only counted once to aid comparison.

5.8 The latest available data suggest that the economic downturn has had a more significant impact on business aviation than on other traffic, particularly for UK–International business flights in the second half of 2008 (Figure 5.2). This is due in part to the fact that business aviation adheres to no scheduled timetable, and so a downturn in demand is likely to result in an immediate decline in movements. For commercial air transport, weakening demand may be reflected first in lower seat factors and yield reductions and only later in fewer flights. This might also suggest that, when economic conditions and business confidence recover from the current recession, business aviation could see a faster increase in movements than commercial scheduled services.

Figure 5.2 Percentage change in UK business aviation and other departures by sector



Source: Eurocontrol.

5.9 The rising popularity of business aviation in recent years has been driven by a host of factors. While some of these are general drivers (such as increasing globalisation and economic growth) that affect all air travel segments, others are more specific to business aviation. For example, the use of smaller airports most convenient for the client, avoiding congestion and delays at some major airports, long queues for airport

security checks, and the ability to choose to fly to specific destinations at the most convenient times (which scheduled flights may not be able to provide) are some of the factors which make use of business aviation an attractive alternative to premium airline travel for some time-sensitive business travellers. The personalised service, including privacy, the convenience of allowing multiple stops en-route to destinations as well as the capability for co-workers to meet, plan and work with each other on board business aircraft are also valued by some business customers.

5.10 Although data on the number of passengers using business aviation services is not readily available, the rapid expansion of business aviation movements in recent years against the backdrop of a declining proportion of business passengers travelling in premium classes (especially in the short-haul market) on scheduled airlines suggests that some premium passengers might have shifted from scheduled carriers to business aviation, albeit the number of passengers travelling on business aviation services is still relatively small (likely to be less than 1.5% of the total UK business passengers).[85]

Business aviation model and traffic characteristics

5.11 Business aviation has a very different business model and operational characteristics from those of commercial scheduled carriers. The essence of the business aviation model is to provide on-demand point-to-point services to and from an airport of the client's choice (often the nearest or least congested one). Factors such as increasing congestion and delays at some major airports, security concerns (in terms of travel delays and safety of senior personnel) and the development of less expensive business jets have made business aviation an attractive alternative to premium travel for some time-sensitive passengers.[86] Thus, busy customers might be able to complete trips in a day which otherwise would involve the inconvenience and expense of overnight stays.

5.12 Business aviation has been considered by many as a niche market exclusively used by those who can afford to purchase a private jet. However, the emergence in recent years of fractional ownership (as typified by a company such as NetJets) and operators that hire out business jets for individual trips has been aimed at stressing their potential cost-effectiveness, and hence brought about changes to the supply of premium air travel.

5.13 Because of its ad hoc nature of demand, business aviation has different operational characteristics from scheduled carriers, as outlined below:

a) There are many small operators with only a few big players

5.14 The business aviation market in Europe is served by a few big operators along with many small operators which have a fleet size of not more than five aircraft.[87] For example, Table 5.2 shows that only ten (or less than 2%) of the more than 500 business aviation operators in the UK had at least 730 UK departures per annum (or two departures per day on average) in 2008. These ten operators, each representing between 1% and 16% of the total UK business aviation departures, accounted for 37% of all UK business aviation traffic in 2008.

85. Typically a business aircraft might have a configuration seating between four and twelve persons. Assuming there are, on average, five business travellers per flight, and given that a high proportion of these are positioning flights, the estimated number of passengers carried by business aviation would be well under 1 million as compared with the 63 million passengers travelling for business purposes or 240 million total UK passengers on commercial flights in 2007.
86. Some companies use corporate aircraft as an integral part of their employees' travel as well as for bringing potential customers to the UK. For example, Ford used to have aircraft based at Stansted and Southend to ferry employees between its car plants.
87. According to the European Business Aviation Association, 80% of European business aviation operators have fewer than five aircraft.

Table 5.2 Top 12 business aviation operators in the UK, 2008

Operator	Departures in 2008	% share of total UK departures	Cumulative share
NetJets	11,676	16.0%	16%
Gama Aviation	3,957	5.4%	21%
Capital Trading Aviation	3,145	4.3%	26%
London Executive Aviation	1,869	2.6%	28%
Vickers	1,819	2.5%	31%
Air London International	1,106	1.5%	32%
Bristol Flying Centre	1,038	1.4%	34%
Euro Business Jets	882	1.2%	35%
Hangar 8	827	1.1%	36%
Edinburgh Air Charter	771	1.1%	37%
Skydrift	729	1.0%	38%
EuroJet Aviation	693	0.9%	39%

Source: Eurocontrol.

5.15 By comparison, the UK commercial scheduled market had around 200 scheduled operators in a market that is well over 10 times bigger than business aviation (in terms of number of movements), in which 98 operators (or almost 50% of the scheduled operators) had more than 730 UK departures per annum and accounted for about 97% of all UK scheduled departures in 2008. Of these 98 operators, 21 (or 10% of all scheduled operators) had more than 1% of the total UK scheduled departures.

b) Business aviation serves a much wider and uneven network than that of scheduled carriers

5.16 Business aviation serves a wide network that spreads small volumes of air traffic among a large number of small and medium sized airports, on routes with no or infrequent scheduled services. The ad hoc nature of business aviation demand for point-to-point services to and from airports most convenient for its clients entails a much greater number of potential airport pairs for business aviation than for commercial scheduled services. Around 7% of the more than 14,000 UK–International airport pairs used by business aviation services in 2008 had alternative scheduled services.[88] This 7% of airport pairs handled a disproportionately large proportion (about 20%) of total UK–International business aviation departures in 2008. The remaining 80% of UK–International business aviation traffic was more thinly spread across the other 93% of airport pairs.

5.17 The direction of traffic flow for business aviation is also relatively uneven compared with the scheduled network. While regular scheduled services normally have matching numbers of outbound and return flights between an airport pair, business aviation has significantly fewer airport pairs with the same number of flights in both directions – and most of these airport pairs are flown less than once per week. For example, while almost 50% of the 1,400 UK–International airport pairs[89] served by

88. Defined as having at least one scheduled departure per working day or 260 annual departures. However, this may also include a more frequent but seasonal service.
89. Airport pairs that had fewer than 20 movements in 2008 were excluded from the data.

commercial scheduled carriers had 10 or more movements per week in 2008, less than 4% of the 14,000 UK–International airport pairs linked by business aviation services had more than one movement per week.

5.18 In part, this is due to the high proportion of air taxi or fractional ownership flights for positioning purposes, where the aircraft is flown with no passengers on board. The volume of such flights is a natural consequence of the on-demand nature of business aviation. Once a passenger has been delivered to their chosen destination, it may be some time before they require an onward or return flight. The business aviation operator may therefore achieve better utilisation of its aircraft by flying to another airport to pick up a new client. Eurocontrol have estimated[90] that positioning flights could be as high as 40% of departures for some business aviation operators in Europe.

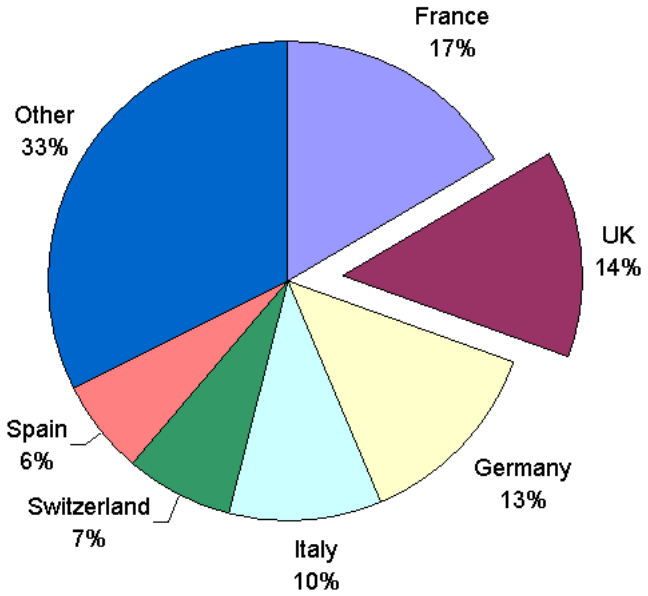
c) Business aviation has more peaky demand patterns (especially for hourly traffic) and the volume and direction of traffic flows can be highly variable

5.19 Due to the peakiness and ad hoc nature (in terms of volume and direction of flows) of its demand, business aviation can add complexity to the management and planning of airspace usage (see paragraphs 5.33 to 5.38 for further discussion on this).

Countries with most business aviation traffic to/from UK

5.20 Business aviation is primarily a domestic and short-haul phenomenon and the bulk of business aviation traffic is concentrated in six States in ESRA[91] (Figure 5.3). According to Eurocontrol, the UK had the second largest market share of European business aviation in 2007 after France.[92]

Figure 5.3 Distribution of business aviation departures in ESRA, 2007

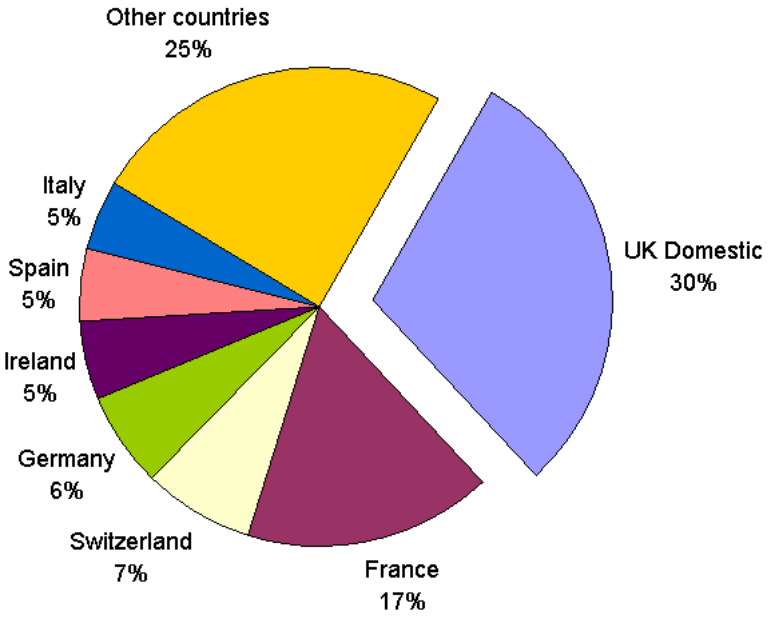


Source: Eurocontrol.

90. Eurocontrol: *More to the Point: Business Aviation in Europe in 2007* (2008).
91. The ESRA (Eurocontrol Statistical Reference Area) in 2002 consists of the airspace of Austria, Belgium, Bulgaria, Croatia, Cyprus, Czech Republic, Denmark, Finland, France, Germany, Greece, Hungary, Ireland, Italy, Luxembourg, Malta, Moldova, the Netherlands, Norway, Portugal (including Azores), Romania, Slovakia, Slovenia, Spain (including Canary Islands), Sweden, Switzerland, Turkey and the UK.
92. See footnote 90.

5.21 Since the time advantages of using business aviation arise mainly through shorter surface access times to and through airports, rather than faster air travel (commercial aircraft may even fly faster), the time saving from business aviation tends to be most significant for shorter trip distances. Consequently, domestic flights made up the largest segment (30%) of all business aviation movements to/from the UK in 2008. As for international traffic to and from the UK, France accounted for almost 17% of all UK business movements – more than double that of any other country (Figure 5.4).

Figure 5.4 Business aviation movements to/from the UK, 2008

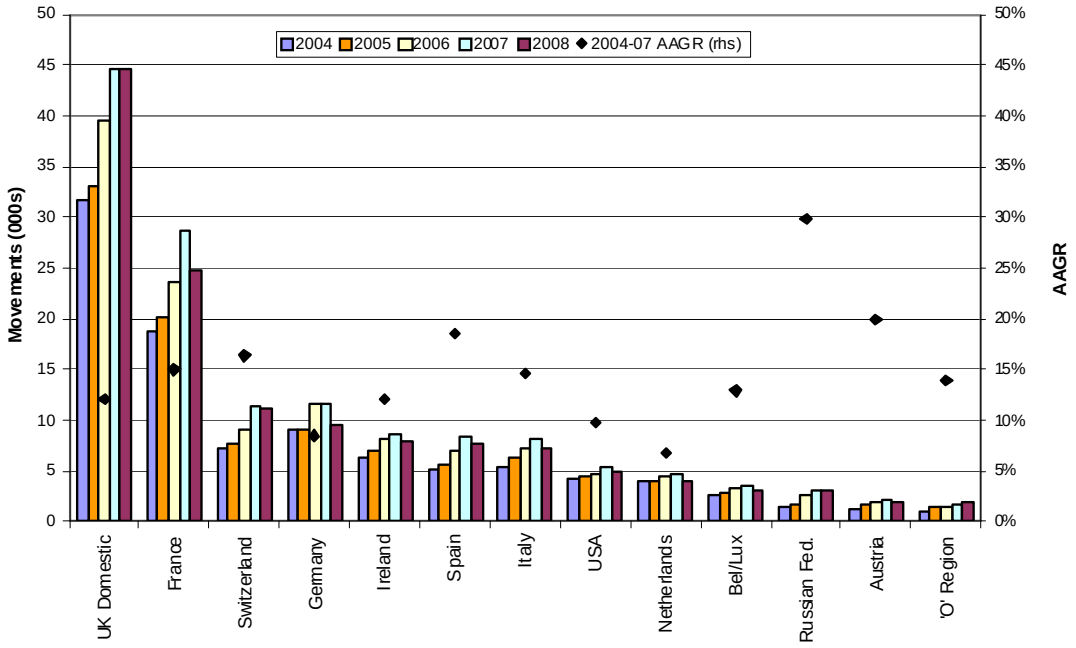


Source: Eurocontrol.

Note: Domestic movements are only counted once to aid comparison.

5.22 Prior to the economic slowdown that began in 2008, UK business aviation was growing at an annual rate of 13.5% on average between 2004 and 2007. Among the top international country destinations, Figure 5.5 shows that business traffic between the UK and the Russian Federation saw the largest growth over this period, with an average growth rate of 30% per annum, although the UK–Russian Federation traffic represented only about 2% of total UK business traffic in 2008.

Figure 5.5 UK business movements and average annual growth (2004-2007)



Source: Eurocontrol.

Note: Domestic movements are only counted once to aid comparison.

AAGR = average annual growth rate

Based on ICAO classifications, the 'O' Region includes the Middle East countries, Afghanistan and Pakistan

International airports with most business aviation departures from UK

5.23 Table 5.3 shows the top 25 destination airports which represented more than 45% of total departures for for international business aviation departures in 2008. While scheduled networks tend to build around capital cities, main population centres and popular leisure destinations, business aviation in Europe mostly links airport pairs as close to business centres as possible that are not regularly served by scheduled carriers. For example, around 60% of the business aviation departures from UK to Geneva-Cointrin and Nice airports in 2008 involved airport pairs that were not served by more than one scheduled departure per working day on average (or 260 departures per annum) by commercial scheduled carriers.

5.24 Table 5.3 shows that business aviation traffic to France and Switzerland tended to be concentrated at Paris, Nice, Cannes, Geneva and Zurich. Although Germany was the third most popular country after France for UK business aviation in 2008, the distribution of business movements was more evenly spread among the German airports in comparison to other countries, with only Munich featuring in the top 25 cities.

Table 5.3 Top 25 destination airports with highest proportion of UK–international business departures in 2008

City – Airport	Country	Departures per day	Growth on 2007	% share of total UK-Int'l departures per day	Cumulative share
Paris – Le Bourget	France	9.0	-24.5%	6.3%	6%
Geneva	Switzerland	7.0	0.4%	4.9%	11%
Nice	France	6.7	-6.9%	4.7%	16%
Dublin	Ireland	5.7	-12.2%	4.0%	20%
Zurich	Switzerland	3.6	-6.8%	2.5%	22%
Cannes	France	3.0	-17.8%	2.1%	24%
Moscow – Vnukovo	Russian Fed.	2.8	-5.6%	1.9%	26%
Palma de Mallorca	Spain	2.5	-4.9%	1.7%	28%
Amsterdam	Netherlands	2.5	-6.2%	1.7%	30%
Malaga	Spain	2.1	2.2%	1.5%	31%
Milan – Linate	Italy	1.9	-16.6%	1.4%	33%
Rotterdam	Netherlands	1.7	-15.4%	1.2%	34%
Brussels International	Belgium	1.6	-18.5%	1.1%	35%
Madrid – Torrejon	Spain	1.5	-14.8%	1.1%	36%
Teterboro	USA	1.5	-4.4%	1.0%	37%
Sion	Switzerland	1.4	-2.6%	1.0%	38%
Chambery	France	1.4	1.2%	0.9%	39%
Bangor International	USA	1.3	-9.7%	0.9%	40%
Munich	Germany	1.3	-15.8%	0.9%	41%
Reykjavik	Iceland	1.2	-31.3%	0.8%	42%
Rome – Ciampino	Italy	1.1	-19.8%	0.8%	42%
Vienna	Austria	1.1	-13.6%	0.8%	43%
Shannon	Ireland	1.1	-1.5%	0.7%	44%
Faro	Portugal	1.1	-10.7%	0.7%	45%
Samedan	Switzerland	1.0	-4.8%	0.7%	45%
Total UK–International		**143**	**-10.1%**	**100%**	**100%**

Source: Eurocontrol.

Distribution of business aviation traffic by UK airports

5.25 The on-demand nature of many business aviation services means that they may have difficulty securing access at major, congested European airports where an allocated slot is required for all movements. Consequently, in the London area, business aviation has migrated to less congested non-primary airports such as Luton, Farnborough, Biggin Hill, London City and Northolt.

5.26 Table 5.4 lists the top 20 UK airports with the most business aviation departures in 2008 and their shares of total UK business aviation traffic. Together these 20 airports accounted for 70% of total UK business aviation departures. While Luton has, on average, the most business departures per day, Farnborough, Northolt and Biggin Hill airports are the airports with the highest proportion of business aviation traffic (more than 85% at each airport). Among these top business aviation airports, London City appears to have suffered the most from the current financial crisis and economic fallout. Business aviation traffic at the airport fell by 27% in 2008 (compared with an

average growth of 27% per annum between 2004 and 2007), resulting in a notable decline of its market share of total UK business aviation departures from 6.5% in 2007 to 5% in 2008.

Table 5.4 Top 20 UK airports with the most business departures per day in 2008

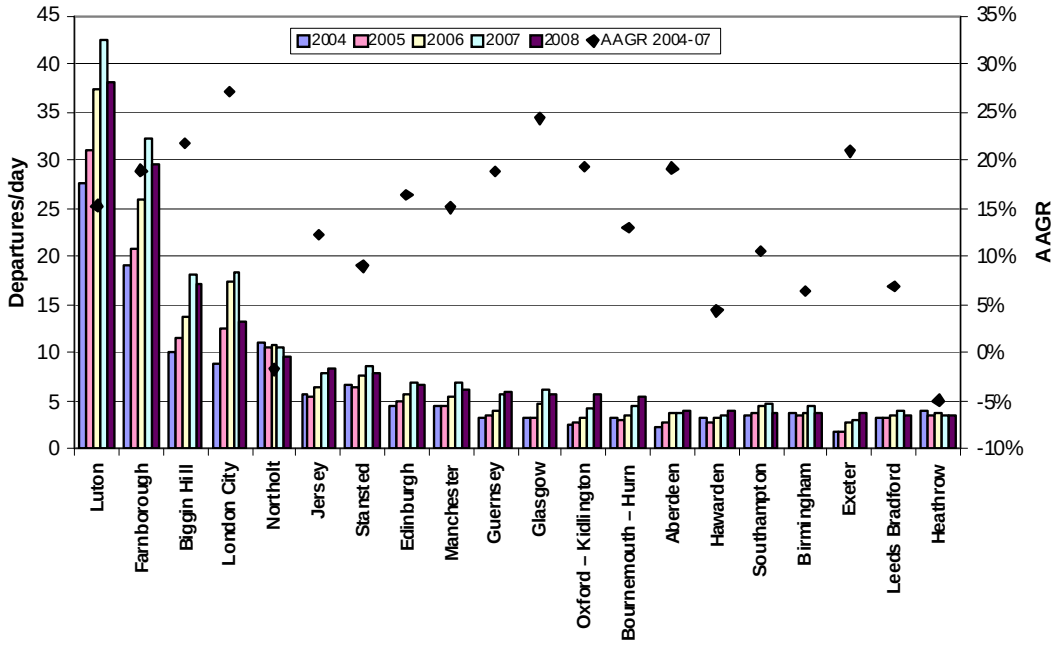
Airport	Business departures per day	% growth on 2007	Total departures per day	% Business departures	Airport share of total business departures	Cumulative share
London – Luton	38.1	-10.1%	159.4	24%	14.4%	14%
Farnborough	29.4	-8.3%	33.6	87%	11.1%	25%
Biggin Hill	17.2	-4.8%	20.0	86%	6.5%	32%
London City	13.2	-27.4%	129.3	10%	5.0%	37%
Northolt	9.5	-8.3%	10.7	89%	3.6%	41%
Jersey	8.5	7.0%	71.3	12%	3.2%	44%
London – Stansted	7.9	-8.5%	261.6	3%	3.0%	47%
Edinburgh	6.5	-5.1%	168.8	4%	2.5%	49%
Manchester	6.3	-8.8%	277.1	2%	2.4%	52%
Guernsey	6.0	8.2%	65.3	9%	2.3%	54%
Glasgow	5.7	-6.7%	130.1	4%	2.1%	56%
Oxford – Kidlington	5.5	35.8%	14.5	38%	2.1%	58%
Bournemouth – Hurn	5.4	18.4%	29.8	18%	2.0%	60%
Aberdeen	4.0	8.4%	94.6	4%	1.5%	62%
Hawarden	3.9	8.2%	6.7	57%	1.5%	63%
Southampton	3.8	-17.4%	67.5	6%	1.4%	65%
Birmingham	3.7	-16.8%	148.1	2%	1.4%	66%
Exeter	3.6	23.1%	28.1	13%	1.4%	67%
Leeds Bradford	3.5	-9.3%	57.4	6%	1.3%	69%
London – Heathrow	3.4	1.8%	653.8	1%	1.3%	70%
Total UK	**265**	**-5.8%**	**3684**	**7.2%**	**100%**	**100%**

Source: Eurocontrol.

5.27 Figure 5.6 shows the volume and average annual growth between 2004 and 2008 of the top 20 UK airports that have the most business aviation traffic. Apart from Northolt and Heathrow, where business aviation traffic has declined since 2004, there was strong growth across most airports prior to 2008.[93] A further disaggregated analysis of the data shows that almost 55% of all business aviation departures in the UK in 2008 were to international destinations. The top four of the above-listed airports in Table 5.4 with the highest number of business departures (together with Stansted) also had the highest proportion of international business flights. In contrast, more than three-quarters of business aviation departures from Jersey, Guernsey, Glasgow and Aberdeen in 2008 were to other UK airports.

93. In particular, London City, Biggin Hill, Glasgow and Exeter had the highest average growth rate (more than 20% per annum) between 2004 and 2007. The low growth in traffic at Northolt is due to an operational cap on business aviation at the airport.

Figure 5.6 Volume and average annual growth of business departures per day by UK airport



Source: Eurocontrol.

Note: AAGR = average annual growth rate.

Issue of runway access for business aviation

5.28 Business aviation may have increasing difficulty in gaining access to major congested airports. The ad hoc nature of flights generally prevents operators taking advantage of 'grandfather rights' at slot-coordinated airports, while at Heathrow and Gatwick the Government has made traffic distribution rules that give airlines priority.

5.29 The slot allocation process at airports designated as slot-coordinated is governed by an EU Regulation[94]. Slots are allocated according to historic precedence ('grandfather rights'), and business aviation can qualify only when operating to a schedule with a minimum of five slots within a summer or winter traffic season at the same time on the same day of the week. Although some business aviation services run almost to a schedule, such as corporate shuttles, most are ad hoc flights, either air taxi operators (as and when chartered by a customer) or corporate or owner-flown business aircraft.

5.30 Slot-coordinated airports in the UK are Heathrow, Gatwick, Stansted and Manchester. However, as other airports become more congested, so the need for them to become formally slot-coordinated increases – and designation as slot-coordinated bestows formal grandfather rights. Thus, business aviation operators using airports such as Luton and London City which have a significant proportion of business aviation traffic (around 25% and 15% respectively of each airport's total movements in 2007) face potential pressure from scheduled carriers in obtaining regular and sustained runway access.[95] London City applied to become slot-coordinated in 2009.

94. Council Regulation (EEC) 95/93 as amended by Regulation (EC) 793/2004 of the European Parliament and of the Council.

95. This has been recognised by both the European Commission and the European Parliament. See European Commission Communication COM(2007)0869 *Agenda for Sustainable Future in General and Business Aviation* (11 January 2007) and the Queiro report on general aviation adopted by the European Parliament on 3 February 2009.

5.31 What is more, traffic distribution rules[96] made by the Secretary of State require that specific permission must be given by the operators of Heathrow and Gatwick airport before business aviation can operate in peak periods, which at both airports are defined as virtually the whole day.[97]

5.32 The development of secondary and less congested airports for the specific use of business aviation (such as Biggin Hill, Farnborough and Northolt around London) has helped to ease the access problem. One large business aviation operator, NetJets Europe, has gone further and sought to collaborate with strategic European airport operators to obtain regular and sustained runway access. It has acquired Frankfurt Egelsbach airport (16 miles south of the city) for business aviation use, undertaking not to allow airline or indeed any scheduled operations there.

Demand from business aviation services on the air navigation system

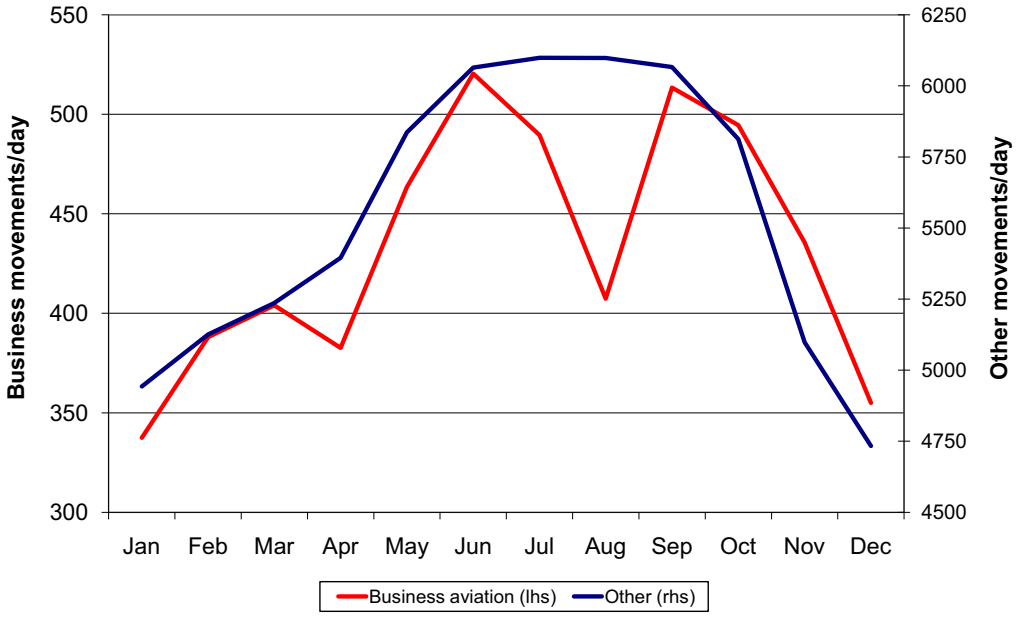
5.33 Although the number of passengers travelling on business aviation services is relatively small compared with that carried by commercial scheduled airlines, business aviation movements made up around 7% of all UK IFR flights (excluding overflights) in 2008. Business aircraft operating IFR exert very different demands on air navigation services than airlines because of their particular demand and supply characteristics:

- difference in monthly, daily and hourly traffic patterns;
- the ad hoc nature (in terms of volume and direction of flows) of their demand;
- the uneven and wide distribution of traffic among smaller airports with different take-off/landing trajectories from those at the nearby major airports;
- difference in aircraft size (hence require greater separation from other flights during landing/taking-off for wake vortex reasons).

96. *Traffic Distribution Rules 1991 for airports serving the London area.*
97. For 2008/09 at Heathrow in both Summer and Winter seasons and at Gatwick in Summer, there are very few periods on weekdays not defined as 'peak'.

5.34 Figure 5.7 shows the UK's IFR traffic patterns by month in 2007 and highlights the twin-peak demand characteristic of business aviation during June and September that differs from the Easter and summer holiday trends of the other non-business aviation traffic.

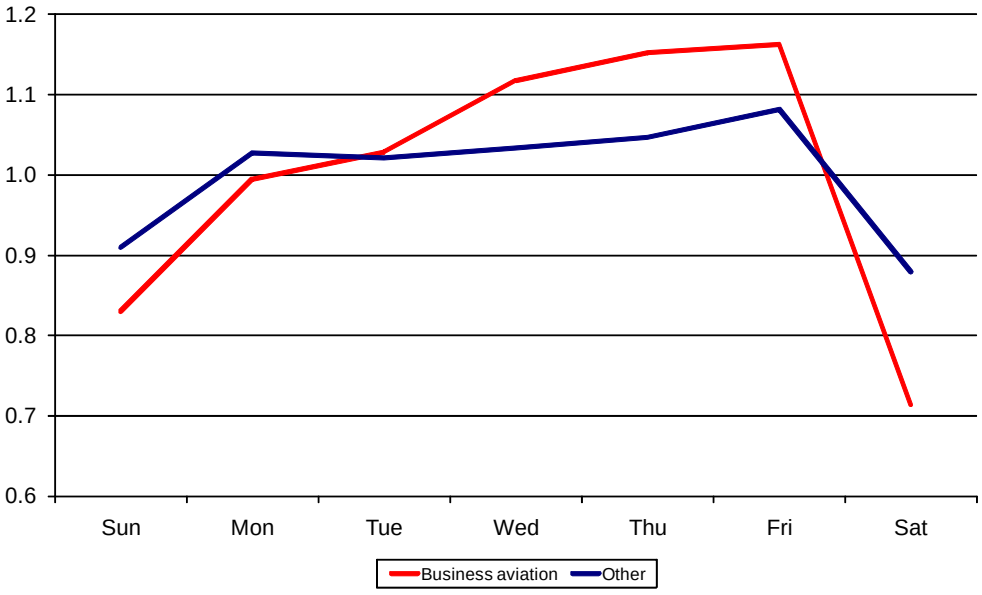
Figure 5.7 Monthly business aviation and other movements per day in UK, 2007



Source: Eurocontrol.

5.35 In terms of the daily traffic pattern, Figure 5.8 shows that there is no significant difference between business and other movements except that business traffic tends to build up more towards the end of the working week than other traffic before falling off sharply over the weekends.

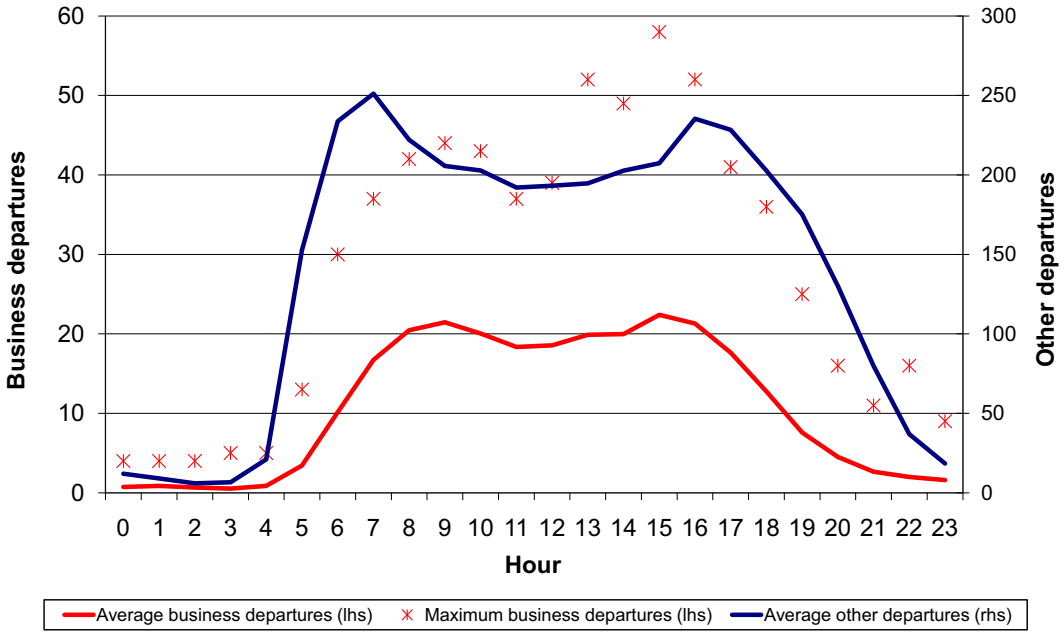
Figure 5.8 Daily business aviation and other departures in UK, 2007 (average over week = 1)



Source: Eurocontrol.

5.36 However, the hourly demand is quite different between the two traffic segments with business aviation movements clustering within a narrower time band, peaking at a slightly later morning hour (between 08.00–09.00) and earlier afternoon hour (between 15.00–16.00) than other flights, as highlighted in Figure 5.9. The maximum business aviation departures during the day can be more than double the average hourly pattern as shown.

Figure 5.9 Hourly business aviation and other departures in UK, 2007



Source: Eurocontrol.

5.37 Business aviation movements are a relatively small volume compared with other flights. However, because of the nature of the demand and flight operation characteristics, business aviation presents different challenges from commercial scheduled air transport services in terms of air traffic management.

5.38 Figures 5.7 to 5.9 above show that business aviation can generate more and bigger peaks (often at short notice) compared with scheduled traffic at some airports. The spread of business aviation traffic to smaller airports (such as Farnborough or Biggin Hill around London) and their high variability in terms of traffic volume and direction of flows could add further complexity to the management and planning of airspace usage, particularly in or near an already congested airport such as those serving the Greater London area. This in part is due to the increased likelihood of conflicting alignments of flight trajectories during take-offs/landings between business aviation flights at these smaller airports and flights using nearby larger airports. On the other hand, the wide range of business aircraft with various degrees of climb/descent capabilities flying over a spectrum of altitudes may help the management of airspace usage.

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Part 1 Annex 1.A List of no-frills carriers that operated at UK airports in 1996 and 2007

NFCs in 1996	NFCs in 2007
AB Airlines	Air Berlin
Debonair	Air Southwest
easyJet	Atlantic Express
Ryanair	Atlas Blue
	BA Connect
	Blue Air Transport Aerian
	Bmibaby
	Centralwings
	Clickair
	easyJet
	easyJet Switzerland
	Flybe
	Flyglobespan
	Flyme Sweden
	Germanwings
	Hapag Lloyd Express
	Iceland Express
	Jet2.com
	Monarch
	NIKI
	Norwegian Air Shuttle
	Ryanair
	SkyEurope
	Sterling Airlines
	Thomsonfly
	Transavia
	Tuifly
	Volare
	Wizz Air

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Part 1 Annex 1.B List of 'primary' airports used in this study

Country	Airport Name	IATA Code
Austria	Vienna	VIE
Belgium	Brussels	BRU
Bulgaria	Sofia	SOF
Cyprus	Larnaca	LCA
Czech Republic	Prague	PRG
Denmark	Copenhagen	CPH
Estonia	Tallinn	TLL
Finland	Helsinki	HEL
France	Paris (CDG)	CDG
France	Lyon	LYS
Germany	Berlin (Tegel)	TXL
Germany	Cologne	CGN
Germany	Dortmund	DTM
Germany	Dusseldorf	DUS
Germany	Frankfurt	FRA
Germany	Hamburg	HAM
Germany	Munich	MUC
Germany	Stuttgart	STR
Greece	Athens	ATH
Hungary	Budapest	BUD
Irish Republic	Dublin	DUB
Italy	Milan (Malpensa)	MXP
Italy	Naples	NAP
Italy	Rome (Fiumicino)	FCO
Italy	Turin	TRN

Country	Airport Name	IATA Code
Latvia	Riga	RIX
Lithuania	Vilnius	VNO
Luxembourg	Luxembourg	LUX
Malta	Malta	MLA
Netherlands	Amsterdam	AMS
Poland	Katowice	KTW
Poland	Warsaw	WAW
Portugal	Lisbon	LIS
Romania	Bucharest	OTP
Slovak Republic	Bratislava	BTS
Spain	Barcelona	BCN
Spain	Madrid	MAD
Spain	Valencia	VLC
Sweden	Stockholm	ARN
Turkey	Adana	ADA
Turkey	Ankara	ESB
Turkey	Bursa	BTZ
Turkey	Istanbul	IST
Turkey	Izmir	ADB
UK	Birmingham	BHX
UK	Glasgow	GLA
UK	London (Heathrow)	LHR
UK	Leeds/Bradford	LBA
UK	Liverpool	LPL
UK	Manchester	MAN

Note: For the purpose of this study, 'primary' airports are defined as the 40 airports with the highest passenger throughputs within each of the 40 largest urban zones (LUZ) as classified by Eurostat (Urban Audit), based on resident population in 2004 in the EU-27 countries plus Turkey, Norway and Switzerland. The largest airport in each of the capital cities of these EU-27 plus three countries is also considered as a 'primary' airport (if it is not in the group of the 40 largest LUZ). Thus, Heathrow is considered as the 'primary' airport within the London area while Gatwick, Stansted, Luton and London City are classified as 'non-primary' airports.

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Part 2 December 2010 – Analysis of the UK Business Air Travel Market

Executive Summary of Part 2

Business air travel supports, and is supported by, international trade

1 This report forms Part 2 of a CAA study of business air travel. Part 1, which the CAA published in May 2009, was largely based on an analysis of the CAA's statistical and survey data. Part 2 develops the analysis further, drawing on factual information from published sources and interviews. It considers the underlying drivers for business air travel, including the effects of the recent economic downturn, and past and future trends.

2 Business air travel supports, and is supported by, international trade. The increasing reliance of the UK economy on international trade in both goods and services, particularly financial services, has resulted in continued growth in business air travel and the expansion of UK air services in terms of destinations and frequency. It also means that business air travel has become more dependent over time on the economic development of the UK's trading partners and other emerging markets. The CAA's econometric analysis on the latest UK data supports the results of previous studies on the UK and other air markets, which show that GDP is the most significant factor in determining demand for business travel, with international trade and air fares making a lesser contribution.

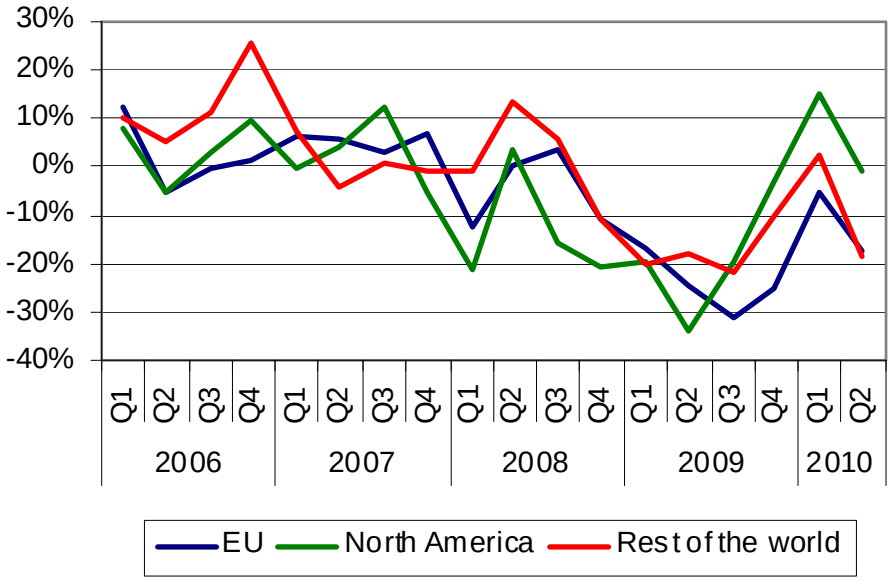
3 For many organisations, travel by employees is an integral part of doing business. This report also considers how organisations procure and manage that travel, and how airlines compete to provide it.

The effect of the recession on demand for business travel

Too early to tell whether there will be lasting effects on demand, but companies are more aware of the potential savings from better travel planning

4 The economic crisis had a huge impact on business air travel. As trade declined, so did demand for the travel that facilitates that trade. Part 1 of this study recorded the early signs of this decline. International business air travel to/from the UK fell by 4.6% in 2008 and 22.2% in 2009. The biggest declines in 2009 were between the UK and the EU (25%), and between the UK and North America (20%) as a result of the financial sector having been particularly badly hit (Figure 1). More recent data shows signs of business travel recovering, but because of disruption caused by the volcanic eruption in Iceland, the figure for the first half of 2010 remained 28% below the same period in 2008.

Figure 1 Year-on-year growth in business passengers to/from the UK, 2006–2010



Source: International Passenger Survey, ONS.

Note: Data exclude domestic and international-to-international connectors.

5 The CAA's econometric analysis suggests that there has been a 'step down' in demand as a result of the recent recession, over and above that which would have been expected from the observed changes in GDP, trade or fares. However, it is still too early to tell whether there will be any lasting effects on business travel from the economic downturn. There is no evidence to suggest that relationships between business travel and some major demand drivers have altered. Therefore, other things being equal, the trends of continuing globalisation, more trade and revived economic growth should continue to drive business travel by air.

6 Of course, company travel policies and the behaviour of business passengers continue to evolve. Some trends are driven by technological change and corporate cost efficiency initiatives. But the economic downturn has focused companies more clearly not only on whether there is a need for employees to travel, but also on smarter travel planning and the potential savings that can be achieved from better travel management, including the use of cheaper fare options. One effect is that the proportion of business passengers travelling in premium cabins continues to decline, in both long-haul and short-haul markets. The decline in business passengers using short-haul premium cabins is particularly marked, having reduced from 41% in 1996 to just 5% in 2009 on routes from London (Table 1).

7 Some elements of tighter company travel policies seem likely to remain even as the economy recovers. As load factors and yields gradually strengthen, the challenge for airlines is whether the greater focus on company travel costs is maintained, and whether yields return to pre-recession levels. There seems to be a general acceptance that demand for Business Class on short-haul trips will never recover; a structural shift was already occurring. Public sector spending cuts could have a significant impact as this was previously an important and growing sector of business travel.

Table 1 Proportion of business passengers travelling in different cabin classes on flights to and from London airports

Class of Travel	How much of each cabin is filled by business passengers?			Which cabin do business passengers use?		
	1996	2007	2009	1996	2007	2009
North America						
First/Business	82%	77%	59%	38%	27%	16%
Premium Economy	n/a	57%	42%	n/a	14%	17%
Economy	27%	20%	17%	62%	59%	67%
Other Long-haul						
First/Business	74%	75%	58%	33%	24%	13%
Premium Economy	n/a	59%	29%	n/a	8%	8%
Economy	27%	18%	16%	67%	67%	79%
Short-haul Int'l						
First/Business	93%	81%	68%	41%	9%	5%
Economy	50%	27%	23%	59%	91%	95%

Source: CAA Passenger Survey, 1996, 2007 and 2009.

Note: Only Heathrow, Gatwick, Stansted and Luton are included, as London City was not surveyed in these years.

Managing business air travel

Choice is influenced by company travel policy and negotiated volume discounts, but employees are also increasingly encouraged to choose 'best fare on the day'

8 Winning new business and maintaining customer relationships are key reasons for business travel, but internal meetings can also be a significant component. As well as focusing on more cost-effective travel, organisations are implementing more coherent travel policies taking into account staff well-being, efficiency and remuneration. Travel policies may be ineffective, of course, unless organisations are able to enforce them effectively.

9 The individual traveller's choice of travel is primarily determined by an amalgam of convenience (schedule, airport, or reliability), cost and ancillary services. However, personal benefits from a frequent flyer scheme can also be a significant influence and potentially work counter to company travel policy.

10 It is relatively common for companies with sufficient buyer power to negotiate directly with airlines for volume discounts tailored to their travel requirements. The level of discount varies, but can be substantial. Discounts are generally provided up-front, based on projected volume measured in terms of revenue or market share (a significant change compared with the beginning of the decade, when some, although not all, airlines were likely to give discounts retrospectively based on total spend). Companies typically contract with multiple airlines to give the necessary choice and route coverage, although this potentially dilutes the volume achieved with any single airline. Increasingly, companies have also encouraged employees to consider what other fare options are available 'on the day'. On shorter trips air travel has become

more commoditised; the choice of product is more dependent on price than on other differentiating features, benefits and value-added services, and travel has become more like other procurement items.

11 Businesses with significant travel spend are increasingly likely to employ dedicated managers overseeing travel policy and procurement, and may also employ a travel management company (TMC). TMCs have evolved from travel agents specialising in selling and booking business travel on behalf of airlines to travel consultants providing companies with a wide range of travel services, including advice on travel policy and procurement, and provision and analysis of management information. The three biggest TMCs in the UK each have annual business travel revenues of around £1bn.

12 Cost pressures, exacerbated by the effects of the economic downturn, have required TMCs to show that the value they add in terms of services and achieving savings in travel budgets outweighs any additional costs. The TMC's role is increasingly one of travel consultant. Complex remuneration arrangements are based mainly on client management fees, transaction fees and 'gainshare' agreements, giving TMCs relative independence from airline suppliers; the old system of airline commissions and incentive payments has largely been replaced. TMCs also use their buyer power to negotiate airline fares based on volume discounts, which TMCs can then on-sell to companies.

Airline competition for business passengers

Continued evolution of cabin products on long-haul services and structural change away from premium products in the provision of short-haul services

13 Many airlines target business passengers as a high-yielding source of revenue, whether they be in premium or economy cabins. However, business travel demand can sometimes be volatile, and bookings tend to be made at short notice. Attracting leisure passengers (and for hub airlines, connecting traffic) brings stability and supports more frequency, which is valued by business passengers (a virtuous circle). The ability of airlines to attract business traffic, and in particular corporate contracts, is greatly influenced by the scope of its network and relative frequency of flights. Consequently, many long-haul airlines believe their offering is more competitive if their network is effectively broadened through alliance membership.

14 The business passenger's historic preference for convenience and quality has led to the evolution of high quality Business Class products on long-haul routes, with a flat bed now regarded as the minimum standard for longer or overnight Business Class flights. This in turn has created a niche for a Premium Economy cabin for business passengers. It also offers the possibility of mixing Business Class in one direction with Premium Economy in the other, depending on schedule or other considerations, and can therefore be a useful part of the proposition by airlines to attract corporate custom.

15 A wider range of Business Class fares has evolved on long-haul services. Many of them have conditions which require booking in advance and a Saturday-night minimum stay. Although these may give a wider range of 'best fare on the day' options to cost-conscious business passengers, they have also encouraged greater use of the Business Class cabin by leisure passengers.

16 Three new entrant all-Business-Class long-haul airlines failed as the financial crisis developed. Some European network carriers have successfully adopted such a model, but only BA currently operates such a service from the UK.

17 On short-haul routes, no-frills airlines have made significant inroads into the business market. For example, in the two biggest short-haul business markets, CAA survey data shows that easyJet has around a quarter of the London–Amsterdam business market and Ryanair more than a third of London–Dublin (excluding any passengers connecting at either end). Changes in fare structures following the entry of no-frills airlines have brought cheaper fares within reach of business passengers as price discrimination barriers, in particular the Saturday-night minimum stay, have fallen away – in contrast to long-haul routes. Many short-haul airlines have 'unbundled' their product, allowing them to offer the lowest possible fare while charging for ancillary items such as meals and hold baggage. This can cause problems for TMCs in terms of comparing fares and managing booking information until the technology of the GDS systems TMCs use for making bookings catches up.

18 Although some airlines still perceive demand for a premium short-haul product, it seems to be generally accepted that the recent decline in the use of Business Class, accentuated by the economic downturn, is a permanent structural change.

Future trends

Outlook for UK business air travel dependent on how national economies fare, including those of emerging markets trading with the UK; improved communications technology, rail alternatives and environmental considerations may have some dampening effect

19 The outlook for UK business travel will largely depend on the sustainability of the world and UK economic recoveries. The rapid economic growth of some emerging markets (particularly the BRIC and the 'Next 11' countries[98]) is expected to become an increasingly important driver for business air travel to and from the UK over time. However, the EU and US will remain the most significant markets for UK business travel for the foreseeable future. The UK Government's public spending cuts, and associated reductions in public employment and administrative costs, are likely to have a direct dampening effect on business air travel demand.

20 Better international communication technology – in particular videoconferencing – is often considered likely to diminish demand for business air travel, particularly where companies are more conscious of environmental concerns. However, where external clients are involved, companies are loathe to replace face-to-face meetings with videoconferencing. So it may be that the greatest effects are on meetings within companies that would once have required travel.

21 However, the more that international communication technology advances, the more it facilitates a greater pace of globalisation, which in turn increases demand for business air travel. Indeed, making communication easier between distant locations can actually open up new business opportunities, while the ability for employees to use communications technology to work remotely from the office may reduce any disadvantages of business travel in terms of productivity.

22 There is likely to be increased focus from businesses on the environmental issues. However, the likely impact on business travel is unclear. For many organisations, travel makes up a small proportion of their overall carbon emissions. Furthermore, those organisations where it does form a more significant proportion are generally service-oriented companies, where business travel is client-focused – and may therefore continue to be considered a necessity. Businesses are therefore likely to focus more on mitigation of greenhouse gas emissions related to travel through activities such as offsetting, and an increased pressure on airlines to reduce such emissions where possible.

98. The BRIC countries are Brazil, Russia, India and China. The 'Next 11' countries are Bangladesh, Egypt, Indonesia, Iran, South Korea, Mexico, Nigeria, Pakistan, the Philippines, Turkey and Vietnam.

23 The success of rail services in winning short-haul business passengers looks likely to continue as high-speed services improve and some company travel policies divert travel away from air on environmental grounds. However, significant diversion is likely to be confined to the shortest routes, because of the importance of journey time to business travellers.

Summary

Provision of business air travel has responded to economic, technological and market changes, and is likely to continue to do so; underlying need for travel for business purposes is likely to persist

24 The airline products available to business travellers to and from the UK, the demands of those travellers and their companies, and the means by which business travel is purchased and monitored have all seen significant changes over the last 25 years. These changes have come about as a result of technological advances, liberalisation of aviation and travel supply markets, and development of the UK economy and its trading patterns.

25 The recent recession has seen a decline in the number of passengers travelling for business purposes at UK airports, and the accentuation of existing trends towards cost-consciousness in companies' travel arrangements. However, the need to travel for business purposes in order to meet current and prospective customers, and, increasingly, to manage the disparate parts of global organisations, is likely to persist, whatever the future brings.

Part 2 Chapter 1 Introduction to Part 2

1.1 Business travel by air supports and is supported by international trade. In the UK, growth in the number of passengers travelling for business purposes[99] has gone hand-in-hand with the expansion of air routes and frequencies, and the increasing reliance of the UK economy on international trade in both goods and services, particularly financial services.

1.2 In May 2009, the CAA published Part 1 of this study on the UK business travel market – UK Business Air Travel: Traffic Trends and Characteristics – which examined how UK business traffic has changed by sector (long haul, short haul and domestic) between 1996 and 2007, and the characteristics of its passengers. It also looked at the expansion of the Business Aviation sector, which provides on-demand air services using small business aircraft, typically with less than 15 seats.

1.3 Part 2 of this study further develops the analysis from Part 1. Part 2 starts with a closer examination of the impacts of the recent recession, before looking at the broader trends and drivers of change in both the demand and supply for business travel. It also examines the way companies manage their business travel, the changing role of travel management companies (TMCs), how airlines compete for and value business travellers, and factors that may affect the future demand for UK business travel.

Structure of Part 2 of this study

1.4 The structure of Part 2 of this study is as follows.

1.5 Chapter 2 examines the effects of the recent recession on UK business travel volumes, developing the analysis from Part 1 of the study. It also examines the reactions of businesses, travel management companies and airlines, and looks at the short term prospects for business air travel in the UK.

1.6 Chapter 3 discusses the economic and other drivers for business travel by air in the UK, and investigates whether the recent recession is likely to cause these to be different in the future than in the past.

1.7 Chapter 4 considers motives for UK business trips requiring travel by air, how businesses manage that travel, including through staff travel policy, the deals that businesses negotiate with airline suppliers, and what drives and constrains the choices that individual travellers make.

1.8 Chapter 5 looks at TMCs in the UK, which have changed from travel agents specialising in selling and booking business travel on behalf of airlines to travel consultants providing companies with a wide range of travel services, including advice on travel policy and procurement, and the provision and analysis of management information.

1.9 Chapter 6 examines UK business travel from the perspective of airline suppliers. It considers the significance of the business market to airlines, the effects of market liberalisation, the development of in-flight products on long-haul and short-haul services, and how airlines' pricing strategies have changed. The discussion includes consideration of the niche all-Business-Class airline model, the adoption by some airlines of a new Premium Economy cabin, the entry of no-frills[100] airlines and the

99. The definition of business passengers used for the purposes of this study appears in the Explanatory Note at the beginning of the document.

network airlines' competitive reactions, and the effect on business travel of trends such as the use of brand loyalty schemes and the practice of 'unbundling' fares to offer the lowest basic price.

1.10 Chapter 7 looks at the likely future of UK business air travel. While it is still expected to be strongly related to economic growth and trade, prospects for the UK market will also be influenced by other factors such as the extent of globalisation, rapid growth of emerging markets, further development in information and communication technologies, rising concerns for the environment and corporate social responsibilities, and increased competition from rail.

100. For a list of airlines categorised as 'no-frills', see Part 1 of this study, Annex 1.A. The term 'no-frills' is used for convenience here to distinguish these airlines from network airlines, but it is accepted that they offer some 'frills', albeit at extra cost.

Part 2 Chapter 2 Impact of the recent recession on UK business air travel

Chapter summary

- International business air travel to and from the UK fell by more than 22% in 2009, following a 4.6% reduction in 2008. The rate of decline slowed in the first half of 2010, although total business air travel was still 28% below its level in the same period in 2008.
- Business traffic between the UK and the EU region fell by 25% in 2009, while business traffic between the UK and North America and between the UK and the Rest of the World were 20% and 17% lower respectively in 2009 compared with 2008. At the London airports, the biggest reduction in business travel between 2009 and 2007 was in the domestic market (25%), followed by the short-haul and the long-haul markets.
- Average business fares (the average for all business passengers irrespective of which cabin they travel in) fell during 2009. The biggest decline was in average business fares to North America which fell by almost 15% in 2009 (increasing by 4.6% in the first half of 2010). Short-haul business fares appeared to have held up relatively well during the recent recession, with only a 2.5% reduction in 2009.
- The economic downturn reinforced companies' focus on cost-effective travel. Some companies badly affected by the recession made dramatic cuts in travel (both in terms of trips and the value booked). Some elements of tightened company travel policies seem likely to remain once the economy recovers. The proportion of business passengers travelling in premium cabins continued to decline in both the long- and short-haul markets, and there seems to be a general acceptance that demand for Business Class on short-haul trips will never recover; a structural shift that was already observable before the recession.
- Airlines experienced a significant decline in volume and yield and found it hard to predict the form and timescale of recovery. As load factors and yields gradually strengthen, the challenge for airlines is whether the greater focus on company travel costs is maintained, and whether yields return to pre-recession levels.
- The short-term outlook for UK business travel will largely depend on the sustainability of the world and UK economic recoveries. Although the robust recovery in Asia and some other emerging economies will further drive UK business travel to and from these markets, the EU and US will remain the most significant markets for UK business travel in the foreseeable future.

Introduction

2.1 Part 1 of this business travel study, published in May 2009, reported that UK business travellers were seeking cheaper alternatives to First and Business Class travel between 1996 and 2007, particularly in the short-haul market. It also noted that the recession (which was then only just beginning) had a significant impact on business travel in the final quarter of 2008 and early 2009.

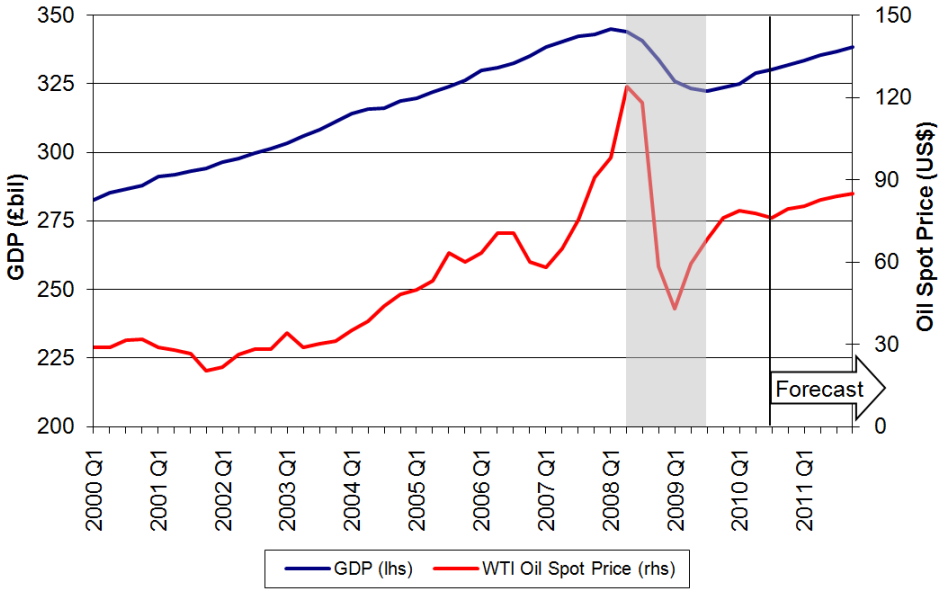
2.2 This chapter gives an updated account on how the recent recession has affected UK business air travel so far. It describes the events leading up to and during the recent recession, the effect on aviation and business travel in particular, the way business and the aviation industry responded to these events and finally assesses the short term outlook for UK business air travel.

2.3 In general, recessions affect business and leisure traffic through different mechanisms and at various speeds. As will be shown in Chapter 3, demand for business travel, like business activities, is highly conditioned by the economic environment. If the overall level of trade (particularly international trade) changes, then so does the requirement for travel to meet customers, and potential customers. Also, in an economic contraction, companies may swiftly cut their 'discretionary' travel budget and enforce travel policy restrictions to reduce costs, while leisure travel may be affected in a more lagged way, as the impact of a downturn takes a longer time to work through the real economy before consumers 'feel' poorer (or lose jobs). Bookings by business travellers tend to be made closer to the date of the flight than those of leisure passengers and are more likely to be changed prior to departure. It is also less easy for airlines to stimulate business than leisure travel demand through lower fares, and leisure passengers are more flexible to choose cheaper alternative destinations, thereby reducing travel spend but keeping numbers of leisure travellers up.

The recent economic crisis and recession

2.4 The recent economic crisis, triggered by the credit crunch beginning in 2007, weighed heavily on the airline industry, which was already under cost pressure from a long period of rising fuel prices. Figure 2-1 shows how the economic recession was preceded by the rapid rise of oil prices since 2002 that peaked at around US$145 per barrel in early July 2008. Although the West Texas Intermediate (WTI) spot oil price stabilised between US$72 and $84 per barrel between October 2009 and October 2010, the upward trend is expected to re-emerge as the global economy continues to recover.

Figure 2-1 Actual and forecast of spot oil price (in US$) and UK GDP (in 2006 prices)



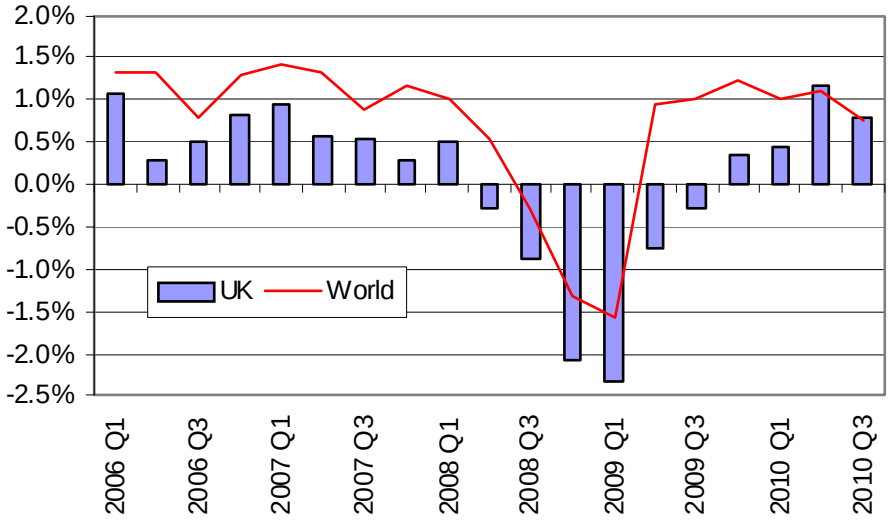
Source: Office for National Statistics (ONS), Consensus Forecasts and US Energy Information Administration.

Note: GDP (in 2006 prices) is seasonally adjusted and in chained volume measures.

2.5 Fuel costs increased from around 10% of UK airlines' total operating costs in the mid-90s to more than 30% in 2008/09 and became the largest and most unpredictable component of operating cost outside airlines' direct control.[101] In response to increased pressure on yields due to rising oil prices, airlines sought to increase their fuel surcharges or raise ancillary revenues from other add-on services.

2.6 Figure 2-2 shows the quarter-on-quarter growth in the UK and world economies since 2006. The economic crisis began in late 2007, as the slowdown in the US housing market affected US providers of 'sub-prime' mortgages. By 2008, uncertainty over the extent to which global lenders were exposed to sub-prime losses led investment and retail banks to require capital support from governments.[102] By early 2009, interest rates were reduced to historically low levels (0.5% in the UK) and many governments had implemented stimulus packages to mitigate the worst effects of the recession, followed in 2010 by significant cuts in public spending among many European countries, while both Greece and Ireland required emergency loans from the EU and the International Monetary Fund (IMF).

Figure 2-2 Quarter-on-quarter UK and world GDP growth 2006 to 2010



Source: ONS and IMF.

2.7 Following a sharper fall in UK national output than experienced in previous post-war recessions, in November 2010 the UK Office for Budget Responsibility (OBR) revised its UK GDP growth forecast for 2010 upward from 1.2% in June to 1.8%.[103] However, its GDP forecast for 2011 was revised downward from 2.3% to 2.1%, partly because the rebound was considered largely a timing effect due to firms rebuilding stocks, and partly as a result of the increase in VAT to 20% due in January 2011. The OBR noted that there was considerable uncertainty around any central economic forecast at this time, with a number of significant risks both to the upside and to the downside, and it judged that growth was as likely to exceed its central projection as it was to fall short.

101. Fuel hedging by airlines normally only provides some price cover up to 12 months or so ahead.
102. For example, in October 2008 the UK Government injected £37bn into banks RBS, LloydsTSB and HBOS, taking a significant shareholding in return.
103. Office for Budget Responsibility: *Cm7979 Economic and Fiscal Outlook* (November 2010).

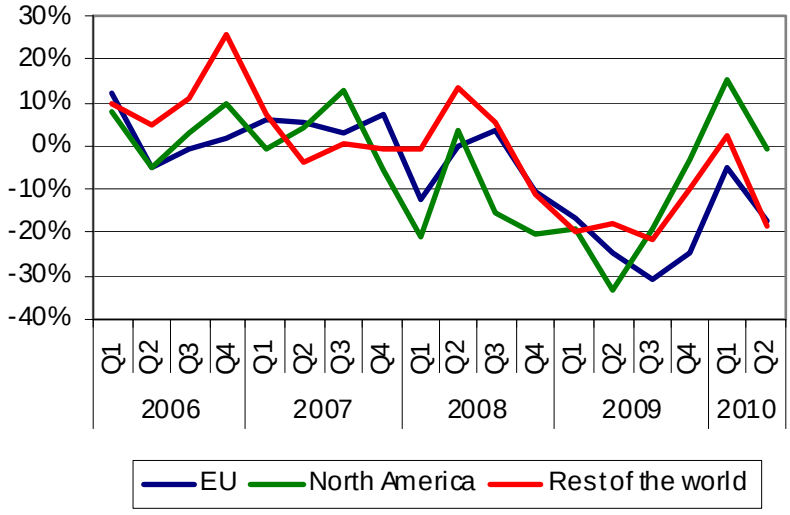
Impact of the recession on volume of UK business travel

2.8 The recent global recession has had a significant impact on international business air travel to and from the UK, which fell by more than 22% in 2009, following a 4.6% reduction in 2008.

Impact on business air travel by geographic region

2.9 Figure 2-3 highlights the impact of the recent economic downturn on international business air travel to and from the UK by geographic region. Business traffic began to fall in late 2007 and early 2008 with the North America business market being hardest hit by the financial crisis. As the global economy began to recover, the decline in traffic slowed, with the North America business segment first to return to growth. However, the pace of traffic recovery appeared to have stalled in the second quarter of 2010 across all three geographic markets, partly due to the volcanic eruptions of Eyjafjallajökull in Iceland that caused disruption to air travel across western and northern Europe over a period of six days in April 2010.

Figure 2-3 Business air passenger (year-on-year) growth to and from the UK, 2006–2010



Source: International Passenger Survey, ONS.

Note: Data exclude domestic and international-to-international connectors.

2.10 Table 2-1 shows that total UK–international business air traffic fell by more than 22% in 2009 following a 4.6% reduction in 2008. The declining trend appeared to be slowing down in the first half of 2010 as the global economy continued to recover. Among the three broad geographic markets, business traffic to and from the EU has suffered the most from the downturn so far, with a drop of 24.5% in 2009 and a further decline of more than 11% in H1 2010. This is likely because the recession has had a greater impact on the EU economy than on that of North America and the Rest of the World, and its economic recovery has also been more protracted by comparison. Despite an increase of 6.5% in business travel to North America in H1 2010 compared with the year before, this segment was still 23% below its pre-recession level of H1 2008. Likewise, the overall volume of business travel to and from the UK in the first half of 2010 remained 28% lower than in H1 2008.

Table 2-1 Growth of business air passengers to and from the UK by geographic area

	EU	North America	Rest of the world	Total
2007	5.3%	2.2%	0.6%	3.7%
2008	-5.2%	-13.2%	1.1%	-4.6%
2009	-24.5%	-20.2%	-17.3%	-22.2%
H1 2010 v 2009	-11.6%	6.5%	-8.6%	-8.8%
H1 2010 v 2008	-30.2%	-22.9%	-25.8%	-28.2%

Source: International Passenger Survey, ONS.

Note: Data exclude domestic and international-to-international connectors.

Impact by traffic sector at the London airports

2.11 The economic downturn has had a differential impact by traffic segment at the London airports. Table 2-2 shows that the biggest reduction in business travel between 2009 and 2007 at the London airports was in the domestic market (25%), followed by the short-haul and the long-haul markets.[104] This was in part due to increased competition from rail as environmental considerations and improved services by rail companies have enhanced its appeal to corporate travellers.

Table 2-2 Distribution of business passengers by sector at London airports

Airport	2009 (millions)				2009 v 2007 (% change)			
	Domestic	Short haul	Long haul	Total	Domestic	Short haul	Long haul	Total
Heathrow	2.0	9.4	7.9	19.2	-30%	-25%	-12%	-21%
Gatwick	1.4	2.9	0.5	4.8	-11%	-12%	-65%	-23%
Luton + Stansted	1.2	3.7	0.03	4.9	-28%	-23%	-74%	-25%
London City	0.4	1.2	0.0	1.6	-33%	-11%	--	-15%
Total London	**5.0**	**17.1**	**8.4**	**30.5**	**-25%**	**-22%**	**-19%**	**-22%**

Source: CAA Passenger Survey, 2007 and 2009.

Note: Figures for London City have been scaled up from 2006 and 2008 surveys respectively.

2.12 Despite its strong attraction for business traffic, Heathrow appeared to have suffered almost as much as Gatwick, Stansted and Luton with a 21% reduction in its overall business traffic, although the impact was felt more in its domestic and short-haul markets than in its long-haul traffic. This contrasts with Gatwick which had lost a significant proportion of its long-haul business passengers (65%) in 2009 compared with 2007, while there was only a relatively modest decline in its domestic and short-haul business traffic. However, this period also saw the implementation of the EU-US Open Skies agreement, which allowed some US carriers to switch their transatlantic operations from Gatwick to Heathrow, whereas easyJet, Flybe and Ryanair all increased their presence at Gatwick. Consequently, total long-haul traffic at Gatwick fell by over 30% between 2007 and 2009, while short-haul and domestic traffic increased by 1.5% (not shown in Table 2-2). At the same time, reduced capacity by easyJet and Ryanair at Luton and Stansted airports over this period has had a

104. A similar breakdown by traffic segment for the regional airports is not possible since some of these airports were not surveyed by the CAA between 2007 and 2009.

significant impact on these two airports. London City appeared to have had the least overall impact among the London airports, reflecting its stronger appeal to short-haul business travellers than the other London airports, although its domestic business traffic fell by a third between 2007 and 2009.

Impact on premium traffic

2.13 While the volume of UK business traffic has declined across all geographic markets, the fall in demand and revenue from premium passengers is significant for network airlines, as these passengers generate more revenue per head than non-premium travellers. Table 2-3 shows that, on IATA airlines worldwide, premium-class travellers in 2008 paid, on average, around three to four times more than economy passengers on the same aircraft, albeit they represented less than 10% of the total passengers on board. Thus, the absence of these higher yield business passengers could have a significant bearing on whether a flight is profitable or not for many traditional network carriers.

Table 2-3 Premium traffic and revenue share by region and ratio of average yield between Premium and Economy class travellers on IATA airlines worldwide

Region	Traffic volume	Revenues	Premium/ Economy Class yield ratio
Africa	7.5%	24.4%	4.0
Asia	6.5%	18.4%	3.2
Australasia	7.5%	22.0%	3.5
Central America	8.0%	14.4%	1.9
Europe	7.6%	26.5%	4.4
Middle East	7.6%	32.3%	5.8
North America	6.6%	22.7%	4.2
South America	8.2%	20.3%	2.9
World	**7.1%**	**22.7%**	**3.8**

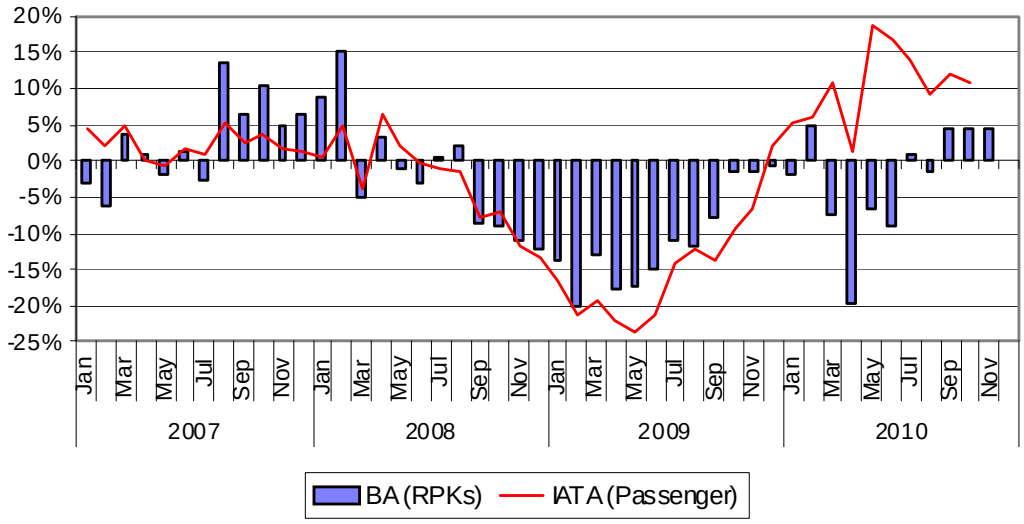
Source: IATA data and CAA calculation.

Note: Data based on one-way traffic from one region to another and within a region between January 2008 and October 2008.

2.14 Figure 2-4 shows the development of premium traffic by BA and IATA airlines since January 2007. International premium traffic as reported by IATA recovered steadily from early summer 2009 and expanded by a strong 18.7% in May 2010 after disruption from the Icelandic volcanic eruption[105] in April and before slowing to 9% growth in August. Despite the upturn in demand for premium travel, which grew by 9.2% in the first ten months of the year, the rebound in traffic is against the low levels of 2009. Indeed, premium traffic in October 2010 was still around 7% below its level in October 2007 and yields and average fares in October were still 13% to 14% below their pre-recession levels of October 2008 and October 2007 according to IATA.[106]

105. The Icelandic volcano Eyjafjallajökull erupted in early April 2010, which, combined with adverse wind directions, caused significant parts of EU airspace to be closed to all traffic for six days.
106. IATA: *Premium Traffic Monitor* (October 2010).

Figure 2-4 Premium traffic growth (year-on-year): BA versus IATA airlines

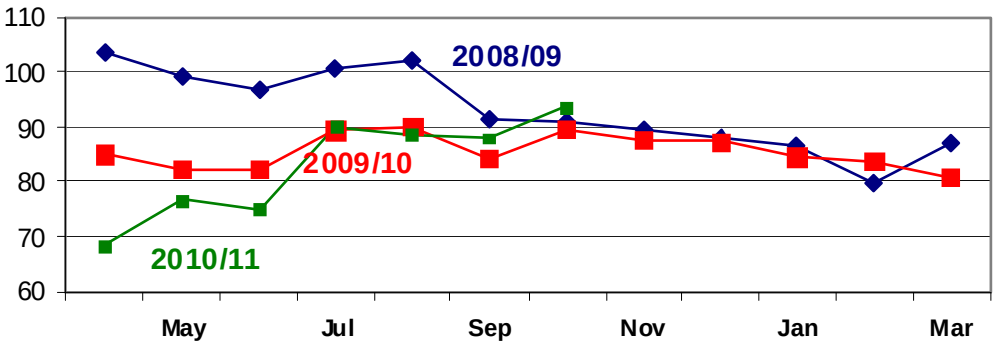


Source: BA and IATA.

2.15 There are also considerable geographical differences in the recovery. Of the large premium travel markets, IATA reported that routes linked to Asia and to the North and Mid Pacific continue to show strong growth rates compared with 2009, while the North Atlantic premium market is still lagging behind Asian and Middle East routes.

2.16 Since BA has a high exposure to the finance and banking sector, its premium traffic is considerably driven by the North Atlantic business market and is therefore conditioned by the economic environment and business activities in the UK, US and Europe which remain relatively subdued. Figure 2-5 indicates that BA's premium traffic in March 2010 (in terms of revenue passenger kilometres) was still around 20% below its pre-recession level in March 2008, leading BA to report an operating loss of £231m in 2009/10.[107] Despite an upturn of premium traffic since July and in particular a strong year-on-year growth in September and October, BA's premium traffic still remained around 10% below its 2007/08 level.

Figure 2-5 Indexed BA premium traffic volume (in revenue passenger kilometres) compared with 2007/08 base year



Source: BA.

107. The airline was also affected by the volcanic ash plume in April 2010 and industrial action during May and June.

2.17 The decline in traffic and yields in premium markets pre-dated the recent economic crisis and there have been concerns[108] that such trends might not be cyclical, but would become more permanent as a result of the economic downturn. Part 1 of this business travel study found that UK business passengers were increasingly seeking value for money and, in some cases, opting for cheaper alternatives to First and Business Class travel, and that no-frills carriers had been successful in capturing a significant share of the short-haul business market. Although this cost-cutting trend had occurred while business travel grew between 1996 and 2007, there is evidence to suggest that it has been further exacerbated by the recent recession, particularly in the short-haul business market. Table 2-4 shows the proportion of business passengers from the four London airports travelling in different cabin classes. f

Table 2-4 Proportion of business passengers travelling in different cabin classes on flights to and from London airports

Class of Travel	How much of each cabin is filled by business passengers?			Which cabin do business passengers use?		
	1996	2007	2009	1996	2007	2009
North America						
First/Business	82%	77%	59%	38%	27%	16%
Premium Economy	n/a	57%	42%	n/a	14%	17%
Economy	27%	20%	17%	62%	59%	67%
Other Long-haul						
First/Business	74%	75%	58%	33%	24%	13%
Premium Economy	n/a	59%	29%	n/a	8%	8%
Economy	27%	18%	16%	67%	67%	79%
Short-haul Int'l						
First/Business	93%	81%	68%	41%	9%	5%
Economy	50%	27%	23%	59%	91%	95%

Source: CAA Passenger Survey, 1996, 2007 and 2009.

Note: Only Heathrow, Gatwick, Stansted and Luton are included, as London City was not surveyed in these years.

2.18 The table indicates that the proportion of business passengers travelling in premium cabins continued to decline in both the long- and short-haul markets.[109] There was a further ten percentage-point drop in the long-haul markets between 2007 and 2009 while the proportion of short-haul business passengers travelling on business class tickets almost halved from 9% in 2007 to 5% in 2009 (compared with 41% in 1996).

108. See, for examples, comments by AEA and BA, as reported on: www.centreforaviation.com/news/2010/02/18/airline-structural-change-in-europe-at-a-major-turning-point--if-labour-allows-it/page1 and http://news.cheapflights.co.uk/2010/02/british-airways-calls-time-on-short-haul-ba-business-class/

109. As shown in the column headed 'Which cabin do business passengers use?'.

The table also seems to suggest[110] that, while some business travellers downgraded in long-haul markets, some leisure passengers may have traded up, since the proportion of leisure passengers in premium cabins increased substantially, particularly in 'other long-haul' markets.[111]

Response of the business travel market to the recession

Impact on business travel spend

2.19 In the course of this study, the CAA discussed the travel market with various travel management companies (TMCs) and large businesses. These discussions are more fully reported in Chapters 4 and 5, which deal with the way business travel is managed and the development and changing role of TMCs. This section concentrates solely on the reported effects of the recent recession on business travel spend.

2.20 The economic crisis had a huge impact on business air travel. The nature of much business travel is to meet customers and suppliers, for example to negotiate new contracts or to check on the progress of existing ones. As the amount of trade declines during a recession, the demand for such travel naturally falls. In the recent recession, where the financial sector was particularly badly affected, this had a significant impact on business travel, particularly transatlantic travel.

2.21 Company air travel policies and the behaviour of business passengers were already changing prior to the downturn, evidenced in the shift away from short-haul premium travel seen in Table 2-4. Some trends were driven by technological changes and a long-term focus by companies on cost efficiency. But the economic downturn focused companies more clearly not only on whether there was a need to travel, but also on smarter travel planning and the potential savings that could be achieved from better travel management.

2.22 As the downturn took hold, some badly affected companies made dramatic cuts in travel. For example, as business prospects receded in the financial services industry, so did travel. Large firms interviewed for this study reported a general fall in business trips of 15% to 25%, with spend reduced by anything up to 45%. The Guild of Travel Management Companies' quarterly transaction survey recorded 17% fewer air transactions among its members in 2009 than in 2007.[112] Certain kinds of travel – for example internal meetings, training, special events or conferences – were the first to be cut back. One large corporate told the CAA that 15% to 20% of its travel was for internal purposes and that 90% of such travel was cut in the first three months of the crisis. In a May 2009 survey,[113] albeit global, by KDS (a supplier of travel and expense management systems), 71% of respondents said that their companies had significantly reduced their business travel, around two thirds seeing this effect within the preceding six months,[114] and internal company meetings and training were the reason given for only 14% of trips.

110. In the column headed 'How much of each cabin do business passengers make up?'.
111. It should be noted that, given the contraction of total traffic in 2009, it is plausible that changes in the make-up of passengers in each cabin may reflect the relative reduction rates between leisure and business travellers rather than individual leisure and business passengers changing their travel habits.
112. See Figure 5-1 in Chapter 5. It should be recognised that GTMC membership covers around 80% of business travel spend in the UK and changes from year to year. Therefore such a comparison can only be regarded as an indication of the trend rather than an absolute.
113. The on-line survey covered 435 professionals across a range of company sizes. http://kds.com/resources/press-room/global-kds-survey-identifies-new-priorities-business-travel-industry-recession
114. In another 2009 survey, again global (American Express/CFO Research Global Business & Spending Monitor), 81% of respondents said they were likely to restrict travel for staff meetings while 79% said they would curtail attendance at conferences. In the same survey in 2010 these figures had reduced to 34% and 35% respectively. However only 13 of the 479 executives responding were based in Europe (ABTN 27 May 2010 – www.abtn.co.uk).

2.23 Some firms, for which travel remained essential to the functioning of the business, considerably reduced the value of travel booked, but with a smaller reduction in the number of trips made. This lower spend per trip was achieved in a number of ways, for example:

- By combining multiple meetings into one trip or permitting fewer team members to travel.
- By stricter enforcement of existing travel policy as rules rather than guidelines. This could mean less flexibility and more pre-trip approval for bookings 'out of policy', for example those exceeding the lowest/preferred supplier rate by a certain margin. This greater oversight slowed the booking process, but accelerated the use of technology for authorisation via the TMC.
- In some cases, pre-trip approval was required for any air travel, sometimes at senior management level. There was a requirement to justify what a trip would achieve for the company, creating an 'essential travel only' culture,[115] and the cost of a meeting for internal purposes was likely to be subject to more scrutiny than a meeting with a client.
- On short-haul services there was some downgrading of class of travel and/or shift to no-frills carriers, or to rail where this was cheaper, easier or newly dictated by travel policy.
- On long-haul services there was some downgrading of class of travel, in particular a trend to confine Business Class more strictly to long flights over a certain duration and/or overnight flights where a flat bed has more value. There was also greater use of Premium Economy,[116] perhaps mixing Business Class on one leg of a round trip with Premium Economy on the other leg.[117]
- There was more cost-conscious buying, in particular greater use of 'best fare on the day' (see Chapter 4 for further discussion of this concept) and conditioned fares generally. Hence, by implication, there was a greater willingness to adapt travel plans to meet the conditions of a lower fare[118] and to consider a wider range of airlines and airport options. (Arguably, the ability to secure lower prices may partially unwind as demand returns, depending on the competitive environment and the extent to which airlines are able to keep a check on capacity and to withdraw tactical fares or raise prices.)
- More planning ahead, allowing earlier booking to secure cheaper fares (to the extent that the reason for travel allows); this may have happened automatically where trips require a pre-approved business case well in advance of travel.[119]

115. This begs the question what constitutes 'non-essential' travel, but an example quoted from some years ago was the 'dot-com bubble', which reportedly generated "travel on a whim".
116. Albeit that not all airlines offer a Premium Economy cabin and the number of seats on those that do is limited. Premium Economy makes up only 7% of Carlson Wagonlit Travel's long-haul bookings and remained static for 2009, *Premium Bonds*, The Business Travel Magazine (May/June 2010).
117. This trend (from research for this study) is also identified in *Premium Bonds*, The Business Travel Magazine (May/June 2010). The article mentions Premium Economy being offered by airlines as part of a corporate deal, despite the potential loss of Business Class revenue, but also that airlines denied that business clients were amending their travel policy from Business Class to Premium Economy.
118. Where journey time is less of a consideration, an alternative cost-effective option is to travel indirect, changing planes en route, but in Business Class, thus securing both comfort and a lower price.
119. Institute of Travel Managers/Argate easyJet price comparison research, autumn 2009, showed that average lead times in the short-haul business market had significantly lengthened from two to three calendar days in 2008 to seven to nine calendar days in 2009. www.easyjet.com/common/img/easyJet_Price_Comparison_Results09.pdf

2.24 Table 2-5 shows the impact of the recession on business expenditure (excluding fares) by UK residents on overseas business trips by all modes of transport (sea, Channel Tunnel and air) and by air travel between 2005 and 2010. Expenditure (excluding fares) by UK residents on overseas business trips by air fell by 13% in 2009 with a further drop of 11% in the first half of 2010.

Table 2-5 Business travel spend (in £m) by UK residents on overseas trips

	All modes	% change	Air	% change
2005	4,611		4,105	
2006	5,067	10%	4,465	9%
2007	5,122	1%	4,556	2%
2008	5,319	4%	4,541	0%
2009	4,334	-19%	3,930	-13%
H1 2010	2,263	-7%	1,967	-11%

Source: ONS.

Notes: Modes of travel include sea, Channel Tunnel and air.

Spending excludes payments for air, sea and rail travel to and from the UK

2.25 There is general agreement that as the economy recovers, so will the volume of business traffic. Travel to meet clients in person is seen as essential to building and maintaining relationships and to securing future sales. This might be supported by travel for internal meetings, which itself could be a good barometer for the return of business travel more widely.

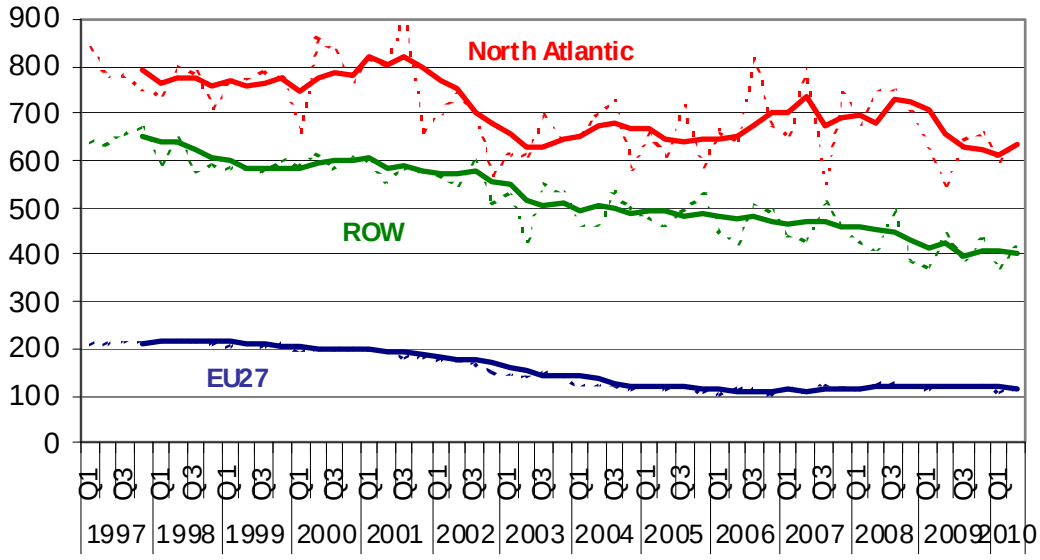
2.26 At the time of writing there are mixed reports about travel restrictions being relaxed and how long this might take. It has been suggested that sales teams and more senior staff have begun travelling again in order to bring in new business, but that other forms of business travel, associated with delivery of the actual product or service being sold, have yet to recover. Another view is that the effects are likely to be industry-specific; for example, some industries, such as engineering, may be more likely to see Business Class as an extravagance and to use Economy or Premium Economy, whereas in sectors like financial services, Business Class travel is considered the norm and the uncertainty is around the volume (and possibly price) rather than class of travel.

Impact on average fares paid by passengers on business travel

2.27 The decline in business travel demand had a significant impact on many airlines, both full service and no-frills, as business passengers are more willing than leisure travellers to pay a premium for ticket flexibility, better in-flight and on-the-ground service qualities, flight frequency and other add-on services. According to CAA Airline Statistics, capacity (in terms of seat km) of all UK scheduled airlines fell by 2.5% between 2007 and 2009 while traffic (in passenger km) rose by 1.3%, resulting in an increase in load factor (ratio of passenger km to seat km) of 2.9 percentage points to 78.9% over the same period.

2.28 Figure 2-6 shows the average one-way fares (in 2005 prices) between 1997Q1 and 2010Q2 paid by UK-resident business passengers.[120] While the average business fare for the Rest of the World (ROW) has continued to decline since the events of 11 September 2001, the average fare paid by business passengers in the North Atlantic market had recovered gradually from the low level in 2003 until the recent economic crisis which saw a fall of almost 15% in 2009.

Figure 2-6 Average one-way fares (in 2005 prices) paid by UK-resident business passengers



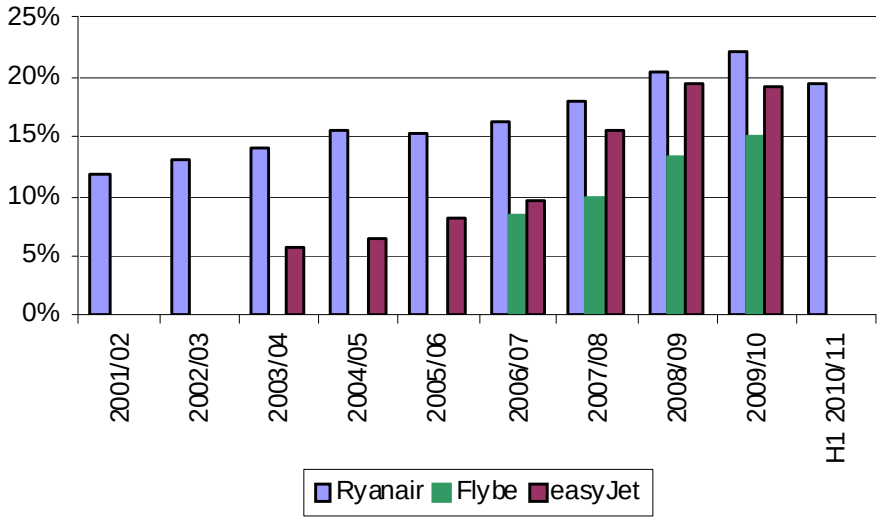
Source: International Passenger Survey, ONS.

Note: The solid lines represent moving averages based on the preceding four quarters.

2.29 On the other hand, the decline in average short-haul business fares started in the late 90s, and coincided with the rapid expansion of no-frills carriers in Europe, brought about by liberalization of EU air services – the average business fare almost halved between 1998 and 2006. Since then, average short-haul business fares have stabilized at around £110–£120 and appear to have held up relatively well (down only 2.5% in 2009) during the economic downturn. This is partly because a significant reduction in short-haul business passengers flying on business class tickets had already taken place over the period 2001 to 2006,[121] and the competitive nature of the short-haul market appears to have largely exhausted the scope for further deflation of business air fares. Indeed, short-haul airlines are increasingly reliant on ancillary services to raise their revenues – services such as seat pre-selection, fast check-in and lounge access that some business travellers still value. Figure 2-7 shows the significance of ancillary revenues for Ryanair, Flybe and easyJet which, for the larger two airlines, appeared to have stabilized at just under 20% by 2009/10.

120. These figures represent the average fares paid by all business passengers irrespective of whether they travel in the premium or economy classes. These fares include airport taxes and other add-on charges such as baggage check-in, fuel surcharge, priority boarding etc. Thus a reduction in the average business fare over time may reflect a declining trend of the premium fares paid by business passengers and/or a reduction in the proportion of business passengers travelling in the premium cabins.
121. See Chapter 3 of Part 1 of this study.

Figure 2-7 Ancillary revenue as proportion of total operating revenues



Source: Financial accounts by Ryanair, Flybe and easyJet in various years.

The airline response to the recession

Airline reactions to the economic crisis

2.30 Interviews for this study revealed the airline perspective on the effects on business travel of the economic downturn, which is summarised below. Following a period of very high oil prices, airlines were hit by the sudden fall in demand for business travel. The effects of the crisis were reported as very different to one-off shocks such as the dot-com bubble, the Asian financial crisis, September 11 and SARS, where the effects tended to be focused on specific markets. In those instances it was easier to see future recovery. Firms curtailed travel for a period, causing a short-term shock to the market concerned, but the underlying demand for travel remained, allowing demand to bounce back. The recent downturn, being global and relatively deep, had the effect of shrinking the market over a longer period.

2.31 Inevitably yields fell as airlines tried to fill excess capacity by lowering prices to attract leisure passengers or to poach business passengers away from rivals. (Fuel prices also subsequently fell, offsetting the revenue loss to some extent.) Airlines' negotiating position with large companies weakened, potentially resulting in greater concessions on price and/or product. Some introduced two-for-one offers and attractive redemption bonuses for frequent-flyer points to fill Business Class seats, but overall load factors saw a less dramatic decline because some business traffic downgraded to economy rather than ceasing altogether, and because airlines took steps to remove capacity.

2.32 On short-haul routes, most airlines offering Business Class use a moveable cabin divider, so this allowed them flexibility to reduce the size of the business cabin as necessary. Short-haul business routes that were operated at a relatively high frequency gave some scope for airlines to reduce the number of flights while maintaining a minimum frequency for business travellers. On long-haul routes, because cabin configurations are fixed in the short term, reducing the number of Business Class seats requires a reduction in frequency or, where the fleet allows,

aircraft size. For example, BA cut frequency on some key long-haul routes, removed aircraft from service, deferred new deliveries,[122] and redeployed aircraft on new leisure-orientated routes.

2.33 At congested airports, reducing frequency potentially means giving up valuable slots. At Heathrow at least, where slots are scarcest and particularly valuable, airlines were generally not prepared to do this, because of the long-term importance of retaining slots to maintain an attractive schedule once traffic returned. They therefore sought to remove services only to the extent that the use-it-or-lose-it rule permitted,[123] replaced Heathrow long-haul services with short-haul services,[124] or in extremis considered how to maintain the slots through 'babysitting'.[125] The use-it-or-lose-it rule was suspended for the Summer 2009 season by an amendment to the EU Slot Regulation in reaction to the downturn in traffic, but the amendment was not formally agreed until well into the season, by which time airlines had to some extent already committed to their schedules.

2.34 Where an existing service is operated only once per day, it may not be cost effective to remove flights, because fixed costs may still be incurred daily and the customer proposition falls to a less attractive sub-daily. It may be a better solution to replace business passengers with leisure passengers, for example by attracting them into Business Class with lower fares,[126] albeit at the expense of yield. Airlines with a strong network may have some scope to use revenue optimisation techniques to cut back inventory in the UK market in favour of other points of sale that have stronger demand for the service in question. Thus a UK airline may seek to attract traffic transferring in the UK from one international flight to another international flight, while a foreign airline may look for traffic destined for the UK that originates from or beyond its hub. However, there may be little scope for attracting more connecting traffic if the city pair concerned is also suffering from weak demand.

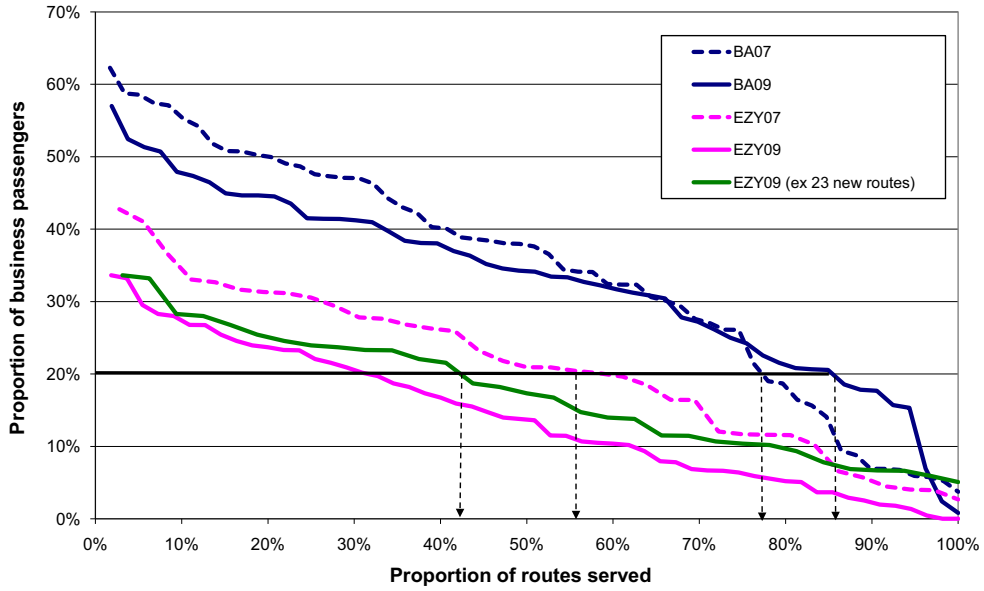
2.35 Research for this study suggests that airlines have now matched capacity with demand much more closely; there is anecdotal evidence that on some routes business travel organisers are finding it hard to find seats for last-minute bookings. Now that demand is returning and yields are recovering, the extent to which capacity is brought back is crucial to whether higher yields can be sustained.

122. www.flightglobal.com/articles/2009/05/22/326904/british-airways-to-ground-16-747s-and-757s-for-winter.html; www.flightglobal.com/articles/2009/07/03/329223/british-airways-pushes-back-a380-deliveries-by-up-to-two-years.html; http://press.ba.com/?p=766 . Virgin also cut frequency on key routes, see for example *Virgin Atlantic to cut flights and jobs*, www.ft.com (2 July 2009).
123. The EU Slot Regulation makes 'grandfather rights' - the right to that slot in the equivalent season the following year - conditional on use of an allocated slot on at least 80% of occasions. Therefore some frequency cuts could be achieved by careful juggling of schedules.
124. For example, BA transferred a significant number of short-haul services from Gatwick http://press.ba.com/?p=766, while Virgin leased out three daily slot pairs to Aer Lingus from Winter 2009 www.slottrade.aero/completed-trades.asp.
125. Essentially arranging for another operator to 'keep the slots warm' to meet the use-it-or-lose-it rule.
126. See paragraph 6.66 in Chapter 6.

Impact on BA and easyJet's business traffic

2.36 The economic recession has impacted not only on the volume and average yield of business travellers, but also on the distribution of overall business traffic among airlines. Figure 2-8 illustrates how the economic downturn has affected the proportion of business passengers on short-haul international routes served by BA and easyJet from London airports (excluding London City) between 2007 and 2009.

Figure 2-8 Distribution of business passengers on BA and easyJet international short-haul routes from London airports (except London City), 2007 and 2009



Source: CAA Passenger Survey, 2007 and 2009.

Note: London City is not included as it was not sampled by the CAA in 2007 and 2009. Routes with fewer than 50 interview records have been excluded from the data to minimize sampling errors.

2.37 The data shows that BA carried a higher proportion of business passengers on the routes it served than easyJet (one plausible reason is that BA has a larger proportion of business routes that link to a primary airport). For example, 78% of the short-haul routes served by BA from London had 20% or more business passengers on board in 2007 compared with 56% of easyJet's routes.

2.38 The proportion of international business passengers on BA routes served out of London airports declined in 2009 compared with 2007 – indicated by the relative position of the two blue curves in Figure 2-8. However, it appears that easyJet suffered a greater dilution of its business traffic than BA. This could be partly explained by its route network expansion between 2007 and 2009 when 23 new international routes were added and four dropped (a net gain of 19 new routes). On 19 of the 23 new routes, less than 20% of passengers were travelling for business purposes. When the 23 new routes are removed from the 2009 survey data, the dilution of business traffic on the remaining 32 routes (as indicated by the relative position of the green and dotted pink curves) becomes closer to BA's.

2.39 Although both airlines experienced a similar dilution of their business traffic, it appears that BA has suffered a bigger fall in its business traffic than easyJet has. Of the 1.7 million travellers (or 10.8% of its total traffic) lost by BA at London airports over the period, 1.3 million of them were business travellers which represented a 20.5% drop in its business traffic. In contrast, easyJet gained almost 0.5 million (4.7%) total passengers on the 32 routes that it served in both 2007 and 2009 while losing 0.3 million (14%) of its business traffic between 2007 and 2009.

Short-term outlook for UK business travel

2.40 The short-term outlook for UK business travel will depend to a large extent on the sustainability of the current economic recovery in the UK and world economies, as the airline industry is historically highly leveraged to the economic cycle with business travel in particular closely linked to the rise and fall of trade, business confidence and economic growth (see the next chapter for further discussion).

2.41 The UK economy grew at a rate of 0.8% between July and September 2010 following a 1.2% growth in the previous quarter (see Figure 2-2).Table 2-6 shows actual and IMF near term forecasts of real GDP growth of the world economy, the UK and its major trading partners – the US and the EU. Compared with the IMF's previous forecast in April 2010, the October forecast represents an upward adjustment of around 0.4 to 0.6 percentage points for the UK, EU and the world economy in 2010 and a downgrade of 0.4 percentage points for the US. As uncertainty about the strength of the economic recovery lingers, the IMF forecasts for the UK and US in 2011 have been reduced by 0.5 and 0.25 percentage points respectively while the growth of both the EU and the world economies was only down by about 0.1 percentage points from its previous forecast.

Table 2-6 Actual and forecast of real GDP growth (%)

	2007	2008	2009	2010	2011	2012
United Kingdom	2.69	-0.07	-4.90	1.70	2.02	2.29
European Union	3.19	0.76	-4.10	1.65	1.70	2.12
United States	1.95	0.00	-2.63	2.64	2.31	3.04
World	5.34	2.83	-0.58	4.77	4.22	4.54

Source: World Economic Outlook, IMF, October 2010.

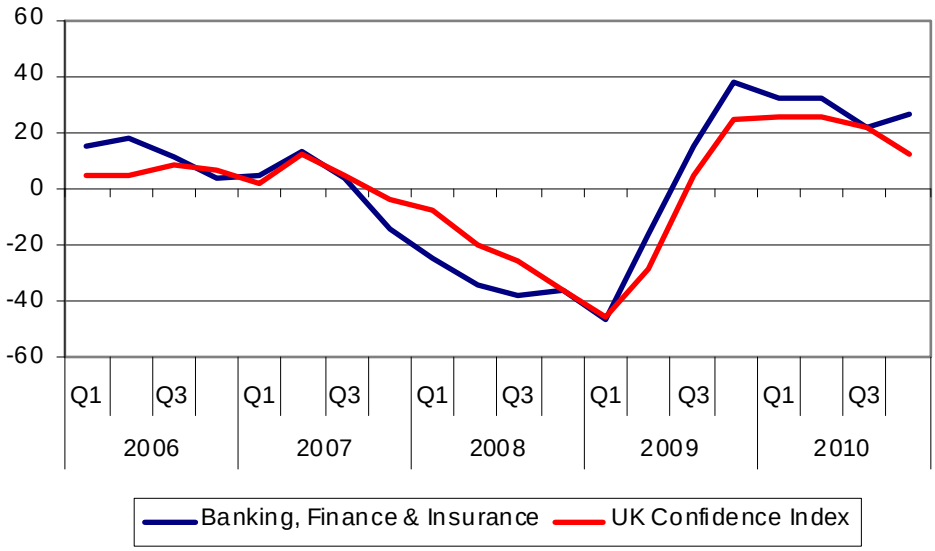
2.42 As the world economy recovers and business confidence strengthens, the need for corporate travel to meet external clients and attend internal meetings in support of sales and expanding the customer base is expected to increase. In particular, the robust recovery seen in the Asian, and some emerging, markets is expected to continue and will likely increase UK business travel to and from these economies. However, the EU and the US will remain the UK's predominant trading partners in the foreseeable future and the most significant markets for UK business travel (representing 64% of total UK trade and 73% of UK international business travel in 2009).

2.43 A global survey of 480 senior finance executives by American Express in May 2010 found that nearly two thirds (62%) of companies expect to maintain or increase their travel spend in the coming year.[127] It found that only around 34% of respondents planned to cut travel to internal meetings and conferences compared with about 80% in 2009. However, later surveys have shown some decrease in business confidence, albeit that it is still at a higher level than in 2008 and the first half of 2009. Figure 2-9 shows the Q4 2010 UK Overall Business Confidence Index[128] fell to 11.9, a drop of almost ten percentage points from the previous quarter.[129] The fall in the overall confidence index is consistent with a range of recent data that have pointed to a slowdown in the pace of economic recovery from the second half of 2010 into the

127. American Express/CFO Research: *Global Business & Spending Monitor* (May 2010).
128. ICAEW: *UK Business Confidence Monitor Q4 2010*. This latest survey was based on 1000 telephone interviews conducted between 28 July and 21 October 2010.
129. The proportion of businesses less confident about the coming 12 months has risen from nearly one in five (19%) to nearly one in four (24%) between Q3 and Q4.

first half of 2011. This contrasts with the moderate rebound of 4.6 percentage points in the confidence index of the banking, finance and insurance sector after three consecutive quarterly drops since the Q4 2009 peak, despite continuing uncertainty from a combination of a toughening of the regulatory regime[130] on the financial sector and concerns over sovereign debt issues in the Eurozone.

Figure 2-9 Business confidence index trend, 2006–2010



Source: UK Business Confidence Monitor, ICAEW, Q4 2010.

Note: A confidence index of zero would indicate that all survey respondents were as confident about future economic prospects facing their business over the next 12 months, compared with the previous 12 months.

2.44 Therefore, despite the uncertainty surrounding the strength of economic recovery in the UK, EU and US, the planned cut in UK public spending by more than 6% of GDP between 2010 and 2015, and the rise in VAT in January 2011, the short-term outlook for post-recession UK business travel is likely to be driven more by GDP fundamentals, and less by consumption confidence effects, which can impact leisure travel.

2.45 There is evidence to suggest that both demand for corporate travel and air fares appear to be firming up again,[131] although some legacy network airlines may not be able to rely as much as before on passengers willing to pay a premium for travelling Business and First class. Indeed, several European carriers have already eliminated First or Business Class on some routes[132] while others may reduce the size of their premium cabins in response to changing demand. As corporate travel buyers and business travellers have become more cost-conscious in the light of the economic crisis, there is a question over whether some of the changes in travel behaviour may become permanent features and thus alter the nature of demand for business travel.

2.46 The next chapter examines some of the main demand drivers for business travel and the question of whether they may have changed in light of the recession.

130. Such as the implementation of Basel III agreement.
131. BA reported a 20% growth of its passenger yields in Q3 2010 and an increase of its premium traffic by more than 4% in September and October 2010. GTMC quarterly transaction data also show significant growth in the corporate use of air and rail travel since the beginning of 2010.
132. For example, Alitalia, KLM and Iberia do not have First Class on their long-haul routes. US transatlantic examples are Continental, Delta, Northwest (now part of Delta) and US Airways. bmi has removed Business Class from its short-haul routes (with some exceptions), as has CityJet (an Air France subsidiary operating from London City).

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Part 2 Chapter 3 Demand drivers for business air travel

Chapter summary

- The main drivers for business air travel demand have traditionally been seen as GDP and globalisation, and the consequent growth in multilateral trade and capital flows; there is no evidence to suggest that these relationships have significantly changed due to the recent recession.
- As the UK economy becomes more integrated with the rest of the world (as indicated by volume of trade and foreign direct investment), demand for business travel to and from the UK has become more dependent over time on the economic development of the UK's trading partners and other emerging markets.
- A small-sample CAA survey of passengers on four business routes (Amsterdam, Dublin, Hong Kong and New York) operated at Heathrow and Glasgow in Autumn 2009 indicated that 'attending internal business meetings' remained the main reason for a significant proportion of business travel, and that ticket price, as well as timing of flights and service quality, was an important factor in business passengers' choice between airlines.
- Econometric analysis[133] undertaken by the CAA indicates that GDP is the most significant factor in determining demand for business travel although outbound business travel appears to have a higher GDP elasticity (between 1.40 and 1.96)[134] than inbound business travel (between 0.65 and 1.27).
- Volume of trade (in goods only) appears to be a significant factor for two of the six business markets considered and demand for business travel is less elastic with respect to trade than to GDP, ranging from 0.33 to 0.53.[135]
- The econometric results also indicate a 'step down' in business travel demand occurring around 2008Q4, over and above that which would have been expected from the observed changes in GDP, trade or fares, which may represent a permanent change in demand. There is no strong evidence to suggest that the underlying relationships between business travel and its main demand drivers (GDP, fares and trade volume) have altered significantly due to the recession.

Introduction

3.1 Demand for business travel is a key source of revenue and profit for many scheduled carriers, as discussed in Chapter 2. This is because business travellers tend to place relatively high value on time, available flight frequency and quality of service and are, in general, less price sensitive than leisure passengers. They therefore have a relatively high willingness to pay for travelling in premium classes or to pay a premium for ticket flexibility or late booking. As a result, this source of demand has an influence on some airlines' pricing and operational strategies out of proportion to the number of travellers.

133. Based on six separate markets: UK or foreign resident international business passengers travelling to and from EU25, North America and Rest of the World.
134. An income elasticity bigger than unity implies that an increase in national income of, say, 10% would induce more than a 10% rise in the demand for total business travel, all else being equal.
135. Quarterly data on UK trade in services was not available for the whole sample period. Also, it can be difficult to separate out the effect of trade on business travel demand from that of GDP.

3.2 In Part 1 of this business travel study and in the previous chapter, it was found that business passengers were increasingly seeking cheaper alternatives to First and Business Class travel, and that no-frills carriers had been successful in capturing a significant share of the short-haul business market. This trend occurred while business travel grew between 1996 and 2007, but there is evidence that the recent recession has further accentuated downgrading by business passengers, particularly in the short-haul business market.

3.3 This chapter begins by looking at the motivation for business travel, followed by a discussion of how it has been stimulated by the process of globalisation, and some of the other potential underlying demand drivers for business travel both at the macro and micro levels. There is then a presentation of the CAA's empirical findings on the historic relationship of some of these macro factors on business air travel demand to and from the UK, and consideration of whether the recent recession is likely to have changed these relationships in the long term.

Motivation for business travel

3.4 In the face of the weakening economic environment and falling profits, many organisations sought to reduce their spending on business travel. Chapter 2 highlighted how the impact of the recent economic downturn on business travel to and from the UK varied by geographical region (EU, North America and Rest of the World), traffic sector (domestic, short and long haul) and by airport/airline.

3.5 The CAA's interviews with business travel stakeholders (corporate travel buyers, TMCs, airlines and airports) reported in Chapter 2 suggested that corporate travel budgets were cut significantly during 2009, and fewer business passengers were booking at short notice on higher-yielding tickets. There was also increased scrutiny by some companies of the need to travel and enforcement of formal pre-trip approval. That these measures led to a cut back in corporate travel seems to be corroborated by ONS data on travel expenditure by UK residents travelling overseas on business purposes (Table 2-5).

3.6 It appeared that business travel expenditure, some of which was regarded as discretionary, was increasingly being considered by companies as a cost item to be contained (particularly during an economic downturn), rather than as an investment.

3.7 However, the CAA's interviews with business travel stakeholders also suggest that GDP and trade flows are seen as far more important in determining the amount of future business travel than, say, videoconferencing. It was suggested that there is little evidence that technology dampens travel; indeed, it facilitates companies becoming global operators, while any medium which facilitates communication is likely also to promote physical meetings in order to cement relationships (see Chapter 7 for more detail).

3.8 Notwithstanding the potential benefits from business travel, it appeared that only a small number of companies explicitly measure the return on travel spending (none of the corporations and travel buyers interviewed by the CAA claimed to measure the return on their business travel directly).

3.9 Research and surveys on company executives and business travellers[136] have indicated some of the main reasons for business travel as:

- Customer retention
- Converting prospective customers into clients

136. Oxford Economics USA: *The return on investment of US business travel* (September 2009); HIS Global Insight: *Can we afford not to invest in business travel?* (September 2009). These studies were conducted on behalf of National Business Travel Association and US Travel Association respectively.

- Establishing new contacts and building relational networks
- Maintaining customer relationships and expanding the customer base
- Investment in human capital (attending conference/trade show)
- Potential returns from initiating and/or closing business deals.

3.10 Based on a combination of surveys of (c. 300) executives and (c. 500) business travellers in the US and an econometric analysis, a recent study by Oxford Economics USA[137] has attempted to quantify the effects of business travel on sectoral productivity and, by extension, on corporate performance. The study tries to measure not only the cost of business travel but also the contribution it makes to businesses in terms of sales and profits. The study finds significant positive relationships between business travel and corporate performance in terms of productivity[138] that could translate into benefits for companies and improve their profitability.

3.11 The surveys indicate that face-to-face meetings are necessary to building successful business relationships with existing and prospective customers. In particular, without such in-person meetings, both surveyed corporate executives and business travellers estimate that a significant proportion (more than 25%) of their business could be lost and a much lower rate in converting prospective customers into new customers could ensue (reduced from 40% to 16% on average).[139]

3.12 Using econometric analysis based on data from 14 sectors over a period of 13 years, the Oxford Economics study also finds that business travel contributes significantly to sales and profit, with an average incremental return of $12.5 in revenue and $3.8 in profits for every dollar spent on business travel in the US.[140] These findings appear to be supported by the survey results which indicate that the average return on revenue was between $10–$15 per dollar spent on business travel, depending on the type of business trip (customer meetings generate three to five times higher benefits than attending conferences or trade shows).[141]

3.13 Finally, based on these findings, the study argues that given the need for business travel, companies that do not invest in business travel will suffer in terms of sales and profitability. Thus, companies should consider the implications of travel budget cuts in terms of potential loss in revenues/profits over a longer-term horizon versus any short-term savings.

3.14 The CAA has undertaken a survey of passengers at Heathrow and Glasgow airports in order to assess the relative importance of different factors that influence business passengers' choice of cabin, carrier and airport for their business trips, as well as their booking behaviour in comparison to leisure travellers.[142] This relatively small-sample survey was conducted over the period of August to December 2009 for passengers travelling from Heathrow or Glasgow to two short-haul destinations (Amsterdam and Dublin) and from Heathrow to two long-haul destinations (Hong Kong and New York). These destinations were chosen because of their relatively high density of business traffic.

137. *ibid*.
138. The study used multi-factor productivity, which measures improvement in the level of output(s) due to improvements in a mix of inputs, of which business travel or travel intensity is only part.
139. These findings are based on counterfactuals and therefore need to be interpreted with caution.
140. Caution should be exercised in interpreting these results as the Durbin Watson statistic cited in the study was not statistically valid due to the regression model including a lagged dependent variable as one of the explanatory variables in the equation. Nevertheless, the findings of positive (bilateral) causal relationships between business travel and productivity growth and that business travel could generate (statistically) significant benefits may still hold, although the extent of these estimated benefits as reported in the study may be questionable.
141. A less rigorous study by IHS Global Insight *Can we afford not to invest in business travel?* (September 2009) even claims that an average company in an industry that is well below its optimal business travel level could potentially attain an incremental ROI of business travel to profits of 14.3 to 1.
142. See Annex 2.A for the business survey questionnaire.

3.15 One factor that may affect business passengers' choices is the reason for the trip. Table 3-1 shows the distribution of trip purposes by business passengers by type of route and by airport. In contrast to business travellers at Glasgow, the majority of business passengers at Heathrow were either travelling for the purpose of attending internal business or meeting external customers. However, these results could have been influenced by how broadly respondents defined 'internal meeting', and the need for internal meetings might be driven directly by external company business. This high proportion of travelling for internal purposes might also indicate the increasing number of multinational firms, particularly in London, with local offices and client bases in New York and other cities. This is supported by the relatively high proportion of business travel undertaken for relocation or home leave purposes.[143]

Table 3-1 Main purpose of business trip

	Glasgow	**Heathrow**	
	Short	**Short**	**Long**
Attending internal business	29%	43%	49%
Relocation / home leave	21%	6%	10%
Conference / trade fair	21%	7%	9%
Meetings with external customers	12%	36%	23%
General business	13%	5%	10%
Other	2%	3%	0%
Total	**100%**	**100%**	**100%**

Source: CAA survey of business passengers in August–December 2009.

Note: Sample size = 89 interviews at Glasgow, 243 at Heathrow (restricted to passengers travelling for business purposes).

Travel requirements of business passengers

3.16 While not directly relevant to the motivation for business travel, considering how the requirements of business travellers differ from those of leisure travellers may provide some evidence for or against the importance of potential demand drivers, in particular the importance of air fares.

3.17 Traditional network airlines offer 'fully flexible' business and economy class tickets at a premium that are aimed at meeting the needs of business travellers whose travel requirements may change after a ticket is purchased. In this survey, Table 3-2 and Table 3-3 show that business passengers were much more likely to have purchased flexible tickets than leisure passengers, and that, even for passengers without flexible tickets, business passengers were more likely to change their tickets after the original booking than leisure passengers. Nevertheless, the data appear to show that the majority of those passengers surveyed who travelled on the four selected routes did not change their tickets (35% or less for business passengers with flexible tickets, and 10% or less for leisure). The lower use of flexible tickets for short-haul than long-

143. The Relocation / Home leave figure for Glasgow is boosted by workers from the oil and gas industries.

haul business travel, with a marked difference between Glasgow and Heathrow, may in part be explained by no-frills carriers increasingly offering a means of providing ticket flexibility by levying a pay-as-you-need fee[144] for changing their tickets.

Table 3-2 Proportion of passengers with flexible tickets

	Glasgow	Heathrow	
	Short	Short	Long
Business	3.4%	21.4%	37.1%
Leisure	0.5%	1.7%	6.1%

Source: CAA survey of business passengers in August–December 2009.

Note: Sample size = 291 interviews at Glasgow, 887 at Heathrow.

Table 3-3 Proportion of passengers that changed tickets after booking

		Glasgow	Heathrow	
		Short	Short	Long
Business	Flexible	0%	35%	31%
	Other	16%	17%	16%
Leisure	All	7%	8%	14%

Source: CAA survey of business passengers in August–December 2009.

Note: Sample size = 291 interviews at Glasgow, 887 at Heathrow.

3.18 Table 3-4 suggests that business passengers are much more likely than leisure passengers to purchase tickets for travel at short notice, with over 40% of short-haul and over 20% of long-haul business travellers having bought tickets less than a week before departure. This compares with around 10% for leisure passengers

Table 3-4 Time of ticket purchase relative to time of travel

	Business			Leisure		
	Glasgow	Heathrow		Glasgow	Heathrow	
	Short	Short	Long	Short	Short	Long
Less than 1 week	40%	46%	22%	10%	11%	8%
Between 1 and 2 weeks	30%	24%	25%	16%	16%	7%
Between 3 and 4 weeks	13%	20%	23%	15%	20%	10%
Between 1 and 3 months	13%	9%	20%	33%	36%	30%
More than 3 months	2%	2%	10%	25%	18%	46%

Source: CAA survey of business passengers in August–December 2009.

Note: Sample size = 290 interviews at Glasgow, 871 at Heathrow.

144. easyJet charges an administration fee of £30 per passenger per sector if a flight change is made online at least two hours prior to the flight's scheduled departure time, plus any difference in the total cost of the flight applicable at the time the change is made. Similarly, Flybe charges £27.50 for reservation changes. More recently, easyJet has launched flexible fares aimed at business travellers that allows passengers to make unlimited changes up to two hours before the scheduled departure time within a four-week time window – one week before and up to three weeks after the original booked travel date.

3.19 Table 3-5 shows the method of purchase for the survey passengers' tickets. The table suggests that less than half of business passengers booked through a company travel department[145] or travel management company (TMC), with far fewer of the Glasgow business passengers using a TMC. The survey indicates around 40% of business travellers at both Heathrow and Glasgow booked tickets through the internet, and 15–20% used a high street travel agent.

Table 3-5 Where ticket was purchased

	Glasgow		Heathrow	
	Business	**Leisure**	**Business**	**Leisure**
Company travel department	27%	2%	26%	0%
TMC implant	8%	0%	20%	0%
Internet (airline)	44%	63%	31%	52%
Internet (other)	2%	14%	7%	25%
Travel agent (high street)	18%	21%	14%	21%
Other	0%	1%	2%	2%

Source: CAA survey of business passengers in August–December 2009.

Note: Sample size = 289 interviews at Glasgow, 827 at Heathrow.

3.20 Finally, Table 3-6 shows how business passengers responded when asked to name up to three factors which were important in their choice of airline at the survey airports. Short-haul passengers gave similar answers at the two airports, except that price was more significant to business passengers at Glasgow and timing of flights and airport proximity were more significant to business passengers at Heathrow. Long-haul business passengers at Heathrow appeared more sensitive to price, service quality and airline loyalty than (Heathrow) short-haul business passengers, but less sensitive to flight timings and airport proximity.

Table 3-6 Business passenger reasons given for choice of airline at airport

	Glasgow	Heathrow	
	Short	**Short**	**Long**
Timing of flights / direct route / availability	29%	50%	25%
Frequent-flyer programme / loyalty / preferred airline	14%	18%	31%
Service quality	21%	19%	32%
Price of ticket	50%	26%	44%
Airport proximity / convenience	7%	34%	21%
Other	50%	44%	40%

Source: CAA survey of business passengers in August–December 2009.

Notes: Sample size = 89 interviews at Glasgow, 243 at Heathrow.

'Other' includes 'only airline serving route' and 'ticket booked by someone else'.

The sum of each column is more than 100% because survey respondents were allowed to provide up to three reasons for their choice of airline and airport.

145. An internal company travel department will itself have to make travel bookings though a TMC or online.

3.21 Although it is not possible to draw firm conclusions from such a small survey, the results confirm that, even in the economic climate of late 2009, significant numbers of business travellers required flexibility in their travel booking, but were using a variety of channels to purchase it. This reinforces the traditional view of the business traveller as more prepared than leisure passengers to pay higher fares or add-ons for greater flexibility, albeit that price was highly significant in the passengers' choice of airline.

3.22 The following sections consider some other macro and micro factors that may have facilitated the growth of business travel to and from the UK, in particular, the effects of globalisation and economic integration on demand for business travel.

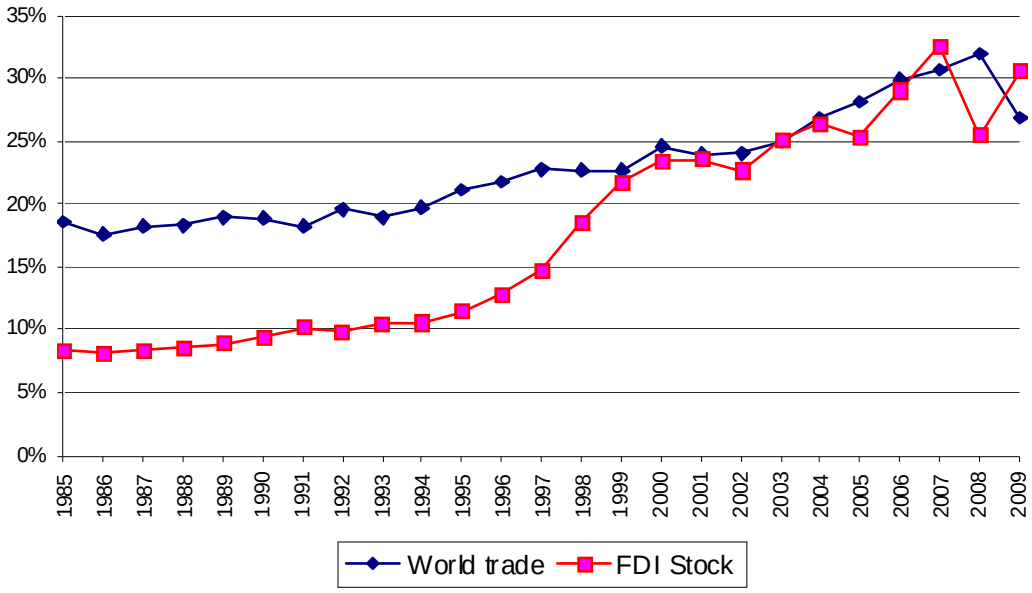
Globalisation, economic integration and business travel

3.23 The world economy has exhibited increasing international linkages and become more 'globalised' over the past few decades. While 'globalisation' was originally intended to describe the process of cross-border integration of economies, the term has evolved to characterize any activity or relationship which extends beyond national borders.[146] This includes international trade in intermediate inputs, movement of goods and services, factors of production (capital and labour) and information across borders. Such cross-border flows of capital, goods and services are facilitated by innovation, technological progress, transportation systems, and government policies promoting deregulation and privatisation in markets around the world. In turn, these result in increased international competition and expansion of markets, which lead to an increase in the demand for business travel.

3.24 For example, Figure 3-1 shows that, according to the IMF, total international trade in goods and services grew from the equivalent of 19% of world GDP in 1985 to 32%[147] in 2008, before dropping to 29% in 2009, and financial linkages – measured as the stock of foreign direct investment (FDI) – increased from the equivalent of 8% of world GDP in 1985 to 33% in 2007. However, FDI stock fell to the equivalent of 26% of world GDP at the height of the financial crisis in 2008 before climbing back to 31% in 2009. This rapid increase in financial and economic integration across different nations over the last 25 years has led to increased observations of business cycle co-movement between countries or regions, as well as countries within a region, a trade block or a monetary union.[148]

146. Putko, M.: *Defining and quantifying globalization*, USAWC Strategy Research Project, US Army War College, Pennsylvania, USA (2006).
147. These totals count international trade as the average of total world import and export values to avoid double counting.
148. There is some evidence to suggest that some emerging economies (such as China and India) are increasingly 'de-coupled' from the more advanced economies in recent years, particularly in light of the recent economic crisis, while they are becoming more 'linked' with other emerging or less developed markets in terms of trade and direct investment.

Figure 3-1 World trade and stock of FDI as percentage of world GDP



Source: IMF WEO October 2010 database and UNCTAD.

Note: World trade is expressed as imports plus exports, so trade's contribution to GDP is only half the figure shown.

3.25 While globalisation is not a new phenomenon, little attention so far has been paid to the potential effect of these synchronised business cycle co-movements on business air travel. This section provides some high level evidence on the business cycle correlation between the UK economy and other countries since 1993 and discusses how that might have affected the demand for business air travel to and from the UK.[149]

Measures of 'globalisation'

3.26 Understanding the overall impact of globalisation and integration on the UK economy, and consequently on the demand for business travel, ideally requires an index that can give a comprehensive measure of globalisation (capturing economic, political, social, cultural and institutional dimensions). A number of indicators have been suggested to measure the extent of economic and financial integration, including de jure measures that reflect the extent of legal restriction on cross-border financial and trade flows and outcome-based de facto measures that reflect a country's actual degree of financial integration.[150]

3.27 However, this study focuses only on the economic dimension of globalisation (in terms of total trade volume and foreign direct investments which are proxies for international trade and capital flows), since business travel is, to a large extent, driven by economic (and financial) activities within and across national borders.[151] This is evident from the CAA's econometric analysis, the results of which are presented from paragraph 3.43 onwards.

3.28 The UK is closely integrated with the world economy through both trade and financial links. Figure 3-2 shows that, between 1980 and 2009, the UK's total trade in goods

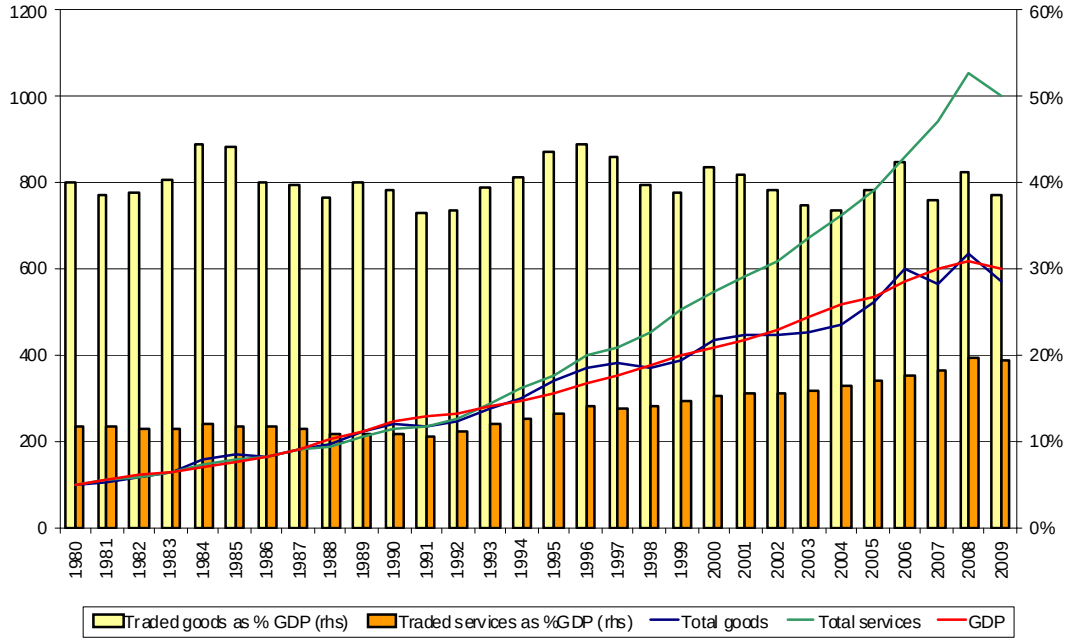
149. A consistent time series for business passengers to and from the UK split by country and by quarter is readily available from 1993 onward from the ONS International Passenger Survey.

150. See Schindler, M: *Measuring financial integration: a new data set*, IMF Staff Papers (2009); OECD: *OECD Handbook on economic globalisation indicators* (2005).

151. For example, the G-Index compiled by the World Market Research Centre is a primarily economic-based index (90% of the weight) with the remaining 10% technology-based (telephone traffic, internet penetration).

(combining the value of imports and exports) grew in line with GDP and, expressed as a percentage of the GDP output value (measured in current prices), it hovered around the 40% level over the period. However, this contrasts with trade in services, which increased much more rapidly from the mid-90s. In 2008, the total value of UK trade in services peaked at the equivalent of 20% of GDP, an increase of eight percentage points from around 12% in 1980, before dropping slightly in 2009. The rising importance of the service sector could have affected demand for business travel, as there is some evidence to suggest that business travellers from finance-related sectors, such as investment banking, tend to have a higher propensity to take business trips and to travel in premium classes than business travellers from other sectors (see Table 7-3).

Figure 3-2 Indexed UK trade in goods and services and GDP (at current prices), 1980 =100

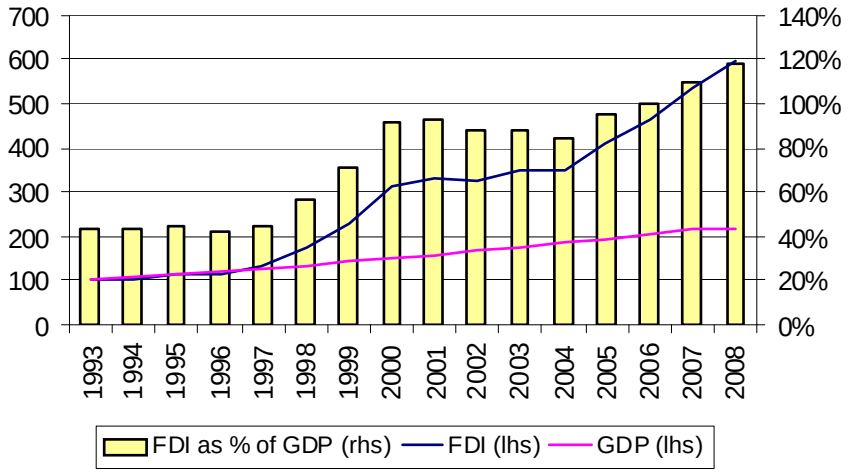


Source: ONS.

Note: Trade in goods and services are expressed as UK imports plus UK exports.

3.29 The extent of UK financial integration, as measured by the magnitude of cross-border foreign direct investment (FDI), has also increased rapidly in recent years. Figure 3-3 shows that the stock of FDI (both inflows and outflows) has increased four-fold since the mid-90s. In 2008, the total value of FDI reached the equivalent of 120% of UK GDP, compared with less than 60% a decade earlier.

Figure 3-3 Indexed total UK FDI and GDP (at current prices), 1993=100



Source: ONS.

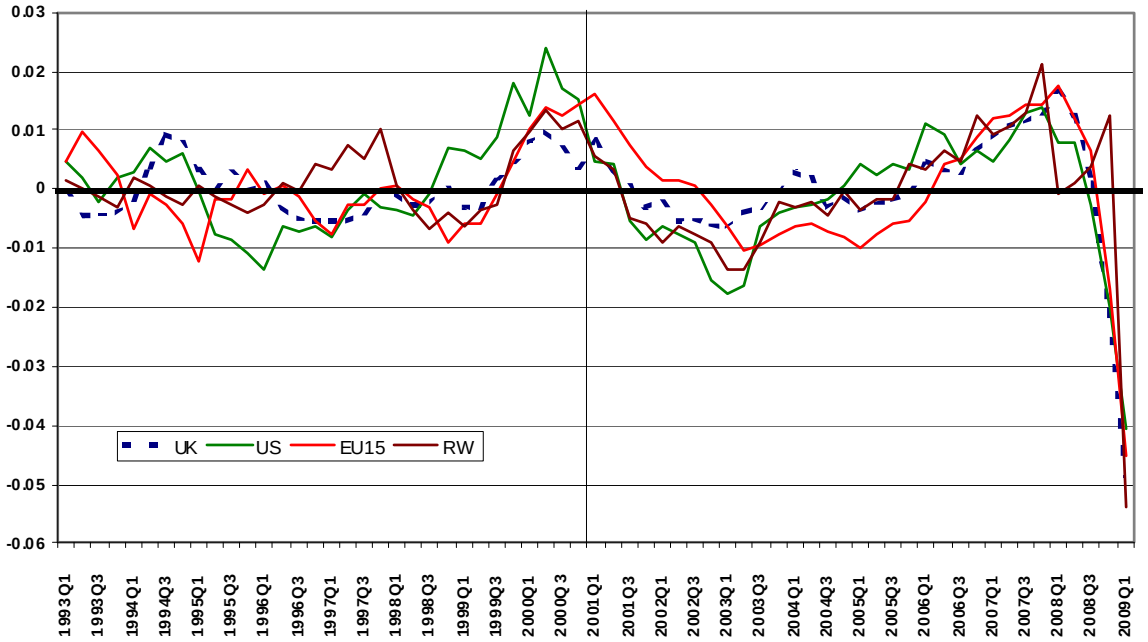
Globalisation, business cycle co-movement and business air travel

3.30 As the world becomes more integrated, national economies have become increasingly interdependent, with barriers to trade and market access reducing and travel times diminishing due to service and technological improvements in transportation. There is evidence that both trade and financial linkages have a positive impact on cross-country output and consumption co-movements. In particular, it has been found that country pairs that have strong trade and financial linkages with each other tend to experience higher business cycle correlation.[152]

3.31 One way to gauge the extent of economic integration of the UK economy with the rest of the world is to correlate the cyclical movement of UK GDP with other major economies over time after removal of the trend component from the time series.[153] Figure 3-4 shows the isolated cyclical component of GDP fluctuations for the UK, US, EU15 and rest of the world between 1993Q1 and 2009Q1 using the Hodrick-Prescott filter.[154] It appears that cross-country output correlations between the UK and the other economies have increased over time (the de-trended series become more 'in-step' with each other over time).

152. See for example, Frankel, J. and A. Rose: *The Endogeneity of the Optimum Currency Area Criteria,* Economic Journal, 108 (449), 1009–25 (1998); Baxter, M. and M. Kouparitsas: *Determinants of Business Cycle Co-movement: A Robust Analysis*, Journal of Monetary Economics, 52 (1), 113–57 (2005); di Giovanni, J. and A. Levchenko: *Putting the Parts Together: Trade, Vertical Linkages, and Business Cycle Co-movement,* IMF Working Paper 09/181 (2009).
153. Macroeconomic variables such as GDP by various countries tend to trend upward together over time albeit perhaps at different underlying rates. By removing the trend component of the series, one is able to assess the extent of contemporaneous correlation of the cyclical movements of GDP across countries.
154. One way of decomposing a time series into its trend and cyclical components is the use of the Hodrick-Prescott filter which is routinely used to de-trend aggregate output in the real business cycle literature. See Hodrick, R. and E. Prescott: *Post-war business cycles: an empirical investigation*, Journal of Money, Credit and Banking, 29, 1-16 (1997).

Figure 3-4 The cyclical component of GDP fluctuations



Source: CAA estimation based on ONS data.

3.32 Table 3-7 shows the degree of synchronisation of business cycles over the two sub-periods. It indicates that the temporal correlations of the cyclical component of UK GDP with those of US, EU15 and rest of the world GDPs were much higher in the second half of the period than in the first, and that the correlation was stronger with the US and EU15 than with the rest of the world.

Table 3-7 Correlations of the cyclical component of UK GDP with US, EU15 and rest of the world

	1993–2000	2001–2009	1993–2009
US	0.62	0.89	0.78
EU15	0.35	0.90	0.80
Rest of World	0.34	0.78	0.71

Source: CAA calculation based on ONS data.

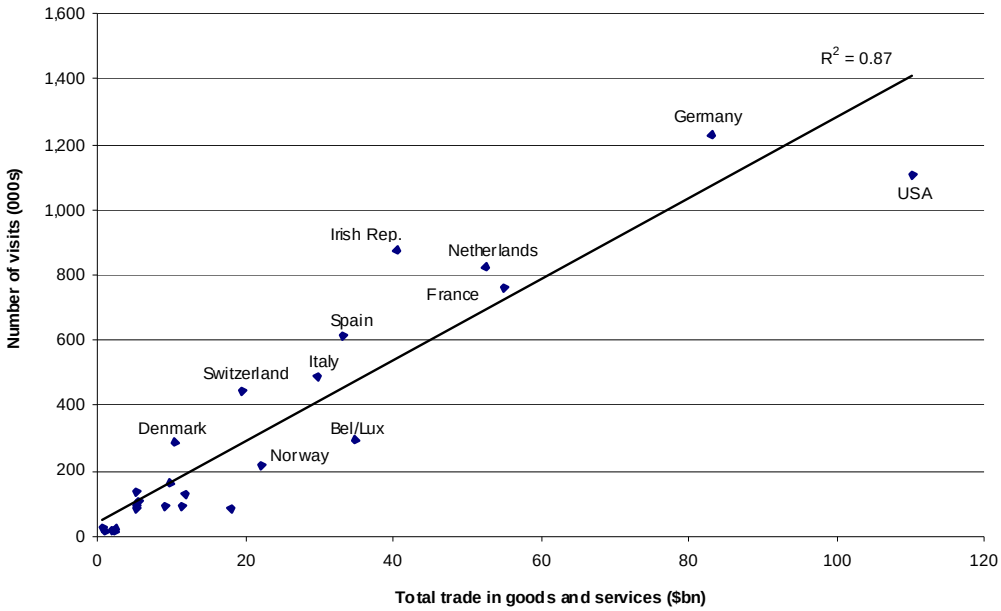
3.33 These findings may have implications for modelling international business air travel demand which is, to a large extent, conditioned by the level of trade and economic activity between countries. If increasing globalisation and market integration influences the correlations of macroeconomic aggregates of the UK with individual countries or country groups, as the simple correlation results here seem to suggest, then variables such as bilateral trade volume, industry structure and/or stock of capital investment between the UK and other countries could be potential drivers for business travel between the UK and the corresponding country (or country group). These relationships are explored further in the following sections.

Trade, capital flows and business travel

3.34 The increase in globalisation, facilitated by development of communication and transport technologies, has enhanced both the tradeability of goods and services and the flow of capital between countries and regions, which have led to increased demand for business travel. Figure 3-5 plots the number of business passengers at

UK airports against total trade volume with the UK in 2009 and shows a robust positive linear relationship,[155] suggesting that countries with high trade flows with the UK also tend to have high levels of business travel to and from the UK.

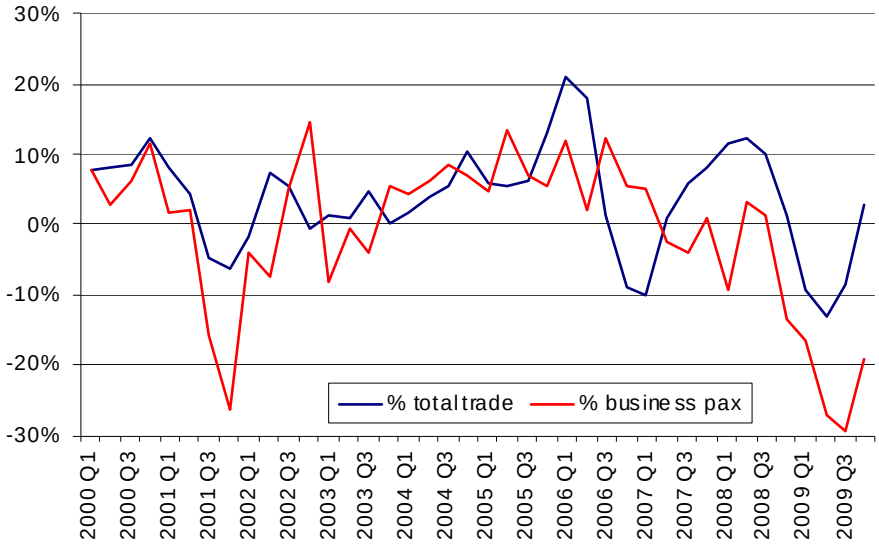
Figure 3-5 Number of visits by business passengers to and from the UK and total trade in 2009



Source: ONS.

3.35 Such a close relationship between trade and business travel appears not only across countries but also over time, as Figure 3-6 shows.

Figure 3-6 Growth of business passengers at UK airports and volume of trade

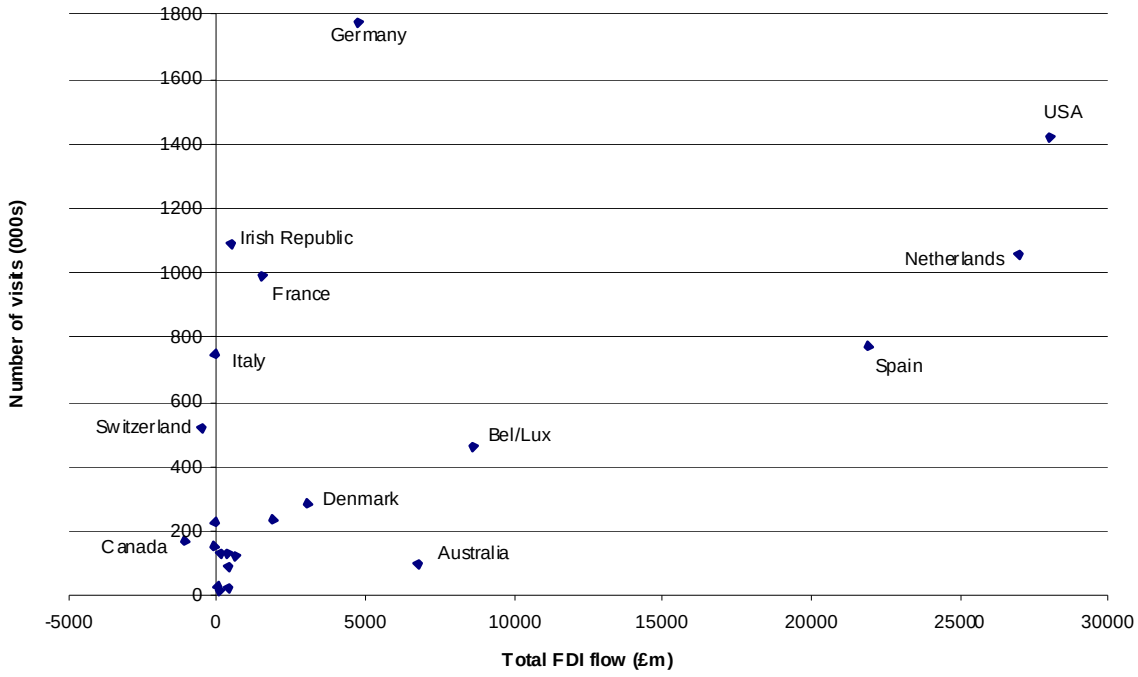


Source: ONS.

155. The linear model has a very high coefficient of determination (i.e. a high value of R^2) indicating that the linear line has a good fit to the data set.

3.36 In addition to trade, FDI may influence business travel in two distinct ways. The flow of FDI is related to new investments, either UK capital invested in overseas assets or vice versa, and might be expected to generate a certain amount of business air travel related to setting up these investments. However, business travel may be incurred in relation to all overseas investments, whether recent or not, the level of which can be measured by the annual stock of FDI. The relationships between either FDI flows or FDI positions (which is an annual measure of FDI stock) and business travel appear to be more complicated than those for trade or GDP. Figure 3-7 and Figure 3-8 indicate that, if a relationship between total UK FDI and business travel exists, then it is likely to be non-linear and hence more difficult to model empirically.[156]

Figure 3-7 Number of visits by business passengers to and from the UK and total flow of foreign direct investment in 2008

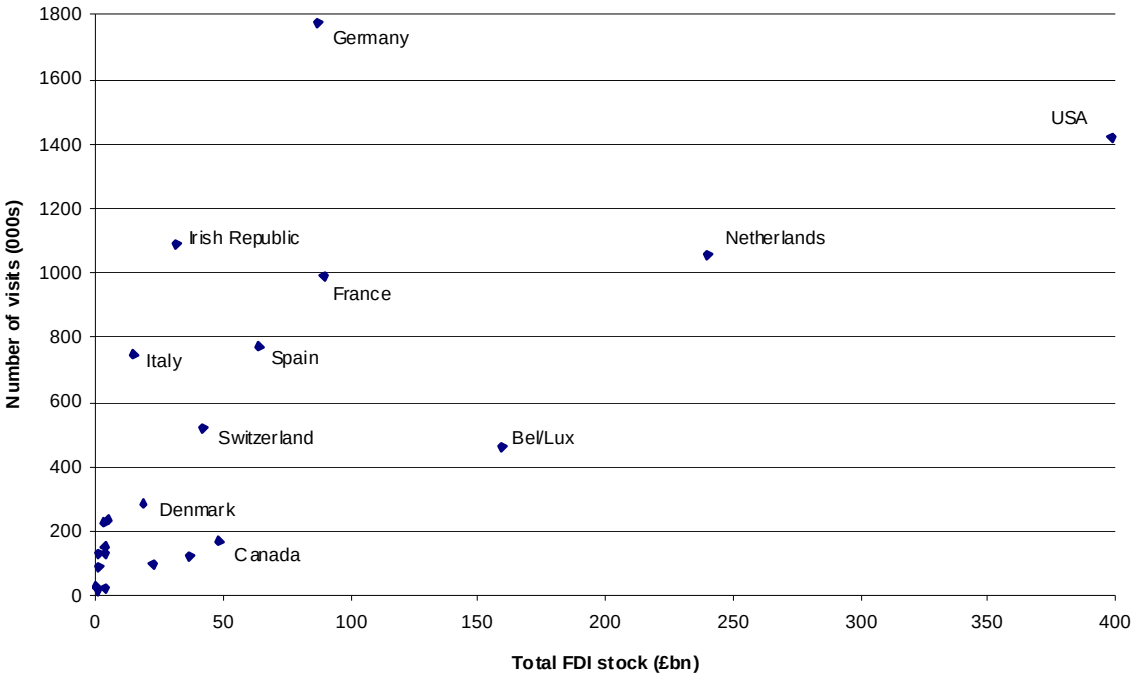


Source: Travelpac and Foreign Direct Investment and Statistical Bulletin, ONS.

Note: A negative inflow/outflow implies divestment out of the UK/foreign country in 2008.

156. Furthermore, quarterly data for FDI flow or stock per country or groups of countries is not available for the econometric analysis.

Figure 3-8 Number of visits by business passengers to and from the UK and stock of foreign direct investment in 2008



Source: Travelpac and Foreign Direct Investment and Statistical Bulletin, ONS.

Econometric modelling of business air travel demand

3.37 Previous econometric analyses have established that demand for business travel is closely related to national and global economic development.[157] However, more price-sensitive behaviour by some business passengers, such as downtrading to non-premium class travel, appears to have been exacerbated by the recent economic downturn (see Table 2-4). This may suggest that the proportion of business passengers showing some price sensitivity has increased over time and other studies have indicated that this appears to be more evident on short-haul routes.[158] Based on IPS data from airports surveyed between 1993 and 2010, this section presents an investigation of UK business air travel demand elasticities by geographical market, and whether there is evidence that they have changed due to the recession.[159]

Demand drivers at the macro and micro levels

3.38 Demand elasticities measure the strength and direction of individual or market response to changes in a given demand driver such as price, income or quality of service. Because of the difference in demand characteristics by business passengers on short and long-haul international flights and by origin of traffic flow, business travel demand to and from the UK has been modelled separately for three broad international market segments (EU25, North America and Rest of the World) and by passenger country of residence (UK or foreign).

157. See, for example, Department for Transport: *UK air passenger demand and CO2 forecasts*, (2009) and Annex 3-2 for a review of empirical evidence.
158. See, for example, Cranfield University Department of Air Transport: *Changes in demand for air travel* (2006). www.airport-int.com/article/changes-in-demand-for-air-travel.html.
159. For estimates of demand elasticities for UK leisure air travel, see *Demand for outbound leisure air travel and its key drivers,* CAA (2005). www.caa.co.uk/docs/5/ERG_Elasticity_Study.pdf.

3.39 Generally speaking, demand for air travel is found[160] to have the following characteristics:

- Business passengers are more time sensitive and less price elastic than leisure travellers (as they have a higher value of time and are more concerned with maximizing productivity while travelling)
- Demand is more price elastic for short- than for long-haul travel (due to fewer substitution modes for long-haul travel)[161]
- Demand is less price elastic at a world region or country level, than at the level of a city- or airport-pair (since, in the latter case, more substitution possibilities – such as alternate destinations – exist outside the market definition)
- The absolute value of the long-run elasticity of demand (on both income and price) tends to be higher than the short-run elasticity (as consumers or companies may take time to adjust their behaviour in response to price signals)
- There is less price sensitivity at peak times than at non-peak times.

3.40 In discussing the demand behaviour for business travel, it is useful to distinguish between those 'macro' or high-level factors that influence the decision to travel or not and 'micro' factors that determine the choice of cabin class, airline or airport once the decision to travel has been made. At the macro level, there is a high correlation between the level of economic activity and demand for business travel (as shown in Figure 3-5). Factors such as price, exchange rate, modal competition and development of alternatives to travel (such as videoconferencing technology[162] may also affect business travel demand, although their influence may be less than broader economic drivers.

3.41 At the micro level, factors such as frequency, price, quality of service, ticket flexibility, convenience, reliability, strategic alliances, brand loyalty or corporate deals could affect business passengers' decisions on which cabin class, airline and/or airport that they will use for their journeys, and hence can also influence the dynamics of competition between airlines. This is discussed further in Chapter 6.

3.42 Given that demand for business travel is mainly driven by the economic environment and business confidence, while the price of travel itself should be relatively small compared with the potential returns from making a business trip, it is not surprising that the price elasticity of business travel demand has been found to be largely inelastic, (i.e. price of travel is not a significant factor in the decision to take a business trip or not). However, this contrasts with the observation of price sensitivity at the airline or route level, whereby travel buyers or passengers are increasingly seeking value for money when considering which airline and level of service they would use in order to meet their travel needs. The recently observed shift from Business to Economy Class suggests that more business travellers are willing to trade service quality in return for lower fares as more corporations reduce travel costs due to the economic downturn.

160. Gillen D.W., Morrison W., Stewart C.: *Air travel demand elasticities: concepts, issues and measurement*, Department of Finance, Government of Canada (2003). www.fin.gc.ca/consultresp/Airtravel/airtravStdy_-eng.asp.
161. Although for the UK, this reasoning is only likely to hold for destinations in mainland UK or near Europe.
162. See Chapter 7 of Part 2 for further discussion.

Has the recent recession changed the drivers of UK business air travel demand?

3.43 Research on the price elasticity of air travel demand at an aggregate level has identified various economic, demographic and geographic factors that may affect price elasticity estimation.[163] From the discussion in the previous section, and because of a lack of consistent data for some plausible determining factors,[164] only GDP,[165] air fares, and volume of trade[166] were included in the analysis as potential demand drivers for business travel. The data has been split by passenger residence (UK or foreign) and world region (travel to and from EU25, North America (NA) and Rest of the World (RW)), giving a total of six separate markets.

3.44 As discussed in the previous chapter, the recent global recession has had a significant impact on the UK business air travel market as companies cut back travel or sought alternative, cheaper travel options. This raises the question of whether the fundamental drivers of business travel demand changed in the light of the economic crisis. This has been tested by deriving an econometric relationship for business demand based on the period before the recession, and then assessing its ability to predict subsequent traffic given the actual values of the economic drivers.[167] Full details of the econometric analysis are presented in Annex 2.B.

3.45 In order to ascertain whether there is a structural break in the relationship, six regression models based on pre-recession quarterly data between 1993Q1 to 2008Q3 were estimated, and their performance evaluated by comparing the out-of-sample forecast of business travel demand with the outturn data over the period of 2008Q4–2010Q2 (a large discrepancy between the two would suggest the presence of a structural break). Table 3-8 compares the root mean sum of squares of the residuals based on an econometric relationship modelled from the preceding years with the out-of-sample forecast errors given the economic outturn data.

Table 3-8 Comparison of root mean sum of squares of residuals and forecast errors

	Estimated period 1993Q1 to 2008Q3	**Forecast period 2008Q4 to 2010Q2**
UK EU25	0.052	0.301
UK NA	0.060	0.336
UK RW	0.054	0.240
Foreign EU25	0.046	0.296
Foreign NA	0.067	0.199
Foreign RW	0.056	0.186

163. See, for example, Brons et al: *Price elasticities of demand for passenger air travel: a meta-analysis*, Tinbergen Institute Discussion Paper TI 2001-047/3 (2001).
164. For example, quarterly FDI data by country is not readily available.
165. UK GDP for business trips by UK residents, GDP from the relevant world area for business trips by foreign residents.
166. Without an appropriate and consistent index for globalisation, the volume of trade measure is used as a proxy for the extent of globalisation over time. It is posited that as the world economy becomes more globalised, cross-border trade in goods and services will increase over time which, in turn, is expected to drive the demand for business travel.
167. Another way of testing for any structural change in the underlying relationship is to perform a Chow type test of parameter constancy (of both the estimated intercept and slope coefficients) before and after the suspected break point. However, this was unlikely to produce conclusive results given the limited number of observations since the onset of the recent economic crisis.

3.46 The results suggest that a structural break may have occurred around 2008Q4, as the forecast errors for the later period are around three to six times higher than the residuals in the preceding period. Since there is such a small amount of data following the break, it is difficult to analyse with any accuracy how the relationships between business travel (the dependent variable) and its demand drivers (the explanatory variables) may have changed because of the economic crisis. However, the next section attempts to fit the simplest econometric model to the data, one where an intercept shift is introduced, corresponding to a 'step down' in demand at 2008Q4, over and above that which would have been expected from the observed changes in GDP, trade or fares.[168] It therefore assumes the presence of a one-off shock to demand, while leaving the relationships between the explanatory variables and business travel demand otherwise unchanged.

Relationships between business travel and demand drivers

3.47 Table 3-9 shows the results of the estimated long-run coefficients[169] for UK/foreign business passengers to and from the three geographical markets based on the ARDL approach to cointegration.[170] This approach allows a model to include other deterministic variables such as an intercept dummy variable, which will correspond to a 'step up' or 'step down' in demand over and above that which would be expected from the actions of the other explanatory variables. The results show that the dummy intercept shift variable is highly significant for all geographic markets and for both UK and foreign resident business passengers, indicating that its inclusion is likely to have improved the fit of the models to the data.

Table 3-9 Business passenger model estimation of long-run relationships

	EU25		North America (NA)		Rest of the World (RW)	
Variable	**UK resident**	**Foreign resident**	**UK resident**	**Foreign resident**	**UK resident**	**Foreign resident**
GDP	1.80*** [0.55]	1.16*** [0.22]	1.96*** [0.22]	0.65* [0.25]	1.40*** [0.32]	1.27*** [0.26]
Fares	0.18 [0.24]	-0.13** [0.06]	0.28 [0.26]	-0.28** [0.14]	-0.61* [0.33]	0.23 [0.18]
Trade	0.03 [0.38]	0.12 [0.09]	0.004 [0.01]	0.53** [0.24]	0.33* [0.19]	0.10 [0.11]
Intercept shift	-0.50*** [0.20]	-0.26*** [0.04]	-0.32*** [0.05]	-0.13** [0.06]	-0.34*** [0.10]	-0.19*** [0.06]

*Notes: Asterisks indicate statistical significance: *=10%; **=5%; ***=1%.*

Figures in square brackets indicate standard errors of the estimated coefficients.

168. This is achieved by introducing a dummy intercept variable, which takes the value of one from 2008Q4 and onward and the value of zero otherwise.
169. These long run coefficients represent the equilibrium relationship between the dependent and explanatory variables. Since the variables are all in logarithmic form, these coefficients also represent long run elasticities of the variables involved.
170. See Pesaran, M.H. and Shin, Y.: *An autoregressive distributed lag modelling approach to cointegration analysis*, in S. Strass, A. Holly and P. Diamond (eds.), Centennial Volume of Rangar Frisch, Econometric Society, Cambridge University Press, Cambridge (1995). See Annex 2.B for further details.

3.48 Given the limited number of observations since the onset of the recent recession,[171] model stability has been tested by using an approach based on recursive residuals.[172] The test indicates that the models presented in Table 3-9 are sufficiently robust in forecasting business travel demand since 2008Q4 and, therefore, that there is no strong evidence to suggest that the long-run relationship of business travel with the underlying demand drivers has been changed by the recession (apart from a step change in the intercept). This seems to suggest that the relationships between business travel demand and GDP, fares and trade have not altered significantly due to the recession, other than to experience a one-off 'step down' in demand around the end of 2008 (over and above that which would have been expected from the observed changes in GDP, trade or fares).

3.49 However, it is difficult to conclude from the data currently available whether the step change in demand suggested by the above analysis is temporary or permanent. It is likely that the intercept shift variable is, in part, capturing the way the current recession particularly affected those sectors of the economy that generate the most business travel,[173] and as these sectors recover so 'step up' might be expected. It is possible that business travel may have been permanently affected by the events of the recent recession[174] (but there is insufficient data currently available to verify this). Alternatively, it may be that the impact of the shock is more temporary, and that business traffic will revert to its pre-recession level and trend growth over a relatively short period of time.

3.50 However, given that the inclusion of an intercept shift variable seems to fit the data relatively well, the remainder of the chapter examines the other model outputs and compares them to the results of similar studies.

3.51 The estimated long-run GDP elasticities shown in Table 3-9 are all positive and highly significant with magnitudes greater than unity for all 'UK resident' business passengers across the three geographic markets, indicating that economic activity remains an important driver for business travel.[175] All else being equal, the responsiveness of business travel by UK residents to GDP growth is strongest for the North America market where a 10% rise in GDP will increase business traffic by almost 20%, compared with 18% and 14% respectively for the EU25 and Rest of the World markets.[176] The GDP elasticities for 'Foreign resident' business passengers are also highly significant, but relatively less elastic than their UK counterparts, with estimated elasticities ranging from 0.65 to 1.27.

171. Ideally, one should test parameter constancy of both the intercept and slope coefficients of the model but limited availability of post-break data makes this approach difficult. (See also footnote 171.)
172. Essentially, it checks that estimated traffic for the period after the structural break is within a reasonable range of the actual outturn. Brown et al: *Techniques for testing the constancy of regression relationships over time,* Journal of the Royal Statistical Society, Series B, 37, pp. 149-172 (1975).
173. Particularly the banking, finance and insurance sectors. The model results suggest the intercept shift is equivalent to a one-off drop in demand of around 20%, and it seems unlikely that none of this will be recovered.
174. Possibly such a change could result in the slope coefficients taking different values before and after the recession, although there is as yet no evidence for this.
175. That Trade was not significant for two of the three UK resident markets may have contributed to the size of these GDP elasticities.
176. The difference between elasticities for the different world areas is also influenced by variations in the mix of business activity associated with each market which, in turn, give rise to different levels of business travel associated with a change in UK GDP.

3.52 Volume of trade (in goods only) appears to be a statistically significant factor in determining business travel for only two of the six markets considered (Foreign NA and UK RW),[177] when trade appears as a statistically significant factor, the results suggest that demand for business travel is relatively less elastic with respect to trade (than with GDP) with elasticities of 0.53 for foreign residents in the NA market and 0.33 for UK residents in the RW market.

3.53 The results suggest that 'Fares' is not a significant variable influencing business travel demand at an aggregate level, as opposed to decisions at a micro level on choice of airline and cabin class. It appears to be statistically significant in three of the six markets (Foreign residents in EU25 and NA markets are significant at the 5% level while UK residents in RW market is significant at the 10% level only) and, even there, the relatively small magnitude suggests that business passengers are price inelastic. In particular, a 10% increase in fares alone is expected to result in only 1%–3% fewer foreign resident business passengers in the EU25 and NA markets and 6% less UK resident travellers in the RW business market, while no noticeable reduction in business traffic is seen in the remaining three markets.[178]

3.54 These findings[179] – that demand for business air travel is largely price insensitive but elastic with respect to GDP growth – are consistent with industry assumptions. Although evidence on UK-specific business air travel demand elasticities is sparse, GDP elasticities varying between 0.65 to 1.96 are within the range of estimated GDP elasticities as reported by other UK and non-UK focused studies. Similarly, the estimated price elasticities of -0.13 and -0.28 for the two markets (foreign residents in EU25 and NA) appear to lie in the lower end of the spectrum while the price elasticity of -0.61 for UK residents in the RW market appears relatively high in comparison.

3.55 The next chapters look more closely at the way that businesses arrange their air travel and their relationships with travel management companies.

177. Quarterly data on UK trade in services by country or country group was not available for the whole sample period. In addition, given the high correlation between trade and GDP growth over time, it is difficult to separate out the effect of trade on business travel demand from that of GDP. These two shortcomings may have contributed to the limited explanatory power of the trade (in goods only) variable found in our regression models.
178. Another reason for the statistically insignificance of price in general is that accurate information on the fare paid by business travellers are difficult to obtain since factors such as corporate discounts and tickets booked by others may also obscure the true cost of travel.
179. See Annex 2.C for a review of empirical findings by others.

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Part 2 Chapter 4 Managing business travel

Chapter summary

- Winning new business and maintaining customer relationships is clearly a key driver for corporate travel, but travel for internal meetings can also be a significant component. There seems to be little evidence that businesses specifically quantify the return on travel expenditure.
- Business travel policies are aimed at securing the most cost-effective travel taking into account staff well-being, efficiency and remuneration. Long-haul trips appear to be more tightly managed than short-haul and road or rail. Encouraging employees' compliance with travel policy can be a challenge.
- Businesses may behave differently depending on travel spend and industry. Differences can also be observed between private and public sectors. Businesses with significant travel spend are likely to employ dedicated managers for travel policy and procurement, or use a travel management company (TMC).
- Companies with sufficient buyer power negotiate directly with airlines for volume discounts. The level of discount seems to vary widely, but can be substantial, and is generally based on projected travel volumes. Companies typically contract with multiple airlines to give the necessary choice and route coverage. While the structure of deals varies by airline, there has generally been a significant change over the last ten years, with discounts no longer likely to be given retrospectively based on total spend. Increasingly, companies have also encouraged employees to consider what other fare options are available 'on the day'.
- On shorter trips air travel has become more commoditised; the choice of product is more dependent on price than on other differentiating features, benefits and value-added services, and travel has become more like other procurement items. Some no-frills airlines have begun offering tailored deals to individual companies either direct or through intermediaries.
- The individual traveller's choice of travel is primarily determined by an amalgam of convenience, cost, ancillary services and frequent-flyer mileage.
- The economic downturn reinforced companies' focus on cost-effective travel, and some elements of tightened travel policies seem likely to persist. There seems to be a general acceptance that demand for Business Class on short-haul trips will never recover; a structural shift was already observable before the recession. Public sector spending cuts are expected to have a significant impact as this has been an important sector of business travel.

Introduction

4.1 For many firms, travel by employees is an integral part of doing business. This chapter considers what motives there are for business trips requiring travel by air, and how businesses manage that travel, including through staff travel policy. (The use of travel management companies (TMCs) is the subject of the next chapter.) The chapter goes on to examine the deals that businesses negotiate with airline suppliers, what drives and constrains the choices that individual travellers make, and how behaviour has changed with the recent economic downturn. Finally, it considers the characteristics

distinguishing smaller firms from larger firms in the market for business air travel, and whether public sector organisations behave differently from privately owned companies.

4.2 The source information for this chapter is drawn largely from interviews with representatives of travel buyers, TMCs, airlines and airports, backed up by published survey evidence where available. However, discussions around procurement are necessarily of a confidential nature, making it difficult to find corroborating evidence or to publish information in other than the most general terms.

Managing business air travel

4.3 The way a business manages its travel is likely to depend on the size of its travel requirements in terms of spend and transactions, rather than on its size in terms of employees or turnover.[180] With that caveat, a significant difference between small and large businesses is that small businesses tend not to have a dedicated travel or procurement department, and travel is typically managed as part of other duties by personal assistants to senior management. Small businesses are also unlikely themselves to secure much in the way of negotiated discounts, because of their limited travel spend.

4.4 This can be contrasted with large companies employing dedicated managers overseeing travel and its procurement. Forming part of the support services of the business, travel managers are typically responsible for travel policy and managing the travel budget and supplier agreements, usually supported by a TMC, which in some cases may have staff located on the premises (an evolution of what was once a travel agency 'implant' in the company). Spend on air travel would make up part of an overall travel budget which could include scheduled airlines, private aircraft charters, hotels, rail, car hire, ground transport and so on. (Data collated by the Guild of Travel Management Companies shows that 42% of 2010 transactions by member TMCs were air bookings.[181]) The administrative arrangements may also depend on the extent to which travel is managed centrally; for example, the UK office of some companies is sometimes responsible for bookings made by offices in other parts of Europe, or EMEA (Europe, Middle East and Africa).

4.5 A December 2008 survey[182] of 2,200 business travellers found that the average monthly spend per individual on business travel in 2008 was £839, with an average of 8.2 days a month spent travelling. It also found that Chief Executives travelled the most, with an average of 16.3 domestic and international flights a year.

4.6 Where a business is buying a significant volume of air travel, the resulting spend should allow it to secure fare discounts (or more value) in exchange for a commitment to place a certain amount of business with the airlines concerned. The TMC will act as adviser and sometimes negotiator, although it is more common for the deals to be negotiated directly between the procurement department and airline. There has also been a trend for businesses to compare their negotiated rate with the best fare available at the time of booking, particularly as no-frills airlines have become increasingly accepted by business travellers as an alternative for short-haul flights. These issues are discussed below in more detail.

180. For example, the UK arm of the Japanese electronics firm Nintendo has only around 25 regular travellers, mostly requiring travel to the company's European headquarters in Germany. Source: *Bring on the Battle,* Buying Business Travel (July/August 2010).

181. Year ending September 2010. GTMC membership covers around 80% of business travel spend in the UK, including the 30 biggest TMCs. See Figure 5-1 in Chapter 5 of Part 2.

182. Barclaycard Commercial: *13th annual Barclaycard Commercial Business Travel Survey* (December 2008) surveying a nationwide sample of Barclaycard Commercial card holders. A total of 2,202 respondents (CEOs, chairmen, non-executives, financial directors, executive directors, managers and personal assistants) provided their thoughts on all aspects of business travel. www.newsroom.barclays.com/Content/Detail.aspx?ReleaseID=1572&NewsAreaID=2

4.7 One theme emerging from research for this study is that short-haul air travel has become more commoditised; in other words, the choice of the product is more dependent on price than on any differentiating features, benefits and value-added services. Although the TMC has an important specialist advisory role, the actual procurement of travel is increasingly being handled by procurement specialists.

Case Study: BT's travel account

BT has one of the largest corporate travel accounts in the UK, spending more than £100m on business travel in the year 2008/09. To manage this cost effectively and to ensure that BT's duty of care is fully covered at all times, all travellers are mandated to use preferred suppliers when booking travel. BT has a clear strategy that all travel is booked using the 'best fare on the day'[183] and says that there is clear evidence that significant savings can be achieved when travellers plan and book in advance. Travel policy and guidance for its staff is set out in BT's Global Travel Policy.

American Express Travel Services (contract period 1 August 2003 to 30th September 2012) is responsible for managing BT's air programme and associated travel and VIP services. BT negotiates its own deals with airlines. Its current programme includes deals with major airlines including BA, bmi, Continental and Virgin Atlantic, which are renewed annually. BT has also recently reached a deal facilitating business travel for its staff on easyJet. Although there is no specific fare discount, easyJet is confident of providing significant cost savings based around BT's 'best fare on the day' policy.

Source: BT website www.selling2bt.bt.com/working/what/travel.htm (October 2010) and easyJet ties up BT corporate deal, www.travolution.co.uk (9 September 2010).

Motivations for business travel

4.8 An analysis of CAA Passenger Survey data in Part 1 of this study[184] showed that the most frequent responses given for the main purpose of business travel were internal meetings (broadly one third of responses) and meetings with external clients (broadly a further one third).[185] The survey data covered 1999–2001 and 2005–2007, with similar results for each.

4.9 The proportions are broadly similar in the CAA's 2008 and 2009 surveys of the four main London airports. However, because of the overall decline in business passenger numbers between 2008 and 2009, in terms of actual numbers there were around 1.5 million passengers fewer meeting external customers in 2009 compared with 2008, and 2.0 million fewer travelling for internal meetings. Therefore, the effect of the recession has been to reduce significantly the number of business passengers travelling for external and internal meetings, but with the proportions of business travel overall that such passengers represent remaining broadly the same.

183. See paragraphs 4.48–4.54.
184. See Table 4.2 in Part 1
185. Other categories were Conferences/Trade fairs (c10%), Overseas employment/Home leave/Armed services (c8%) and General business (c12%).

4.10 A benchmarking survey of travel policies and practices by UK organisations commissioned by Barclaycard Business in October 2007[186] showed that working at different sites of the company was given as one of the reasons for travel by 58% of organisations, and this rose to 73% if organisations with fewer than 1000 employees were excluded. This compares with between 46% and 57% of organisations giving sales, marketing or client servicing as one of the reasons for travel (broadly the same for larger organisations). However, these figures are not directly comparable to the results of the CAA survey, since this survey covered travel by all modes, not just by air, and it allowed multiple responses (on average, each respondent gave just over three reasons for travel).

4.11 Research by Cranfield University for the Omega partnership's Project Icarus[187] in November 2008 included a survey of how companies satisfied their need for meetings (Table 4-1). The table shows how important travel is for establishing new business and maintaining customer relationships. It also confirms that travel is significant for internal company reasons, albeit as part of a mix with telecommunications.

Table 4-1 Meeting motive by mode

	Mostly travel	Mix of travel and telecoms	Rarely travel
New business relations	57%	40%	3%
Internal process development	10%	78%	12%
Day-to-day management contact	6%	52%	42%
Training	23%	56%	22%
Conferences	67%	26%	6%
Customer service provision	34%	46%	20%

Source: Final Report Project Icarus, Cranfield University for the Omega partnership (November 2008).

Note: Based on an on-line survey of 129 travel manager members of the Institute of Travel and Meetings. The majority of respondents were from large organisations, with 58.9% employing more than 10,000 people worldwide.

4.12 All these results depend on how broadly respondents defined 'internal'. Global companies, such as those providing financial services, would make up a large part of business travel in dense markets such as London–New York or London–Hong Kong, as they would be likely to have regional headquarters in major cities and internal travel naturally tends to focus on connecting the offices of the company concerned. Thus the travel could be internal only in the sense that each regional headquarters is under one company umbrella; smaller companies interacting with business partners might label the equivalent travel as external. It should also be recognised that at least some of the 'internal' travel is likely to be inextricably linked to services being provided to an external client, in the sense that the travel would not otherwise have occurred without that link. For example, many overseas trips may involve sales teams coordinating with other sales teams within the company that are closer to the client.

186. *Barclaycard Business Travel Policy Benchmarking Survey*, based on an Illuminas Expense Management and Travel Policy Benchmarking Presentation commissioned in October 2007.

187. Cranfield University Business Travel Research Centre: *Final Report Project Icarus – A carbon reduction framework for buyers of business travel* (November 2008).
www.omega.mmu.ac.uk/Downloads/Final-Reports/Project%20ICARUS%20-%20Final%20Report.pdf
Omega is a publicly funded partnership that offers impartial, innovative and topical insights into the environmental effects of the air transport industry and sustainability solutions.

Measuring return on business travel

4.13 The discussion below records that business travellers are highly time sensitive. Unsurprisingly, businesses will tend to weigh the benefits from a trip – such as the potential for generating new business – against the potentially unproductive time employees spend away from the office. This manifests itself in travel policies which allow air travel for short-haul journeys over a certain length or duration, and which focus on direct rather than cheaper indirect flights. Policies allowing Business Class travel take into account the ability for employees to work en route (at the airport and in flight) and to arrive sufficiently rested to minimise recovery time and maximise time spent with the client or supplier etc. However, research for this study revealed little formal quantification by businesses of the return on travel expenditure in terms of, for example, potential revenue from a client – even where a judgement is made beforehand as to whether there is a sufficient business case justifying the travel. Of course, for some businesses, the price of travel, while significant in aggregate, might be small relative to the potential value of a big deal.

Company travel policy

4.14 The means and price of travel is likely to be governed by company travel policy. Travel policies naturally vary widely between companies. Their purpose is usually to achieve the most cost-effective travel, but they also have a bearing on staff well-being, efficiency and remuneration. As noted above, cost effectiveness may be consistent with the use of a premium product where the benefits outweigh the additional cost, although this tension has been exacerbated by the economic downturn and a greater focus on travel costs.

4.15 Depending on the business, long-haul trips may be less frequent than short-haul, but they potentially incur much greater travel spend (in terms of air fare as well as being more likely to include overnight accommodation and meals). There is also greater potential for long-haul journeys to be more complex where the options available and the booking process itself may be less straightforward. Therefore, they are more likely to be subject to greater oversight by travel managers and travel policies. The class of travel is sometimes mandated according to flight time, specifying when Premium Economy, Business Class or (more rarely) First Class can be used. On shorter trips, travel policies are increasingly influencing or dictating the choice between air and rail travel, depending on the length of journey and the quality, reliability and price of the rail alternative. A travel policy mandating bookings through the TMC also facilitates a company's exercise of its duty of care to travelling employees by providing information in the event of disruption or incidents, tracking their whereabouts, and so on.

4.16 A company may have access to negotiated discounts on fares, either through its TMC (see Chapter 5) or a bilateral deal direct with the airline. It may also recommend the use of 'best fare on the day' (see paragraphs 4.48–4.54). Encouraging the use of discounted fares may not necessarily require the use of a particular airline, although this can sometimes be a feature. Instead, the travel policy may relate to price rather than airline, requiring specific management authorisation where the chosen fare is significantly higher than the discounted fares available from the travel office.

4.17 One large company explained that its travel policy was common to all employees, because a system based on seniority risked creating a 'them/us' culture within the company, making the policy more difficult to enforce. It also complicated the negotiation of rates with airlines if these had to cover a range of products. However, such divisions reportedly continue to exist in some industries (such as the banking or financial sectors) where premium travel is part of the negotiated remuneration package for some grades and seen as necessary for staff retention.

4.18 The research by Cranfield University for Project Icarus[188] referred to earlier in this chapter included a survey of companies on travel policy or requirements affecting road, rail and air travel (Table 4-2). Companies were asked to classify the level of existing policy into three categories: no guidelines, 'encouraged' practice and a required corporate policy. The results show that road and rail travel are more lightly managed than air travel, probably because of the expense of air travel relative to other modes, at least on longer journeys, but also because of the much wider range of products and prices available for air travel giving significant potential for savings from exercising some control. Around 70% of companies had a mandated policy for air travel, with 74% mandating economy travel in some form, whereas only 33% and 42% had mandated policies for road and rail respectively, and 40% had no guidelines at all for road travel. Long-haul trips were more tightly managed than short- or medium-haul. More than 75% either encouraged or mandated the use of particular airlines.

Table 4-2 Company travel policy requirements by mode

	No guidelines	Encouraged practice	Mandatory Policy
Road	40%	27%	33%
Rail	19%	39%	42%
Air			
Short haul (up to two hours)	16%	16%	69%
Medium haul (two to five hours)	12%	18%	71%
Long haul	9%	19%	72%
Air – Economy Class	6%	20%	74%
Preferred airlines	23%	40%	38%
Require advance booking	10%	57%	33%

Source: Final Report Project Icarus, Cranfield University for the Omega partnership (November 2008).

Note: Based on an on-line survey of 129 travel manager members of the Institute of Travel and Meetings. The majority of respondents were from large organisations, with 59% employing more than 10,000 people worldwide.

4.19 The 2007 Barclaycard Business benchmarking survey referred to in paragraph 4.10 also analysed company travel policies. It considered policies applying to air travel only and is a useful illustration of the typical position prior to the economic downturn. Although respondents were permitted multiple responses, a flavour of the variation in travel policies can be seen from Table 4-3 based on this survey.

4.20 Fewer than a quarter of companies in the sample[189] had a strict budget in place for air travel and, of those that did, 60% had a policy which differed depending on destination, and 54% had a policy which differed with employee seniority. Business Class was permitted for all employees on long-haul flights by 31% of companies and was permitted on all flights, mainly for senior employees, by 27%.

188. Cranfield University Business Travel Research Centre: *Final Report Project Icarus – A carbon reduction framework for buyers of business travel* (November 2008). www.omega.mmu.ac.uk/Downloads/Final-Reports/Project%20ICARUS%20-%20Final%20Report.pdf

189. The sample size is not given in the report.

Table 4-3 Corporate travel policy constraints

Policy	100–999 employees	1000 or more employees	Total
There are no guidelines in place for air travel	13%	2%	8%
At the discretion of the line manager	14%	21%	18%
Employees must book the most convenient option for travel, e.g. may not be the cheapest flight but avoids delay in returning to work	26%	16%	21%
Company has no actual budget for air travel but employees are advised that it must be a reasonable amount	30%	33%	32%
Employees must always go for cheapest flight on the day of travel	28%	34%	31%
Company has a budget that should not be exceeded for air travel	16%	26%	22%

Source: Barclaycard Business Travel Policy Benchmarking Survey of travel policies and practices of organisations in the UK, based on an Illuminas Expense Management and Travel Policy Benchmarking Presentation commissioned in October 2007.

Note: Companies appear to have been allowed to make multiple responses. Sample size was not given in the report.

4.21 Compliance with travel policy, and in particular how it could be undermined by the ability of employees to search, compare prices and book travel using the internet (as they would for personal travel) was a common theme from CAA discussions with travel buyers and TMCs. Greater compliance has risen in profile as companies have become more cost-constrained during the economic downturn and managers have focused on the potential for savings. Hence the enforcement of compliance with travel policy is likely to have been tightened further since these surveys, and conversely may be relaxed over time as cost constraints ease.

4.22 TMCs in particular see part of their value as realising for their clients the potential savings from greater enforcement of travel policy and use of technology such as self-booking tools, while also providing management information on travel spend and tracking or assisting employees in the case of emergency or disruption (see Chapter 5).

4.23 Of course, the travel policy needs to be framed so as not to create perverse outcomes. It has been suggested that some travel policies mandating the use of Economy Class (or blocking the use of Business Class) are not based on sound logic, in that they allow travel on a flexible economy ticket but not on discounted Business Class tickets which can be a cheaper option. In branding Premium Economy cabins, airlines have reportedly taken care to ensure that the word Economy is retained because of the way some travel policies are worded.[190]

190. For example, a United Airlines senior manager is quoted as saying, "The people who are choosing to fly in Economy Plus [United's enhanced Economy product, albeit not in a separate cabin] are the business travellers whose company travel policy is to fly in economy…", *Premium Bonds*, The Business Travel Magazine (May/June 2010).

Corporate deals

Overview

4.24 This section explores the nature of the agreements for volume discounts which are struck between airlines and businesses with sufficient travel spend. Such agreements are generally confidential, and so little information is available publicly. Consequently, as described in the introduction to this chapter, this discussion is largely based on interviews.

4.25 A deal is usually based on volume in terms of spend or number of sectors, and is one of various bulk-purchase arrangements including those negotiated with TMCs as well as leisure-specialist intermediaries such as tour operators. From the airline's perspective, the commitment to volume from a big customer is naturally an attractive prospect. One airline said that it can be 'critical' to a route to obtain such a commitment.

4.26 Airlines also offer bulk 'net' fare[191] arrangements to TMCs which TMCs can on-sell as discounted fares to clients. Such fares via a TMC appear to remain a significant part of airlines' business, despite the associated sales costs and the trend for larger companies to negotiate contracts direct.

4.27 The development of the corporate market has led to relatively sophisticated exchanges between the buyer, often advised by a TMC, and the airline supplier. Reportedly, some corporates deliberately keep the travel manager relationship with the supplier separate from the procurement process, so as not to cloud the procurement manager's cost-focused negotiations. It is left to relationship managers to liaise with the airline over ongoing customer issues around product and service etc. Because corporates are relatively heterogeneous groups of buyers with different needs, for example in terms of the routes that are of most importance, the airline's offer to them is, in general, individually tailored. Network airlines also want to avoid their product becoming commoditised to the point where one brand has no features that differentiate it from other brands, and where consumers will buy on price alone.

4.28 easyJet and Ryanair, the biggest no-frills[192] airlines serving the UK market, do not offer individually negotiated fare discounts. Their business models already rely to a great extent on driving volume through offering low fares, stripping out costs and complexity wherever possible (or creating a separate revenue stream for them), thus negating the need for a volume discount. Indeed, the labour-intensive aspect of corporate deals – because of the added cost from having to respond with individually tailored offers – runs counter to the low-cost philosophy. Nevertheless, these airlines are clearly aware of the potential for attracting business passengers, and easyJet is openly targeting a greater share of this segment with a tailored product (see the easyJet case study in Chapter 6). Part 1 of this study[193] showed that the combined share of short-haul international business passengers carried by Ryanair and easyJet rose from 3% in 1996 to 21% in 2007.

4.29 The tailored nature of corporate deals makes it difficult to summarise them in a meaningful way, but the following discussion attempts to give a flavour of typical characteristics based on research conducted for this report.

191. In the sense that these fares would originally – when fares were commissionable – have been net of commission and subject to the intermediary's own mark-up.
192. The term no-frills is used for convenience here to distinguish these airlines from network airlines, but it is accepted that they offer some 'frills', albeit at extra cost.
193. Figure 3.4 and paragraph 3.18 in Chapter 3 of Part 1.

Structure of corporate deals

4.30 In order to keep the frequency of negotiations manageable, corporate deals typically last between one and three years, with interim annual reviews. They can cover all cabins. The proportion of an airline's passengers travelling on business using fares negotiated through a corporate deal varies according to the airline and nature of the route; a further, probably more significant, proportion may be travelling using 'net' fares negotiated by TMCs and on-sold to companies. CAA survey data (2009) shows, for example, that 33% of business passengers with an origin/destination London–New York were in the financial services industry, while 21% of business passengers with an origin/destination Heathrow–Houston were in the oil industry. A large firm in these industries would be likely to negotiate direct for a significant volume discount.

4.31 On routes to and from UK points outside London, the proportions may be smaller, because fewer business passengers on those routes tend to be employed by companies with the necessary travel spend, although the proportion of business passengers from the public, education and healthcare sectors tends to be higher at regional airports than London airports. But, on the very limited information available, the CAA's research suggests that, in very broad terms, typically between one quarter and one half of premium passengers could be travelling at some kind of negotiated fare which is discounted from the published fare levels.

4.32 It was also clear from the CAA's research that the way corporate deals are structured varies from airline to airline, and this should be borne in mind in the following discussion.

4.33 The discount the travel buyer can expect is based on the value to the airline of the deal overall. Thus some airlines may offer a low fare conditional on acceptance of a contract covering a bundle of routes. Some airlines reportedly use markets where they are stronger to attract business traffic in markets where they are weaker. As well as fare discounts, the deal may cover extras such as loyalty cards or First Class travel for senior executives.

4.34 As part of the 'request for proposals', the buyer often provides relevant airlines with a summary of the anticipated number of sectors per year on the routes concerned based on historic data, and invites bids, leading to negotiated deals. Depending on the amount of information provided, the airline may be able to quantify how much potential business the buyer represents, and to identify how much of it the airline is currently receiving (thus indicating the airline's current market share and hence its bargaining strength, potentially influencing how attractive a deal it is prepared to offer). The request for proposals may be relatively complex, requiring the contract to cover items such as a process for handling complaints or commitments on environmental sustainability.

4.35 Once a deal is implemented, an airline is likely to monitor regularly through the year the business delivered by the company, taking into account the trading environment. Although it is unlikely that an airline would withdraw a deal mid-contract, the extent to which the predicted volume is fulfilled is likely to influence the terms of future deals. The airline will wish to be reassured that significant business is not being placed with its competitors, and may write into the contract that the customer or its TMC should supply data showing what potential volume it is missing out on.

4.36 In general, most of the corporate deals described to the CAA appeared to place the buyer under no hard obligation to meet volume criteria. The discount was given up front rather than retrospectively, with no 'clawback' if volumes were not achieved[194] and sometimes bonus payments for greater volume. Some airlines specified volumes in terms of growth targets and others used market share.[195]

4.37 This approach represents a significant change in the structure of such deals compared with the beginning of the decade when discounts were more likely to be given retrospectively based on total spend on the corporate account. This change seems likely to be connected to competition authority investigations into discounts offered to travel agents[196] and corporates.[197]

4.38 Applying the discount at the point of sale means that an airline can load into the Global Distribution Systems[198] discounted fares specific to a particular customer that are visible only to that customer's TMC. This allows the TMC to provide its client with a direct comparison with 'best fare on the day' on a single screen. There is general acceptance that the buyer may choose 'best fare on the day' over the negotiated fare if there is an advantage to doing so; this is discussed further in paragraphs 4.48 to 4.54.

Number of suppliers

4.39 A large multinational company would typically contract with multiple airlines, the number depending on the extent of its travel requirements. On individual routes where it will buy a lot of travel, the company is increasingly likely to negotiate deals with more than one airline to give a choice of price, schedule and supplier (for example, where flights on the first choice airline are full). Although this means more negotiations, it is likely to give the buyer a better chance of securing the best deal overall across a diverse set of journeys. The travel policy may or may not rank the airlines involved. This might depend on whether the deal is based on achieving a certain market share with a given airline compared with its competitors. An airline may prefer a market share target – if the corporate is prepared to share the relevant data – since an apparently stretching revenue target can be achieved relatively easily during an upturn.

194. Although isolated airlines reportedly still have a clawback arrangement.
195. Where targets refer to the proportion of business passengers on a particular route that fly with the airline, rather than the absolute number of passengers.
196. See footnote 235 in Chapter 5.
197. The Office of Fair Trading's summary of its investigation into non-linear discounts in BA's corporate deals, launched in 2003 and closed in 2007, gives some idea of the structure of BA's discounts at that time (www.oft.gov.uk/advice_and_resources/resource_base/ca98/closure/British-Airways2). It states that BA's corporate deals usually included some combination of up-front route-specific discounts (URDs) and back-end aggregate rebates (BARs), and sometimes only one or the other. It goes on to say "URDs are usually percentage discounts on published fares for specified booking classes on a specified route and are provided at the time of purchase on the basis that the corporate customer is expected to meet a certain target on that route (such as the number of journeys or spend) during the period of the deal. BARs are percentage discounts provided to the corporate customer as a rebate at the end of a set period (such as a year) based on the total air spend with BA during that period relative to a target. Typically higher rebate percentages are paid as higher targets are met. The rebate percentage applies to all eligible expenditure rather than just expenditure beyond the target. The terms of a corporate deal (such as the routes covered, the URD and/or BAR rates given and the targets set) vary considerably between customers, which may reflect their different needs." In May 2007 the OFT announced that it was dropping the investigation because it saw insufficient benefits for consumers in continuing (primarily because of a lack of evidence indicating that BA's corporate deals were likely to have a substantial foreclosure effect).
198. GDSs provide customers with, among other services, instantaneous information about the availability of air transport services and the fares for such services. They permit travel organisers, including TMCs and internet travel sites, to make immediate confirmed reservations on behalf of the consumer (with most, but not all, airlines).

4.40 However, the CAA's research did reveal one company which, instead of dealing with multiple suppliers, had obtained a very attractive discount by negotiating exclusivity with a given airline for a high volume commitment on a frequently travelled route. The example quoted involved the company purchasing 'miles' from the airline in advance and drawing down from this as required. In order to secure the necessary volume, the company would need to mandate travel on that airline, requiring strict enforcement of the company travel policy (the only exception being where the airline's flight is full).

4.41 Although there has been a trend towards more route-by-route deals with multiple airlines in the interests of securing the best deal, budget constraints mean there is greater pressure on travel managers to use resources more effectively. This could be why large multi-nationals – which might have deals with as many as 20 or more airlines – are increasingly negotiating deals on a regional or global basis. Anti-trust immunity allows airline alliances to offer corporate deals jointly on an alliance-wide basis. Buyers have the advantage of fewer points of contact, and potentially bigger discounts because of the greater, aggregated spend. A possible downside for individual airlines is that they may have less flexibility to tailor a deal than in one-on-one negotiations.

Level of discount

4.42 Volume discounts take two forms: either a fixed fare for the duration of the contract – although as noted above there will usually be provision for a review, typically after 12 months – or a percentage discount from the published fare. Travel buyers are likely to prefer the first because the fare is fixed over a specified period, while airlines are likely to prefer the second, as the discounted fare rises and falls with the published fare, allowing the airline to recover unexpected cost increases.

4.43 Airlines control inventory in each cabin using a set of 'nested' reservation classes (see Table 6-8). Each fare type is assigned to a specified booking class based on anticipated yield. Inventory is controlled such that the highest booking class in each cabin ensures access to the last available seat, while the capacity allocated to lower classes will be optimised for greatest yield, relying in part on past experience of bookings. So the lowest fares will be allocated to the lowest booking class and will sell out first (or on peak flights be closed out altogether).

4.44 The booking class is therefore an important consideration in negotiating a discounted fare as it will determine whether seats are available on busier flights. The customer's expectation is that there would be reasonable seat availability in the relevant booking class such that they would only rarely be forced to a higher, more expensive class or to another airline. Similar prices on different airlines may not be meaningfully equivalent if, near to the departure date, the availability of seats in the relevant class is significantly different between those airlines. Furthermore, fare conditions on some published fares can be quite onerous, for example requiring a Saturday-night minimum stay. Where the discounted fare is based on a published fare with such conditions, the negotiation may also include a waiver of those conditions.

4.45 CAA research suggests that discounts range widely depending on the relative strengths of the buyer and supplier, the terms of the deal (principally volume), whether there is a package of routes on offer, the reservation booking class and conditions of the fare, and the quality of product (in particular whether a flat bed is offered in Business Class). It is therefore difficult to summarise these discounts, not least because detailed information is hard to come by and subject to commercial confidentiality. It seems to be accepted that on long-haul services buyers could typically expect to achieve at best a 20% to 30% discount off the published Business Class fare on their busiest routes, but in the right circumstances a company offering

high volume could negotiate discounts up to 50% or substantially greater.[199] However, it was also suggested that some of the larger discounts available recently had been as a result of airlines suffering the most from the economic downturn offering unsustainable reductions in order to preserve market share in the face of demand that had softened significantly at the height of the recession. Discounts on short haul (to the extent they are available at all) appear to be generally smaller, the reason being that on short haul, schedule is as much a driver of passenger choice as price.

Mid-term renegotiation of corporate deals

4.46 There are mixed reports as to whether buyers have sought to re-negotiate contracts as a result of the downturn. The scope for renegotiation appeared to be linked to the relative strengths of buyer and seller – whether there were alternative airline suppliers, whether volume targets had been met (failure to meet targets might stem from the use of tactical fares on other airlines as well as cuts in travel during the downturn), and the strategic importance of the buyer. There were some reports of contracts being renegotiated. Other reports described renegotiations as taking place more where contracts came up for renewal or review anyway, albeit perhaps brought forward by a few months. There was agreement that buyers would take advantage of the downturn to force weaker suppliers to remedy any shortcomings in the supplier's service and to obtain a better value package, but it was also acknowledged that this instinct might be tempered in order to maintain good long-term relationships.

4.47 Some airlines were said to have pre-empted negotiations by offering very attractive fares to companies that they knew to be travelling in markets where they operated. It was also suggested that some buyers have simply switched to 'best fare on the day', and that some are no longer sufficiently resourced in travel management to engage in lengthy renegotiation of multiple contracts.

'Best fare on the day' policy

4.48 Traditionally, where a company has sufficient travel spend to warrant the negotiation of volume discounts with airline suppliers, it could be expected that a request for air travel through the TMC on a relevant route might have been booked with one of those airlines, which would have 'preferred' supplier status.

4.49 More recently, there has been increasing use of 'best fare on the day' (or 'lowest logical fare') policy. In contrast to automatic selection, this means that the employee will be presented with a series of fare options (according to choice of airline, schedule, etc.) that are available in the market at the time of booking and can choose that offering best value. In addition to the negotiated fares (where they exist), the options can include any fares negotiated by the TMC itself, and published fares (i.e. fares publicly available), including fares on no-frills airlines.

4.50 This allows the employee to take advantage of any 'tactical' special offer fares that airlines happen to be offering in the market at the time of booking, which might be both negotiated and published fares. During interviews for this study it was widely reported that the economic downturn had given rise to airlines offering tactical fares more frequently. These may have short selling periods and be relatively volatile in fare level, with the lowest fares occurring when business demand is traditionally lowest, such as the summer months. Such fares may also be characterised by conditions –

199. Given the range of published fare types available, each with its own price and conditions, a direct comparison needs to take account of whether more onerous conditions apply to the negotiated fare. For example, a published Carlson Wagonlit brochure *Public Sector Travel* recommends "Book CWT negotiated fares on long-haul journeys and save up to 50%. Restrictions are not that severe, but you will need to book a return with the same carrier."

inventory controls restricting the number of seats available at those fares, advance purchase requirements, a minimum stay period, penalties for reservation changes or cancellation, and so on. One TMC observed that fare volatility meant that in some cases, contrary to usual revenue management practice, fares selling a few days before the departure date could be lower than those available 10 days earlier.

4.51 On short haul, the choice could include a range of no-frills and network airlines, with associated product differences. On long haul a lower fare might also mean accepting a trade-off in terms of product, in particular a less attractive departure or arrival time or the lack of a flat bed in Business Class. TMCs have been making use of technological improvements in order to present clients with fare options which are exclusive to particular websites alongside the fares accessed through Global Distribution Systems.

4.52 Companies already able to negotiate attractive discounts might see little need for a 'best fare on the day' policy, or might even be able to negotiate their own rates down temporarily to match a tactical fare. But for companies with less buyer power, use of best fare on the day might, temporarily at least, negate the need for a negotiated corporate rate.

4.53 That said, the short-term gain from a 'best fare on the day' policy may have some longer term negative implications for the company, because it will lose volume with its preferred supplier and potentially not deliver the revenue target or market share that formed the basis for the negotiated rate. This could impact the rates the company can negotiate in the future. The 'best fare on the day' may also be less attractive where travel plans need to be changed.[200] Not only do such fares often have penalties for reservation changes, they may also have stricter inventory controls (the fare is sold in a lower-priority reservation booking class than standard fares, and therefore sells out more quickly). This could mean that seats at the tactical fare have sold out on the new date of travel, requiring upgrade to a much higher fare, thereby negating any benefits from choosing the lower fare in the first place.

4.54 Depending on company travel policy, these considerations will be taken into account by the travel manager or TMC in advising and managing optimum travel choices on behalf of the company. A TMC may be able to highlight possible lost opportunities for savings from using 'best fare on the day' as part of its auditing process and management information provided retrospectively to the company.

Factors influencing travellers' choices

4.55 Once the decision has been made to travel, the individual's choice of travel options will be influenced by a range of factors, which are set out below.

Schedule

4.56 The decision is likely to be primarily influenced by a combination of time to get to destination, flight times and airline route network, with a strong emphasis on minimising time spent out of the office. Where a connection is involved, the schedule may be dictated by the choice of connecting flight and optimum connecting times at, and convenience of, the intermediate airport. The CAA sees little evidence that business passengers have become any less time sensitive and therefore more likely to take an indirect flight unless there are very significant benefits in terms of price or class of travel.

200. Carlson Wagonlit Travel estimates that companies typically change or cancel 20% to 35% of tickets. Source: CWT *Smart Travel Guide*.

Price

4.57 To some extent company travel policy and procurement are likely to determine the options available and therefore will narrow down to some extent the price options available. Traditionally, at the level of the individual journey, business passengers have been regarded as more concerned with schedule and convenience than price. However, there are increasing signs that staff have been educated to greater awareness of the potential for cost savings from informed choices, particularly following the economic downturn. Self-booking tools can also be used to introduce an element of 'visual guilt' (see paragraph 5.23). Therefore, while the firm's decision for an employee to make the trip in question may not be influenced greatly by price, there may be price sensitivity around the choice of airline and class of travel, for example.[201] That said, airlines also suggest that there may be some variation in this price sensitivity depending on the size and industry sector of the business concerned. An important consideration is ticket flexibility; airlines now offer a range of price options to passengers prepared to accept conditions and to plan travel around them (see Table 6-8).

Quality of service

4.58 Quality of service is particularly important on long haul, with the advent of the 'flat bed' seat in Business Class, which is a prime consideration on longer and overnight flights. As well as in-flight product, quality of service would include lounge access and ground facilities, transfers, general customer service and possibly aircraft type where there is a material difference. On short-haul routes, no-frills airlines have penetrated the business market and brought an awareness of the savings that can be achieved by flying on a restricted economy ticket, including on network airlines. This has led to much wider acceptance that flights of relatively short duration do not warrant an enhanced in-flight product if this means a significant difference in fare.

Departure/destination airport

4.59 The wide availability of services by no-frills airlines from South East airports other than Heathrow has given business passengers a wider choice of airports, at least on short-haul services. Such airports may be more convenient geographically, and they have gained wider acceptance generally among business passengers who might previously have considered only Heathrow (or, to some extent, Gatwick). Services at London City have also expanded, marketed on the basis that less 'dwell' time is required at the airport. The rapid expansion of services from UK regional airports in the last 10 years, including some long-haul services and connections with the global network via non-UK hubs, has also dramatically widened the choice available. Part 1 of this study[202] showed that between 1996 and 2007, Heathrow's share of total UK business passengers declined from 51% to 39%, while the Luton and Stansted combined share increased from 4% to 10%, and regional airports' combined share increased from 35% to 38%.[203]

4.60 However, time considerations may override any preference. For example frequency from a local airport may be low relative to that offered from London, or the use of

201. Table 3-6 shows the results of a CAA survey of travellers travelling from Heathrow for business purposes between August and December 2009. On the two long-haul routes surveyed, more passengers gave price as the main reason for the choice of airline than any other reason (although conceivably some passengers may have been aware that their company made use of a corporate discount).
202. Table 2.4 of Part 1. Source: CAA Passenger Survey, 1994–1996 and 2005–2007. Figures include passengers who were using the airport solely to connect to another flight. A review of more recent data shows that the proportions are much the same in 2009.
203. Part 1 of this study (Table 1.2.5 and Figure 1.2.4) also explains that while the number of business passengers using Heathrow increased over this period, this growth was almost entirely on long-haul flights, and was offset by a significant decline on domestic flights.

secondary airports at the destination by some no-frills airlines may negate the advantage because of poorer surface access between the airport and the ultimate destination.

Frequent-flyer programmes

4.61 Airlines use frequent-flyer programmes (FFPs) to promote brand loyalty and to build customer relationships. The FFP is aimed at influencing the choice of the passenger as an individual, since the benefits will accrue to the passenger, not the firm that is likely to be paying for the ticket. The FFP will therefore have little or no impact on a company's purchase decisions.[204] While schedule and in-flight product will generally be the key drivers of choice, and travel policy may exclude particular airlines on cost grounds, if these factors are broadly comparable[205] then the FFP can be a powerful influencer of the individual passenger's choice because of the benefits it brings.

4.62 FFPs therefore clearly have the potential to work against company travel policy in terms of preferred supplier or cheapest option. The benefits include lounge access, upgrades and personal travel etc, but also, reportedly, status among peers. A 2007 survey of business travel managers by the Institute of Travel and Meetings (ITM)[206] found that 58% were "adamant" that personal traveller loyalty programmes such as FFPs influenced the purchasing habits of bookers/travellers, and a further 41% – virtually all other respondents – that there was a link on occasion between such schemes and the product chosen. It also found that 30% believed that such programmes would generally undermine their managed travel programme and a further 63% that they would sometimes undermine it. Only 7% said that they generally had no influence. This demonstrates that the degree of flexibility which a company travel policy gives the individual passenger in choosing the airline and fare without requiring special authorisation is potentially very important for the company's travel management. As travel policies tighten the choice available, it might be argued that FFPs will be less influential, although frequent travellers can of course be members of more than one scheme, and this is more realistic as airlines consolidate FFPs within alliances.

4.63 Travel managers give the impression that they cannot easily police the influence of FFPs where travel policy allows a choice of airlines – despite the potential impact FFPs can have on travel budgets if a less than optimum choice is made. Employees may be able to give reasons (such as schedule) why they would like to travel with a particular airline, when the real reason is the FFP. It is also difficult for companies to intervene at the booking stage because individuals have personal membership and can claim points retrospectively if necessary.

Reputation, reliability and previous experience of airline

4.64 Greater airline competition has led to a wider range of products and services on both short-haul and long-haul routes, and has increased the likelihood that passengers will consider flying with a different airline. However, reputation (for example, how the airline will handle problems when things go wrong) may play an important part where the passenger has a choice. A perception that an airport or airline is less likely to be subject to operational disruptions or delay may be more important than, say, the quality of in-flight product on a short flight. Airlines tend to highlight punctuality in their strategies for attracting more business passengers.

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204. One potential influence that airlines can achieve at the corporate level is that a corporate deal might include value-added 'extras' that include premium frequent-flyer programme membership status for selected employees. Separate company-based loyalty schemes exist, aimed at smaller companies.
205. For example, a travel policy might allow a choice of airline within a 10% range of the lowest fare. And of course not all employees will necessarily adhere to travel policy.
206. Institute of Travel and Meetings: *Exploring Personal Loyalty Programmes in Travel and Meetings* (updated May 2009).

The effect of the economic downturn on behaviour

4.65 Chapter 2 described the huge impact which the economic crisis had on business air travel, although company air travel policies and the behaviour of business passengers were already changing prior to the downturn, evidenced in the shift away from short-haul premium travel. The downturn has turned the spotlight on company travel costs and there is greater awareness of the potential for savings through 'smarter' travel management – whether this be a more restrictive travel policy or tighter enforcement of existing policy. Therefore, it seems likely that even if business travel in premium classes returns in time, companies are unlikely to move away from best practice, in the form of greater use of 'best fare on the day' or mandating the use of preferred suppliers. One large company said that widespread pre-trip approval was being retained to ensure a good justification for business trips, such as meeting clients. One TMC said that travel policies were likely to remain stricter for the time being, particularly for 'routine' travel. This may have implications for whether airlines are able to achieve the same yields, at least until corporate memory fades and travel policies slacken.

4.66 There seems to be a general acceptance that demand for Business Class on short-haul routes will never recover; and that, prior to the recession, a structural shift was already clearly observable.[207] As noted earlier, on short journeys many business passengers have developed an expectation of relatively low fares and an acceptance of economy class with few frills, confining Business Class on short-haul services to more of a niche market.

Corporate travel in specific sectors

Smaller firms

4.67 As noted earlier, a significant feature of the business air travel market is the volume discounts offered to companies with sufficient air travel spend to wield some buyer power. However, opportunities for smaller firms to obtain discounts are more limited.

4.68 Although it may not have a dedicated travel or procurement department, a smaller firm may still be able to benefit from discounts (or better value deals) by using a TMC.[208] As noted earlier, TMCs use their buyer power in order to negotiate discounts on fares, etc. which they can on-sell to clients, as do other wholesalers. These discounts are available to both large and small clients. As noted in the next chapter, the larger TMCs have recently been revamping their travel management programmes for smaller firms[209] so as to offer them a dedicated, separately branded product.

4.69 For the smaller firm, there is a balance to be struck between the additional costs of employing a TMC and the value the TMC is likely to add, given the more limited services that a smaller firm may need. A smaller firm may prefer the flexibility of making its own bookings using the internet, whether this be a company secretary using a company credit card or allowing its employees to self-book and to reclaim the cost on expenses. Management at a smaller firm is arguably more likely to have direct oversight of travel expenditure and to know where its employees are. A significant proportion of smaller firms are reported not even to have a company travel policy (Table 4-3 above).

207. It is interesting to note that BA acknowledged the possibility of a permanent change as far back as 2003, in the wake of the September 11 traffic decline, see for example page 11 of http://media.corporate-ir.net/media_files/irol/69/69499/ba_transcripts/Q20304_transcript.pdf

208. For example, see *Cut your business travel budget by 20%*, www.smeweb.com/finance/top-tips/cut-your-business-travel-budget-by-20-percent-021009.html (9 February 2010).

209. Although TMCs refer to 'SMEs', the definition of such firms seems to be based on annual travel spend (of the order of £3 million or less), which seems more appropriate than the usual SME definition based on employee count and turnover/balance sheet thresholds.

4.70 One consequence of firms self-booking is that it can be more difficult for airlines to identify and to gather customer information on bookings, whereas bookings through a corporate account and TMC are readily identifiable.

4.71 In the absence of TMCs, airlines may seek to attract smaller firms using loyalty schemes. There is no up-front discount on fares under these schemes, but the company (rather than the individual) earns points on every flight booked, whether direct or through travel agents. As well as encouraging brand loyalty, the scheme gives airlines greater information about the company's travel patterns.

4.72 For example, BA's *On Business* travel loyalty programme allows points to be aggregated and redeemed against any employee's future flights,[210] cabin upgrades and hotel vouchers. Employees still earn their own individual frequent flyer points. Other airlines/alliances have similar corporate loyalty schemes.

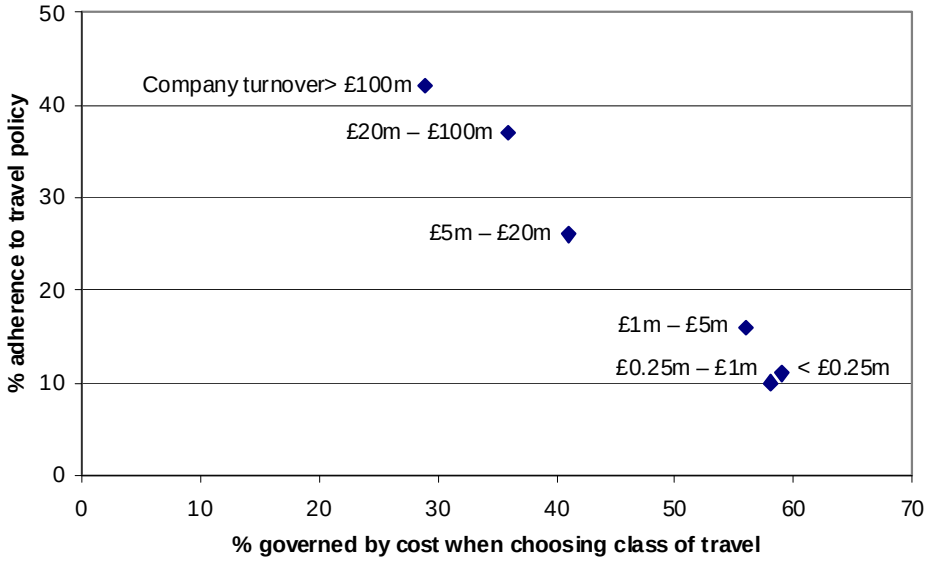
4.73 There is a further important consequence of the different circumstances around bookings by smaller firms. As noted earlier, smaller firms, by their nature, may be more likely to supervise travel costs closely. This could mean a travel policy specifying travel in Economy Class, choosing the 'best fare on the day', including no-frills airlines, and benchmarking what can be achieved through booking direct ('off programme') with what can be achieved through the TMC. Or it could mean a greater propensity to alter a travel schedule or combine multiple trips into one to achieve a lower fare.

4.74 As a result, airlines and TMCs generally regard business passengers from smaller firms as more sensitive to price (in terms of greater value, including ticket flexibility), although clearly this may be a relative comparison, depending on the type of firm or industry. Hence they see such passengers as more likely to be stimulated by price to upgrade to a higher class of travel or to switch airlines – but also that the actual decision to travel could be sensitive to price. In other words such passengers could be priced off a journey altogether.

4.75 These comments about the relationship between size of firm and cost-consciousness are illustrated by Figure 4-1. Based on a December 2008 Barclaycard survey of more than 2000 corporate travellers, it shows that the smaller the firm, the more the traveller is governed by cost when choosing the class of travel. It also shows that in larger companies, travellers are more likely to be adhering to a company travel policy.[211] The survey was carried out at the outset of the economic downturn and it is conceivable that the relationship has changed in the light of the greater cost-consciousness of larger firms discussed earlier in this chapter.

210. BA marketing material states that five employees flying Business Class to New York earn sufficient points for two employees to fly to Paris (excluding taxes, fees and charges).
211. This is also a finding of Table 4-3 above.

Figure 4-1 Relationship between company turnover and (a) adherence to travel policy and (b) cost constraints governing choice of class of travel



Source: 13th annual Barclaycard Commercial Business Travel Survey.

Note: Conducted in December 2008, from a nationwide sample of 2,202 Barclaycard Commercial card holders. www.newsroom.barclays.com/Content/Detail.aspx?ReleaseID=1572&NewsAreaID=2

Services from UK regional airports

4.76 Several industry representatives noted that services from UK regional airports showed noticeably different characteristics in terms of business passengers to those from London. In particular, the traffic base included fewer employees of large multinational companies, and particularly those from the financial services sector. Therefore, traffic overall on these services was more responsive to changes in price, and a link was made to the greater price-sensitivity of smaller firms described above. Firms based outside London have benefited greatly from the development of short-haul no-frills services from UK regional airports where, compared with previous option of connecting 'full-service' flights via a hub, not only is the journey now more feasible as a day trip without the need for an overnight stay, but also fares have fallen dramatically in the last 10 years.

4.77 The CAA has published two studies on air services from UK regional airports, in 2004 and 2007.[212] The studies highlighted the substantial growth in regional air services prior to the economic downturn. They noted that the improving 'visibility' of regions (as somewhere worth visiting or doing business) and their airports (as the region's gateway) had attracted more services flying to major business centres, including London, as well as to leisure destinations, and also to foreign hubs (which could be in the EU but also in the US or Middle East) that can provide an alternative to Heathrow as a connecting point to the global network. However, as Table 4-4 shows, there has been something of a decline in regional connectivity to near hubs following the economic downturn.

212. *CAP 754 UK Regional Air Services: a study by the Civil Aviation Authority*, CAA (February 2005), www.caa.co.uk/cap754. *CAP 775 Air Services at UK Regional Airports: an update on developments*, CAA (November 2007), www.caa.co.uk/cap775.

Table 4-4 Effect of recession on services between UK regions and international hubs

Hub airport	UK regional airports served			Average round trips per day		
	2006	2008	2009	2006	2008	2009
Amsterdam	19	17	17	73	64	63
Paris CDG	13	14	14	48	48	43
Frankfurt Main	4	5	4	18	18	14
Dubai	3	4	4	5	6	6
New York	6	6	6	9	10	9

Source: CAA Airport Statistics.

Note: The table shows routes with 500 or more one-way flights (in either direction) over the year, broadly equating to a daily weekday round-trip service.

4.78 The table shows that the main reductions have been in average frequency of service to hubs rather than the number of UK regional points served, and that the effect has been mostly seen at European hubs typically served with more frequencies per day. However, while this may have less relevance to leisure passengers, business travellers to and from the UK regions may find that these changes increase their expense, in both time and, possibly, the increased likelihood that their trip entails an overnight stay.

Public sector air travel

4.79 Although it can be difficult to generalise given the diverse range of businesses and organisations within each sector, interviewees for this study suggested that there are some key distinctions between public and private sector travel. The impacts of the economic downturn or other external factors on business travel are more likely to be felt first and most dramatically by the private sector, where the reasons giving rise to the travel may change quite suddenly. In the short term at least, public sector travel is more likely to be driven by particular, fixed events which are less susceptible to external factors.

4.80 Much of public sector travel is within the UK and therefore many potential air journeys have rail as an alternative. TMCs report a notable shift in this public sector traffic to rail, in part as a result of a permanent shift in travel policy,[213] and that, with the exception of the longest journeys (such as London–Scotland), rail now dominates. One TMC reported that fewer air and hotel bookings and more rail bookings had resulted in an 18% fall in public sector travel spend year-on-year for the first quarter of 2010, but with the number of transactions stable.[214]

4.81 For TMCs, public sector contracts – which may require complicated tender processes but have the potential advantage of providing more stable business and payments than the private sector – have been a large and growing component in the travel mix over recent years. For some TMCs, they have reportedly helped to mitigate the impact of the recession. The public spending cuts announced in 2010 will inevitably have significant implications for areas of discretionary spending such as travel budgets. Public sector job cuts alone will mean fewer people travelling. The

213. For example, Greater London Authority, DEFRA and Environment Agency policies on short-haul flights referred to at www.buyingsolutions.gov.uk/document/indexed/public/tinymce_uploads/travel/Sustainable%20Business%20Travel%20Policy%20Guidance%200.57.doc (section 2.8, Annex 3) and at www.environment-agency.gov.uk/news/119869.aspx.

214. *How is travel management in the public sector going to be affected by the looming budget cuts?* Buying Business Travel (July/August 2010).

Government plans to implement new standard guidance on travel policies, bringing them in line with industry best practice, to save £100 million a year. This will include reducing travel through the use of videoconferencing and telephone and eliminating First Class travel.[215] The Government has also announced greater centralisation of the procurement of commonly used goods and services. Centralised public-sector procurement of air travel is already offered through a national agency, Buying Solutions (see the case study below).

Case Study: Buying Solutions

Buying Solutions are the national procurement partner for UK public services, and were established in 2001. They are part of the Efficiency and Reform Group within the Cabinet Office.

The primary role of Buying Solutions is to maximise the value for money obtained by government departments and other public bodies through the procurement and supply of goods and services, aggregating purchasing where appropriate. Run on commercial lines, Buying Solutions generate income to cover costs and operate at no cost to the taxpayer. Buying Solutions have a range of offerings, including travel, fleet, IT, facilities, HR, financial services and consultancy. Travel encompasses air, ferry, rail, conference facilities, serviced accommodation and hotels. Procurement is based around framework agreements to ensure compliance with EU public-sector procurement legislation. Seminars were used to educate airlines about the key features of complying with EU legislation, in particular transparency.

Buying Solutions facilitate the process of securing the best deals available either through negotiating a deal direct with airlines or negotiating with the TMC. Their role also extends beyond value for money through procurement, to guidance on model travel policy documents to help organisations meet recommended minimum requirements. This includes how best to optimise travel as a means of communication with clients, how to meet travellers' needs including their safety and well-being, and how to approach sustainable travel. Through collaboration, Buying Solutions encourage all customers to have a robust travel policy as a keystone, tailored to their own needs, although Buying Solutions have no enforcement role.

Having grouped around 50 stakeholders with £80m of air travel expenditure as part of a Government Air Programme, Buying Solutions identified 600 of the denser city pairs which might be attractive in a tendering process and invited bids. Buying Solutions launched the Government Air Programme on 1 August 2009, with 30 airlines on around half of those city pairs, representing £50m expenditure. Typically, deals are for two years with an option to extend for up to an extra year, and the overriding driver is value for money. Discounts are a percentage off the prevailing published fare in a given booking class, rather than a fixed fare, and average 24%, maximum 80%. There are no guarantees given on volume, and public sector organisations are also encouraged to take advantage of other discounts available by choosing 'best fare on the day' if this offers better value for money.

Future developments to manage travel expenditure will focus on further aggregation of public sector expenditure to drive down costs, and demand management to reduce the need for travel.

Source: CAA interview with Buying Solutions, March 2010, www.buyingsolutions.gov.uk.

4.82 Despite the review, public sector spend on travel will remain a significant market, and public sector organisations under pressure to reduce travel costs could present opportunities for TMCs able to offer better management of travel.

215. Spending Review 2010 announced by the Chancellor of the Exchequer on 20 October 2010. www.hm-treasury.gov.uk/spend_spendingchallenge_ideas_taken_fwd.htm

4.83 Some interviewees for this study suggested that public sector travellers form a more significant component of business travel on services from UK regional airports. Table 4-5 uses CAA survey data to rank UK airports according to the proportion of business passengers using the airport who gave their employer as public sector or health/ education (sectors likely to include a significant proportion of public sector travellers). The table seems to support the contention that public sector business travel forms a more significant proportion at UK regional airports than at London airports. The top five airports are all in Scotland, Northern Ireland and Wales (by either of the measures used in the table, although the ranking changes) whereas London airports are towards the bottom of the table.

4.84 Nevertheless, there are clearly large differences between regional airports. The relatively low importance of public sector travel for the East Coast airports of Aberdeen, Humberside and Durham Tees Valley can probably be attributed to the significant traffic generated by the oil and gas industry.

Table 4-5 Proportion of public sector business passengers by UK airport

Airport	Survey Year	Public Sector	Health / Education / Public Sector
Inverness	2009	15.3%	26.6%
Belfast City	2006	11.4%	26.2%
Glasgow	2009	10.1%	23.3%
Cardiff	2008	9.8%	26.7%
Belfast	2006	8.0%	17.5%
Exeter	2008	7.7%	18.9%
Edinburgh	2009	7.6%	19.1%
Newcastle	2009	7.1%	21.1%
City of Derry	2006	6.8%	26.4%
East Midlands	2006	6.5%	18.4%
Doncaster Sheffield	2007	6.5%	11.6%
Bristol	2008	6.3%	15.6%
Gatwick	2009	5.9%	19.1%
Birmingham	2006	5.5%	21.7%
Liverpool	2007	5.0%	15.8%
Stansted	2009	4.6%	17.5%
Heathrow	2009	3.9%	16.7%
Manchester	2009	3.7%	16.5%
London City	2008	3.5%	9.0%
Prestwick	2009	2.6%	21.5%
Luton	2009	2.4%	15.8%
Aberdeen	2009	2.4%	8.4%
Durham Tees Valley	2009	2.0%	6.8%
Humberside	2007	0.4%	4.2%

Source: CAA Passenger Survey, 2006–2009.

4.85 The next chapter looks in more detail at the travel management companies which assist some businesses in their travel planning and purchasing.

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Part 2 Chapter 5 Travel management companies

Chapter summary

- Travel management companies (TMCs) have evolved from travel agents specialising in selling and booking business travel on behalf of airlines to travel consultants providing companies with a wide range of travel services, including advice on travel policy and procurement, and provision and analysis of management information.
- The three biggest TMCs in the UK each have annual business travel revenues of around £1bn; there is a long tail of smaller companies. Air travel represented 42% of TMC transactions in 2010.
- Cost pressures, exacerbated by the effects of the economic downturn, have required TMCs to show that the value they add in terms of services and achieving savings in travel budgets outweighs any additional costs.
- The TMC's role is increasingly one of travel consultant; much of the physical booking of travel can now be achieved through the use of automated self-booking tools for employees.
- Complex remuneration arrangements are based mainly on client management fees, transaction fees and 'gainshare' agreements, giving TMCs relative independence from airline suppliers; the old system of airline commissions and incentive payments has largely been replaced.
- TMCs use their buyer power to negotiate airline fares based on volume discounts, which TMCs can then on-sell to companies.
- The trend towards unbundling of ancillary services creates greater complexity for TMCs and travel buyers in managing travel and in contract negotiation. Until technology catches up, it makes it more difficult for buyer and TMC to compare prices for equivalent products and to capture meaningful management information.

Overview of TMCs

5.1 Business air travel is characterised by the use of intermediaries in the form of travel management companies (TMCs) which specialise in managing the business travel needs of companies. Although they evolved from travel agents specialising in selling business travel, their services often go beyond just organising travel tickets and itineraries. As an outsourced travel management and consultancy service, they may offer everything from advice on travel policy and procurement to provision and analysis of management information.

5.2 TMCs have therefore moved from being agents for airlines, remunerated on a commission basis, to travel consultants acting on behalf of corporate clients. Over time, TMCs began rebating some or all of their commission to their clients in exchange for fixed fees. It seems to be generally acknowledged that BA's *Fresh Approach* initiative in 2001 (described further below) was central to a fundamental change in the relationship between UK corporate travel buyers, business travel agents and airlines. In stages, BA removed commission payments leaving TMCs to compete for corporate business on the basis of the fees levied on clients and the service provided, including the value for money they can achieve through passing on savings negotiated with suppliers.

5.3 With clients facing greater pressure on costs, and demanding more for their money, particularly following the economic downturn, the challenge for TMCs has been to demonstrate that they can add value to the company sufficient to outweigh the fees through which they recover their own costs.

TMCs in the UK

5.4 Table 5-1 shows the 15 biggest TMCs by business travel revenue in 2009.

Table 5-1 Top 15 TMCs by UK business travel revenue

Company	2007 (£m)	2008 (£m)	2009 (£m)	2009 transactions (000)	2009 % on-line bookings	2009 staff
American Express	--	1,100	1,090*	--	--	5,724
Hogg Robinson Group (HRG)	1,100	1,100	1,080*	--	--	1,865
Carlson Wagonlit Travel (CWT)	1,038	1,200	1,003	--	--	1,390
BCD	460	410	405	950	21	537
FCm Travel Solutions	350	370	380	1,640	28	650
Portman Travel	296	365	302	1,300	35	505
ATP International	176	183	194	504	--	353
Capita Business Travel	132	151	145	1,203	51	200
Hillgate Travel	178	151	145	315	10	171
Uniglobe Travel	95	117	123	256	5	234
Reed & Mackay Travel	102	116	113	327	12	233
Co-operative Travel Management	70	101	102	515	23	209
Egencia UK	--	--	95*	--	85	114
Chambers Travel Management	63	66	71	235	46	92
Grosvenor Travel Management	54	58	51	91	2	58

Source: Buying Business Travel, 50 Leading TMCs, July/August 2010.

Notes: – indicates information not available.

** indicates figure derived from Buying Business Travel research.*

Figures include all types of travel etc and are not specific to air travel.

Staff numbers are expressed as full-time equivalent.

5.5 Table 5.1 shows that the market is stratified to some extent. The three biggest TMCs in the UK, American Express, Hogg Robinson Group and Carlson Wagonlit Travel, each have business travel revenue of just over £1bn. These are followed by three mid-ranking TMCs with business travel revenue in the £300m–£400m range. These are Netherlands-based BCD, FCm (owned by Australian travel retailer Flight Centre) and Portman Travel. There is then a long tail of smaller TMCs with business travel revenue of less than £200m. In 2009, the 15th ranked TMC (the last shown in the table) achieved business travel revenue of £51m, while the 50th achieved around £8m. In terms of 2009 staff numbers, only one TMC outside the top 15 had more than 100 full-time equivalent employees.

5.6 The effects of the economic downturn meant that in 2009 the business travel revenue for the top 50 TMCs fell by almost 10% compared with 2008. However, there was little consolidation among the top 50 TMCs during 2009 with only two acquisitions.[216]

TMC corporate clients

5.7 Although the bigger TMCs serve a wide mix of companies, their focus has traditionally been regarded as on larger, high-spend corporate accounts. Smaller TMCs have been regarded as concentrating more on smaller firms.[217]

5.8 Although their travel requirements will differ, as noted in Chapter 4, it is arguable to what extent the size of firm is in practice that relevant to the choice of TMC. TMCs generally maintain that they cover all market segments.[218] However, the bigger TMCs have recently been revamping their travel management programmes for smaller firms so as to offer them a dedicated, separately branded product.[219] Examples are Hogg Robinson Group's Simply HRG (launched September 2009), FCm's Corporate Traveller (January 2010) for companies with annual travel spend of between £5,000 and £1.5 million, American Express' aXcent (January 2010) for companies with annual travel spend of up to £3 million, and Carlson Wagonlit's CWT Connect Now (March 2010) for companies with annual travel spend of between £50,000 and £2 million.[220]

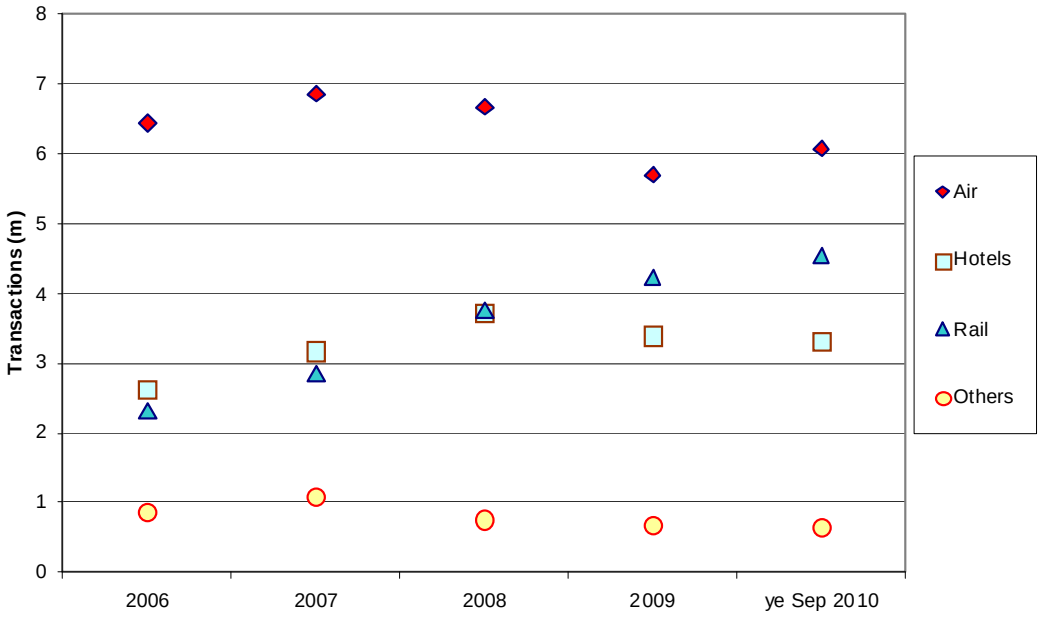
5.9 Smaller TMCs argue that this is a reaction to the economic downturn as bigger TMCs seek to attract smaller firms – perhaps firms which would not otherwise have considered switching from their local TMC.

216. Source: *50 Leading TMCs*, Buying Business Travel (July/August 2010).
217. See footnote 209 in Chapter 4. The definition of 'smaller firm' seems to be more around its annual travel spend (of the order of £3 million or less) than the more usual SME definitions.
218. For example, Carlson Wagonlit Travel has stated that 60% of its clients have an annual spend of less than £225,000, while American Express makes available its on-line booking tool and preferred rates irrespective of the size of firm. Source: *Bring on the Battle,* Buying Business Travel (July/August 2010).
219. To some extent this trend may therefore be more of a change in marketing emphasis than in the product itself.
220. Source: TMC websites, The Business Travel Magazine (May/June 2010), *Bring on the Battle,* Buying Business Travel (July/August 2010), *Amex joins the scrap for SME business* www.abtn.co.uk/news/0213716-amex-joins-scrap-sme-business (2 February 2010), and *Indie TMCs to fight big multiples for SMEs*, www.ttglive.com (17 September 2009). In early 2010 FCm's existing SME clients were reported as representing a total spend of £150m, source: Buying Business Travel (March/April 2010).

Air travel as a proportion of TMC business

5.10 The proportion of transactions which air travel represents for TMCs is illustrated by Figure 5-1, which is based on data from members of the Guild of Travel Management Companies. GTMC membership covers around 80% of business travel spend in the UK, including the 30 biggest TMCs.

Figure 5-1 Business travel transactions by GTMC members, 2006–10



Source: Guild of Travel Management Companies quarterly transaction survey.

Note: The survey is based on statistical returns by GTMC membership. Since the membership covers around 80% of travel spend and members may join or leave during the year, the survey gives an indication of general trends and relativities rather than absolute figures.

5.11 The chart shows how air travel dominated in 2006 with 52% of transactions, but that hotel and particularly rail bookings have become a much more significant part of TMCs' business, with air representing only 42% of transactions by the third quarter of 2010. The relative proportions are a factor both of shifts in demand and the way travel is organised. So, for example, as discussed in other chapters, there has been a shift from air to rail, and a general reduction in business air travel because of the economic downturn, but TMCs are also now better able to offer rail bookings through technological improvements. Hence rail continues to show a rise in bookings in 2010 despite the recovery in air transactions.

Services provided

5.12 TMCs have adapted their business models so as to diversify into providing a wide range of services covering all aspects of corporate travel – air/rail tickets, car hire/ transfers, hotel bookings and meetings – including travel management, planning and advice. Their aim is to exploit their knowledge, expertise and access to negotiated discounts from travel suppliers, and to tailor these for the client depending on travel needs, company travel policy and budget.

5.13 Depending on the size of the company and volume of travel, the TMC's services might include:

- advice on procuring travel; on travel policy including potential savings from best practice and proper policy enforcement; on duty of care and corporate social responsibility issues; and on educating travel bookers within the company on best practice (the advisory role is discussed further below)
- using their buyer power to negotiate their own volume discounts with airlines in the form of 'net' fares,[221] which they can then offer, with a mark-up, to companies, including those which have neither the resources nor the buyer power to secure such discounts; these negotiated fares are loaded by the airline in the Global Distribution Systems alongside existing equivalent 'published' fares[222]
- for straightforward bookings, providing desk-top access for employees to a portal with a 24-hour on-line self-booking tool (see paragraph 5.20 below) by integrating the necessary third-party applications with the company's own IT system; the portal also stores employee profiles, frequent-flyer details etc
- advice and booking service for more complex bookings, including finding the best value fares by sourcing from multiple systems
- billing/credit facilities through the IATA Billing and Settlement Plan (BSP)[223]
- data collation, management information reporting and analysis, and other non-transaction services, including environmental impact monitoring.

5.14 However, the TMC continues to face challenges. Over the last 10 years or so, employees have become used to making bookings for their own personal travel using the internet rather than a travel agent. The temptation is to research and book their own business travel in the same way. Chapter 4 explained that companies have had to adapt their travel policy – and perhaps to enforce that policy better – so as to ensure that travel is arranged and procured in the most cost-effective way. Consequently, TMCs have reacted by encouraging companies to deploy on-line self-booking tools for their employees to make straightforward bookings themselves, while the TMC takes a more strategic role through account managers to offer advice on the most cost-effective way of booking and travelling. These developments are discussed below.

Advisory role

5.15 The TMC's advisory role may take various forms, depending on the client company's resources. Chapter 4 explained that companies with significant buyer power, and sufficient resources and expertise in their procurement department, are likely to negotiate their own, company-specific fares direct with airlines. By analysing the company's overall spend and the airlines regularly used, the TMC can establish whether there is merit in negotiating such a corporate deal over and above the net fare the TMC itself has negotiated with that airline. For example, the airline might be willing to improve upon the TMC net rate in return for an improved volume share. The TMC can benchmark discounts against rates achieved by comparable clients. The TMC may even take the negotiating lead on behalf of the company, given the time-consuming nature of such negotiations, with a specific remit to deliver cost savings.

221. See footnote 191 in Chapter 4.
222. Although the negotiated fares are loaded in the GDS, they are only visible to the TMC for which they have been provided. 'Published' fares are visible to all users of the GDS.
223. The IATA BSP system facilitates and simplifies the selling, reporting and remitting procedures of IATA-accredited Passenger Sales Agents (which includes TMCs), and improves financial control and cashflow for BSP airlines (which may include non-IATA members). In short, agents/TMCs issue one sales report and remit one amount to a central point while airlines receive one settlement covering all agents. www.iata.org

5.16 The TMC will have expertise in understanding the multiplicity of airlines, air fares (published and net), and fare conditions available. For example, airlines control seat inventory using a system of reservation classes within each cabin, each giving different levels of seat availability, and each linked to a set of prices and fare conditions (see Chapter 6). The TMC can advise on how to optimise company spend through the use of cheaper fares where appropriate.[224]

5.17 No longer incentivised by airline commission, and now remunerated by some combination of management and/or transaction fees, the relationship between TMC and client tends to be based on securing value for money (this is discussed further in paragraphs 5.24 to 5.30 below). The TMC's advice to the company and education of its workforce regarding travel policy best practice will therefore primarily be driven by the potential for cost savings. It may therefore begin by establishing whether the trip is really necessary, or whether it could be substituted by a non-travel solution such as videoconferencing, potentially with the TMC providing appropriate facilities. The TMC may encourage meeting times to be arranged around the most cost-effective travelling times rather than vice versa, and for bookings to be made further in advance of travel in order to benefit from significant fare savings that early booking can bring.

5.18 Pushing against the use of the TMC are the twin pressures of cost and individuals making their own internet bookings. From the company perspective, the value that a TMC can add may be questioned when each transaction will, at face value, have an added cost compared with booking direct with the supplier. This may be particularly true of smaller firms where monitoring travel is easier. From the employee's perspective, with internet booking for simple trips now the norm for leisure travel, it is common for employees to be tempted to arrange their own business travel (potentially finding cheaper options than the TMC has offered). Companies are often keen to avoid this, since it may not represent a good use of the employee's time, potentially circumvents travel policy and negates employing a TMC. In addition, such self-booked travel may not incorporate ancillary charges (reclaimed later through expenses), nor will they count towards volume deals negotiated with airlines. Either could mean that what appears to be a cheaper fare has hidden cost implications and that a TMC-negotiated fare may be better value overall. Direct bookings will not be captured by the TMC's BSP reporting nor the company's management information, which includes the monitoring of environmental impact. The traveller may also be less easily tracked or assisted in the case of emergency or disruption.

5.19 TMCs are therefore trying to make their own booking processes of comparable convenience for the traveller. TMCs are making more use of technology that can incorporate fares which do not appear in GDSs – those of no-frills airlines or offered through particular agents – on the same screen as the GDS display. TMCs are also recommending that companies introduce an on-line self-booking tool (SBT) which allows employees themselves to search for travel and make straightforward bookings from their desktop, and which is also a lower-cost booking solution for both the company and the TMC.

On-line self-booking tool

5.20 The on-line self-booking tool[225] (SBT) allows company staff to book simple point-to-point journeys, hotels, currency, etc themselves 24 hours a day via an integrated

224. Effectively the opposite of the airline managing its inventory through these same booking classes so as to maximise yield.

225. For more information see Cranfield University Department of Air Transport, Business Travel Research Centre: *A study on the adoption of self-booking tools* on behalf of Amadeus (2007). www.amadeus.com/corporations/documents/corporations/Cranfield%20WP%20Lores.pdf?src=WP.

desktop application linked to the GDS. This will typically display on one page fares for full-service and no-frills airlines, including the company corporate rates, allowing users to view and compare travel and pricing options[226] more comprehensively than booking direct with the supplier or via any on-line booking portals that are generally available on the internet.[227] This therefore encourages take-up by staff of the SBT.

5.21 The SBT will typically filter travel options so as to identify those which are 'out of policy', and therefore may require special authorisation, for example non-preferred airline suppliers, some fare and cabin class options, or fares outside a specified range. Again, this automatic management of the company travel policy provides an advantage over the employee using the internet to book direct.

5.22 The SBT also allows a TMC's specialist consultants to focus resources on advice to high-end travellers and more complex, perhaps multi-sector, long-haul journeys where they are likely to deliver greatest value; it may take several hours to research the best options for complex air itineraries using net fares. Another prime consideration in encouraging use of the SBT is that because transactions are still processed via the TMC, the bookings are included in everything from volume targets to management information, as noted earlier.

5.23 The savings of an SBT, to the extent that there is take-up by staff, therefore potentially come from several sources – fewer TMC resources are needed for the booking process, meaning lower transaction fees, earlier bookings may mean lower fares, and the 'visual guilt' from highlighting travel options which are 'out of policy' tends to induce more cost-effective travel choices.[228] The proportion of bookings (not just air travel) handled on-line by the top 15 TMCs – and therefore unlikely to involve any human intervention – is shown in Table 5.1 above. The table shows big differences between TMCs with on-line proportions varying from 2% to 85%. Among the highest are an on-line TMC and some which handle a high proportion of rail bookings.[229]

Remunerating the TMC

5.24 As noted above, until around 10 years ago, airlines generally paid business travel agents a percentage commission on sales. The standard rate was originally 9% for international tickets (in certain cases there was also the potential for agents to be paid additional 'override' commission). This percentage arrangement resulted in a wide range of revenue per transaction depending on the route and fare type, particularly as the range of fare levels in the market was tending to broaden. As volume and technology reduced agents' unit costs, a model therefore developed whereby agents rebated some or all of their commission to corporate clients in exchange for fixed fees.

226. See, for example, *Galileo/KDS self-booking tool to compete with online retailers*, Travelmole (16 July 2007), www.travelmole.com/stories/1120302.php.
227. Although the trend for airlines to unbundle ancillary services makes it more difficult to compare prices for equivalent products until GDS technology catches up (see Chapter 6). For the time being this creates greater complexity for TMCs and travel buyers in managing travel and in contract negotiation.
228. The Cranfield study on SBTs (based on a worldwide survey of travel managers in September 2006) found that using an SBT saves an average of 25.6% of TMC fees and 9.1% of air ticket costs. A worldwide survey by the Travel Management Institute of TMC Carlson Wagonlit Travel in autumn 2009 found that 75% of travel managers planned to increase implementation of on-line booking tools or had done so in the previous 12 months, and 86% planned to monitor the use of on-line booking or had begun doing so in the previous 12 months. Source: Carlson Wagonlit Travel: *Travel Management Priorities for 2010* (February 2010), no longer available on-line but referenced at www.carlsonwagonlit.com/en/global/news_and_media/news_releases/2010/20100201_cwt_travel_management_priorities_for_2010.html
229. *50 Leading TMCs,* Buying Business Travel (July/August 2010).

5.25 Airlines also became increasingly conscious of the need to reduce their distribution costs. This manifested itself in different ways, in particular the rapid growth of sales via airline websites, but it also led, over time, to a progressive reduction or restructuring of agency commission. For example, BA reduced its 9% commission to 7% from January 1998.

5.26 In April 2001 BA sought to regularise the way it paid commission to UK agents[230] with its *Fresh Approach* scheme.[231] BA replaced its 7% commission with a fixed 'booking payment', thus removing the problem of commissions varying widely depending on fare level, and moving more towards the model that had emerged in the business market, where agents were passing on some or all of their commission to the client. BA's payment per sector booked ranged from £6 (short haul, economy class) to £20 (long haul, premium class). On low-priced tickets this could give agents a higher commission than before, while on relatively high fares the commission was significantly reduced.[232] BA regarded the payment as remuneration for the work an agent did directly for the airline in making a booking and collecting money.[233] Where an agent did work for a customer beyond the basic booking, BA suggested that it should levy a service charge direct on the customer.

5.27 By 2005, BA had abolished standard commission payments in the UK altogether. There were two notable intermediate steps where BA cited a need for further reductions in distribution costs in reaction to the growth of no-frills airlines and the shift to on-line bookings. In February 2002, as part of its *Future Size and Shape* review designed to return the airline to profitability, BA announced that from June it was more than halving the short-haul fixed booking payments, and in December 2003, BA reverted to a percentage commission payment on all UK sales, but set at a level of just 1%.[234] Agents were therefore left relying on service charges levied direct on the customer. Other airlines followed a different course, but in most cases with the same outcome of non-commissionable fares and agency service charges.[235]

5.28 That said, although few airlines now pay standard commission, there remain some revenue streams to TMCs from airlines. Airlines may offer sales and marketing

230. BA had already been required to alter its scheme for paying commission following a ruling in 1999 by the European Commission. The Commission declared that since 1992 BA had been infringing Article 82 of the Treaty of Rome by operating a commission override scheme which, by rewarding loyalty from and discriminating between agents, had the object and effect of excluding BA's competitors from the UK markets for air transport. Case No. IV/D-2/34.780, Virgin/ British Airways, Commission decision of 14 July 1999. The Commission's decision was upheld on appeal by the European Court of First Instance (2003) and the European Court of Justice (2007).

231. Source: BA *Key News*, issue 30/00 (27 November 2000).

232. A return fare using two flights would count as two sectors, so a £100 economy return fare London–Paris would attract £12 commission rather than £7, and a £3000 Club World return fare would attract £40 rather than £210. Of course, the actual effect on agencies depended on the volume of tickets sold at particular fare levels, whether they had a pre-existing agreement with BA on commission beyond the standard arrangements, what commission they were rebating to corporate clients.

233. BA made an additional, percentage-based, 'money collection payment' where agents collected money other than through BA credit card merchant agreements.

234. In September 2003 BA noted that distribution costs still remained a significant part of its cost base and were a key aspect of the focus of its three-year business plan on cost reduction and business simplification. "Rapid changes in market conditions over the past year have accelerated the need to reduce these costs further in order to restore profitability and ensure our survival. To support our strategy to offer full service at low fares, we must compete more effectively with no-frills carriers, who pay nothing to travel agents. We have lowered our fares during the last 18 months and to sustain these lower prices we must reduce our distribution costs further." Source: BA *Key News*, issue 06/03 (5 September 2003).

235. For example, Lufthansa was the second large European airline after BA to move from percentage commission to flat fees from 1 January 2002, and abolished commission altogether in 2004. *Source:* Articles in Financial Times 26 June 2001 and Die Welt 27 July 2004. Virgin Atlantic reduced commission payments for Premium Economy to 5% and Upper Class to 4% from April 2003, and further reduced commissions on all UK sales to 1% from May 2004 alongside a new agency incentive scheme. *Source:* articles in Travel Trade Gazette, 6 January 2003 and 26 January 2004.

agreements with TMCs which incentivise the TMC[236] to place a certain amount of business with that airline. Sometimes there remain override commissions rewarding TMCs based on the amount of business with the airline, and there may be sales incentives for agents at the point of sale. (The economic downturn has reportedly led airlines to monitor these arrangements more closely.)

5.29 Today, TMCs are primarily remunerated by their client companies. There appears to be a complex flow of revenue between the triangle of travel buyer–TMC–airline, plus the added complication of Global Distribution System (GDS) fees.[237] There is no fixed method of remuneration; the CAA's discussions with TMCs and their clients suggest that it is likely to involve an annual management fee and/or a per-transaction fee, which may vary according to the complexity of the booking. The management fee will cover items like staff, rent, rates, technology and account management. The contract may require certain deliverables from the TMC, including data analysis and targets for reducing travel spend, with savings shared with the client through a 'gainshare' agreement, in exchange for a guaranteed level of business. Where the traveller books through an on-line booking tool, i.e. without TMC intervention, the TMC may still levy a small transaction fee to cover its costs in managing the data requirements. Where a company uses a 'net' fare which a TMC has negotiated with an airline, the TMC may add its own mark-up (as indeed it may on published fares).

5.30 It could be argued that TMCs are now better placed to give independent advice compared with an arrangement where the prime means of remuneration, and therefore a potential influence, is a commission incentive. Travel buyers and TMCs will still be engaging with specific, preferred, suppliers, but they can pick and choose between those suppliers. However, the European Commission has identified the potential for competitive distortion through the use of GDS booking data and legislated so as to prevent transport providers from using such data to influence unduly choices by either TMC/agent or the buyer.

Booking information from GDS data

5.31 Global Distribution Systems (GDSs) were originally known as Computerised Reservation Systems (CRSs). They provide customers with, among other services, instantaneous information about the availability of air transport services and the fares for such services. They permit travel organisers, including TMCs and internet travel sites, to make immediate confirmed reservations on behalf of the consumer (with most, but not all, airlines).

5.32 GDSs are governed by a specific EU Regulation supplementing wider competition law to deal with competition concerns arising in this part of the supply chain. The Regulation has been revised three times since 1989. One issue particularly relevant to TMCs is the sale by GDS providers of Marketing Information Data Tapes (MIDT) data derived from booking data, including corporate bookings via a TMC. Airlines are the main users of MIDT data for the purpose of marketing, route planning, revenue management and so on.

236. In the CAA's discussions, such agreements were typically with non-UK airlines which were looking for greater exposure to UK-based companies and their account managers – advertising in client magazines, co-sponsoring of customer events, free training courses, etc. Some TMCs have reportedly sought to renegotiate these as monetary payments which they can pass through to clients, and indeed there is reportedly client pressure for a share of any revenue streams from suppliers, see for example www.procurement.travel/news.php?cid=agency-remuneration-fees-trust.Sep-09.01

237. See paragraph 5.31. Like commission, GDS fees have been another distribution cost targeted by airlines for potential savings. For a summary of developments in this area see European Commission: *Consultation paper on the possible revision of Regulation 2299/89 on a Code of Conduct for computerised reservation systems,* section 4.5.1, (2007) http://ec.europa.eu/transport/air/consultations/doc/2007_04_27_regulation_2299_89_en.htm.

5.33 Because the information is highly detailed, including a complete breakdown of a TMC/agent's sales by destination, airline and fare class, the European Commission was concerned that it allows an airline to monitor the demand for travel on rival airlines and the use of individual TMC/agents, enhancing its bargaining power vis-à-vis travel agents. It may allow airlines to impose incentive schemes whereby payments are based on the agency's ability to meet an agreed-upon target for bookings on a particular airline (where the target is expressed in the form of a market share of the agency's total bookings, or as some increment above last year's bookings for the airline concerned[238]). Because these incentives are voluntary payments that allow an airline to influence how much business an agent directs to it, the Commission saw them as more problematic from a competition standpoint than standard commissions, which are independent of market share (and which, as explained above, have tended to zero in recent years). The Commission saw potential for the incentives to transform an intermediary from a neutral seller's agent to a direct distribution agent for a particular airline – but with no disclosure to the consumer.

5.34 Because of these concerns, the Regulation governing GDSs was amended in 1993 and 1999[239] to prevent MIDT data identifying corporate users. The identification is achieved by means of the specific code for the travel agency 'implant' making the bookings on the company premises. In 2009[240] the Commission extended this to prevent identification of any TMC/agent in the data, either directly or indirectly, except where the TMC/agent and GDS provider agree on the conditions for the appropriate use of such data. The issue was not raised as a concern during discussions with TMCs and travel buyers for this study.

The changing role of the TMC

5.35 The TMC industry has been through many changes over the last 10 years. It has evolved from travel agents specialising in selling and booking business travel on behalf of airlines to travel consultants focused on providing corporate clients with a wide range of travel services. The pattern on remuneration has changed to give TMCs relative independence from airline influence, and this has been reinforced by legislative requirements around the identification of TMCs and corporate buyers in MIDT data produced by GDSs.

5.36 The TMC model may yet evolve further as companies require TMCs to maximise the value they provide at minimum cost. The sharp focus among companies' senior management on obtaining value for money in travel procurement seems likely to remain. It seems likely that TMCs will therefore focus more on their advisory role. This advice ranges from best-value procurement, including negotiating and choosing appropriate fares, to devising and enforcing a coherent approach to travel within client companies through appropriate travel policies. TMCs are likely to continue to encourage client companies to make the booking process more automated, with appropriate controls. There appears to be scope for advising smaller companies whose travel is currently self-booked and therefore relatively unmanaged. Developments in business travel such as greater use of no-frills airlines, the 'unbundling' of ancillary charges, and corporate responsibilities around duty of care and the environment also seem likely to strengthen what TMCs have to offer.

5.37 The next chapter considers how airlines compete for business traffic.

238. Source: summary of findings by consultants Brattle and Norton Rose taken from http://ec.europa.eu/transport/air/consultations/doc/2007_04_27_regulation_2299_89_en.htm. *Consultation paper on the possible revision of Regulation 2299/89 on a Code of Conduct for computerised reservation systems.* See also the Article 82 case referred to at footnote 230 above.
239. Council Regulation (EEC) No 2299/89 of 24 July 1989 on a code of conduct for computerized reservation systems, revised by Council Regulations (EEC) Nos 3089/93 and Council Regulation (EEC) No 323/99.
240. Article 7 of Regulation (EC) No 80/2009 of the European Parliament and of the Council of 14 January 2009 on a Code of Conduct for computerised reservation systems and repealing Council Regulation (EEC) No 2299/89.

Part 2 Chapter 6 Airline competition for business passengers

Chapter summary

- Many airlines target business passengers as a high-yielding source of revenue. However, business travel demand can be volatile, and bookings tend to be made at short notice. Attracting leisure passengers (and for hub airlines, connecting traffic) brings stability and supports more frequency, which is valued by business passengers (a virtuous circle).
- The ability of airlines to attract business traffic, and in particular corporate contracts, is greatly influenced by network and relative frequency. Loyalty schemes can also be a powerful influencer of individual passengers. Consequently, many long-haul airlines believe their offering is more competitive if their network is effectively broadened through alliance membership.
- Competition between airlines for business passengers has led to the evolution of high quality Business Class products on long-haul routes. This in turn created a niche for a Premium Economy cabin for business passengers. A wider range of Business Class fares has evolved on long-haul services, although many of the options require booking in advance and a Saturday-night minimum stay.
- On short-haul routes, changes in fare structures following the entry of no-frills airlines have brought cheaper fares within reach of business passengers as price discrimination barriers in the form of onerous fare restrictions have fallen away – in contrast to long-haul routes. Against a background of tighter travel policies, short-haul business passengers are now more likely to choose 'best fare on the day', despite any penalties for rebooking, because of the potential savings.
- Many short-haul airlines have reacted to the increased focus on price by 'unbundling' their fares, allowing them to offer the lowest possible fare while charging for ancillary items such as meals and hold baggage. Although some airlines still perceive demand for a premium short-haul product, there has been a continuing fall in demand for Business Class on short-haul services (which appears to be a permanent structural change), accentuated by the economic downturn.
- Three new entrant all-Business-Class airlines failed in succession between December 2007 and May 2008, attributing their demise principally to high fuel prices, the economic slowdown and an inability to secure further investment in the prevailing global financing environment. Some European network carriers have successfully adopted such a model, but only BA currently operates such a service from the UK.

Introduction

6.1 Previous chapters considered the demand for business travel and the way it is procured and booked. This chapter looks at business travel from the perspective of the supplier airlines. It considers the significance of the business market to airlines, the effects of market liberalisation, the evolution of in-flight products for business passengers, developments in airlines' pricing strategies and airline reactions to the economic downturn.

6.2 This chapter begins with an overview of airline competition for business passengers. The next section considers the long-haul market, including the introduction of flat beds in Business Class, the gradual adoption of a new cabin class, Premium Economy, and the all-Business Class airline model. The final section considers the short-haul market, including the inroads that no-frills airlines have made into the business market, network airlines' competitive reactions, and trends such as the practice of 'unbundling' the fares offered in order to offer the lowest possible base price.

Overview

Significance of business passengers to airlines

6.3 Depending in part on the traffic mix on the route concerned, airlines may (to a greater or lesser degree) specifically seek to attract business passengers. For most airlines, the business market is highly attractive because of the potential for higher yields per passenger. As outlined in Chapter 4, the prime concern of late-booking, must-travel passengers is often convenience, and, to some extent, flexibility and price. This is likely to mean that their choice will be guided by the product on offer, in particular the flight schedules which best meet their needs, as well as price. Such passengers may be willing to purchase a premium product, including Business Class and also other services in the period leading up to the flight (such as choice of seat, flexibility to change a booking, or business lounge access at the airport) particularly where someone else, probably their company or client, is picking up the bill. Such choices may, of course, be constrained by their company travel policy.

6.4 Airlines are able to take advantage of the greater willingness to pay and the greater tendency to book close to departure to differentiate on price. By using revenue management systems and fare rules to close off availability of cheaper fares as the date of departure approaches, they are able to segment the market without too great a risk of dissuading the passenger from booking. All these factors give rise to the potential for higher yields.

Comparison with the airport perspective

6.5 Certain UK airports specialise in providing for business travel, such as London City or Farnborough. However, interviews for this study suggest that – unlike those two airports, and unlike airlines – larger UK airports do not focus on attracting particular categories of passenger, to the extent that this is within their control. Their focus is more on passenger volume[241] and the airline/route portfolio, which in turn drives volume through attractive destinations, potentially larger aircraft, and maximising connecting possibilities.[242] Adding frequency on a dense but underserved route may attract more traffic than adding a new destination, which might be served with a relatively smaller aircraft. The greatest passenger volume is likely to be generated by routes attracting new leisure passengers, even though business routes may bring wider benefits to the economy.

6.6 To the extent that airports measure the relative value of business and leisure passengers, it seems that leisure passengers (being less frequent travellers) are likely to spend more at the airport, whereas business passengers are likely to pass through the airport more quickly and to use airline business lounges rather than spend at airport concessions.[243]

241. Where an airport is subject to capacity constraints, growth in terms of passenger volume can only come from attracting larger aircraft and better seat factors.
242. Albeit that transfer passengers generally bring less revenue to the airport than passengers beginning/ending their journey at the airport.
243. Airline lounges themselves bring some income to the airport and some airports offer their own lounges. Airports also reported that business passengers tend to spend more on car parking.

Attracting business traffic

6.7 The UK market gives plenty of scope for airlines to attract business passengers: seven out of the top 10 business routes in the world have London (and Heathrow specifically) at one end.[244] Of airlines offering scheduled services to and from the UK, BA has by far the largest market share of business passengers. In 2007, BA carried 41% of total business passengers on long-haul services to and from the UK and 23% of the total on short-haul.[245] BA has acknowledged that its premium product is the most profitable part of its business,[246] although that was prior to the sharp drop in premium traffic during the economic downturn. In 2009 around 13% of BA's total passengers travelled in First or Business Class cabins, accounting for 45% of revenue.[247]

6.8 The proportionately greater revenue from premium compared with non-premium passengers is essential to cover the costs of the higher standards of service, the greater cabin space taken up by premium seats (for example, BA's long-haul Business Class seat takes up around 2½ to 3 times the space of an economy seat) and potentially lower load factors than in the economy cabin. Therefore, it is particularly important for the airline's revenue management that its premium products are not undersold. Similarly, when setting prices and revenue managing, an airline takes account of any difference between the quality of its product and that of competitors – such as whether there is a flat bed in long-haul Business Class. Table 2-4 illustrates that a significant proportion of business passengers has always travelled in the economy cabin rather than premium cabins. It also shows that, more recently, some business passengers appear to have shifted from premium cabins towards economy (or premium economy) while some leisure passengers have been attracted to upgrade to premium cabins by the introduction of lower fares with restrictive booking and travel conditions.

6.9 At the route level, the ability of airlines to attract a workable mix of business and leisure passengers can vary considerably depending on the route, in terms of both the destination and the UK airport.[248] Many airlines rely on corporate deals to secure business passengers and to obtain some sort of non-binding volume commitment in terms of future custom, as described in Chapter 4. Because business passengers tend to prioritise journey time, they value a good schedule and frequency, and in general travel on direct flights where they can. Airlines which compete in a given market only by offering indirect services involving a change of plane at their hub are therefore less likely to attract them, at least not without discounting the fare. The typical pricing model of no-frills airlines, now widely adopted by network airlines on short-haul services, recognises that late-booking passengers are likely to accept a higher price.

244. BAA written evidence to the House of Commons Transport Committee inquiry on the Future of Aviation (2009). www.publications.parliament.uk/pa/cm200910/cmselect/cmtran/125/125ii.pdf
245. Survey results for London airports in 2009 (excluding London City which was not surveyed) show little change in BA's share of the London market over the two years.
246. For example, BA Chief Executive quoted in *Flat Out*, Airline Business (January 2007).
247. Speech by BA Chief Executive, BA Annual General Meeting (July 2009) phx.corporate-ir.net/External.File?item=UGFyZW50SUQ9MTAyOTh8Q2hpbGRJRD0tMXxUeXBlPTM=&t=1
248. See Chapter 1.2 of Part 1 of this study.

Market shares – top five long-haul business routes

6.10 Table 6-1 shows market shares in terms of business passengers for airlines serving the top five long-haul business routes from London. It illustrates that the ability of airlines to attract business traffic, and in particular corporate contracts, may depend on network and relative frequency.

Table 6-1 Market share of airlines on top five long-haul routes from London in terms of business passengers, 2009

Route London–	Airline (approx. daily frequency)	Passengers (000) Journey purpose Business	Total	Business % of total	Market Share Journey purpose Business	Total	% connecting (at one or both ends) Journey purpose Business	Total
New York	BA (11)	309.0	1454.9	21%	45%	41%	42%	50%
	Virgin (5)	143.1	879.2	16%	21%	25%	23%	20%
	American (5)	117.7	607.4	19%	17%	17%	43%	51%
	Continental (3)	64.9	355.5	18%	9%	10%	49%	60%
	Delta (2)	44.3	253.8	17%	6%	7%	19%	40%
	Kuwait A/w(0.4)	6.3	28.1	22%	1%	1%	21%	18%
	Air India (--)	0.0	8.1	0%	0%	0%	0%	0%
New York total		**685.2**	**3586.8**	**19%**	**100%**	**100%**	**37%**	**43%**
Dubai	Emirates (8)	352.1	1748.4	20%	68%	75%	66%	76%
	BA (3)	126.7	377.2	34%	24%	16%	60%	51%
	Virgin (1)	39.6	170.6	23%	8%	7%	21%	8%
	Royal Brunei(1)	0.0	43.6	0%	0%	2%	0%	27%
Dubai total		**518.5**	**2340.0**	**22%**	**100%**	**100%**	**61%**	**66%**
Hong Kong	Cathay (4)	205.0	835.7	25%	52%	49%	70%	74%
	BA (3)	121.0	506.2	24%	31%	30%	69%	60%
	Virgin (2)	52.5	178.6	29%	13%	11%	7%	18%
	Air N Zealand(1)	9.0	80.3	11%	2%	5%	27%	20%
	Qantas (1)	5.1	93.7	5%	1%	6%	82%	58%
Hong Kong total		**392.5**	**1694.4**	**23%**	**100%**	**100%**	**60%**	**60%**
Boston	BA (3)	130.3	448.6	29%	55%	53%	56%	58%
	American (3)	74.4	239.9	31%	32%	28%	32%	46%
	Virgin (1)	30.2	162.1	19%	13%	19%	37%	27%
Boston total		**234.9**	**850.6**	**28%**	**100%**	**100%**	**46%**	**49%**
Tokyo	Japan A/l (2)	50.7	251.6	20%	24%	33%	44%	43%
	BA (1)	61.3	205.5	30%	29%	27%	58%	66%
	Virgin (1)	39.7	152.9	26%	19%	20%	37%	19%
	All Nippon (1)	62.9	143.6	44%	29%	19%	40%	48%
Tokyo total		**214.6**	**753.6**	**28%**	**100%**	**100%**	**46%**	**45%**

Source: CAA Passenger Survey, 2009, OAG Flight Guide July 2009.

Notes: Passenger numbers include those connecting at either end. Connecting proportion represents passengers connecting at either end or both.

6.11 Table 6-1 shows that business passengers form between 19% and 28% of total passengers on these five routes. London–New York and London–Dubai carry the most business passengers, but 61% of Dubai business passengers are connecting at one or both ends, compared with 37% of New York business passengers. BA significantly outcarries other airlines in terms of business passengers on London–New York and London–Boston, with 45% and 55% of the market respectively. On London–Tokyo the market shares are more equal, while on London–Dubai and London–Hong Kong Emirates and Cathay Pacific respectively significantly outcarry BA, with market shares of 68% versus 24% (Dubai) and 52% versus 31% (Hong Kong). Virgin also serves each of these routes but at a lower frequency. In terms of traffic mix, the proportion of business passengers on Virgin services is lower than BA in each case except on Hong Kong, where the higher proportion could be a function

of the higher frequency offered. Virgin's aircraft are generally configured with fewer Business Class seats than BA's (see Table 6-4 and Table 6-5). As an independent airline Virgin's penetration of business markets will depend on how successfully it can compete for corporate contracts compared with airlines and alliances with bigger networks and the more extensive frequent flyer programmes that result from network scale.

6.12 The proportion of business passengers on Emirates' services to Dubai is lower than for BA and Virgin despite Emirates' high frequency. Emirates' business model focuses on attracting connecting traffic over the Dubai hub to destinations beyond, but an indirect service may be less attractive to business passengers where there are direct services available. If connecting passengers are ignored (76% of the total), the proportion of business passengers on Emirates' services rises to 28%. The proportion of business passengers carried by fifth-freedom services[249] is particularly low in most cases, probably because of their relatively low frequency and lack of a home market.

Market shares – top five short-haul business routes

6.13 Table 6-2 shows market shares in terms of business passengers for airlines serving the top five short-haul international business routes from London. London–Dublin has the most passengers overall, but is second to London–Amsterdam in terms of business passengers because of the stronger business content of the Amsterdam route (38% versus 25%). Of the five routes, London–Brussels has the strongest business content at 54%, and this increases to 76% if passengers connecting at either end are excluded.

6.14 The table shows that there is a strong business content on flights to and from London City, in excess of 50% in each case. It also shows that although network airlines generally carry a higher proportion of business passengers than no-frills airlines, in terms of overall numbers, no-frills airlines have built up a significant share of the business market. That share is even greater if passengers connecting at either end are excluded – for example, the table shows that easyJet has around a quarter of the London–Amsterdam point-to-point business market and Ryanair more than a third of London–Dublin.

249. 'Fifth-freedom' means the right for an airline of Country A to carry passengers and cargo between Country B and Country C on a flight that originates or terminates in Country A. In Table 6.1 the airlines concerned are Royal Brunei to Dubai, Air New Zealand and Qantas to Hong Kong, and Kuwait Airways and Air India to New York.

Table 6-2 Market share of airlines on top five short-haul business routes from London

Route London-		All passengers (000) Business	Total	Business % of total	Market share (city pair) Business	Total	Point-to-point pax (000) Business	Total	Market share of business point-to-point pax (city pair)
Amsterdam									
KLM	LHR	268.7	734.1	37%	24%	26%	154.7	342.3	18%
VLM	LCY	156.8	247.3	63%	14%	9%	156.4	246.0	18%
AF-KLM gp total		*425.6*	*981.4*	*43%*	*39%*	*34%*	*311.1*	*588.3*	*35%*
BA	LGW	89.8	216.3	42%	8%	8%	71.1	151.5	8%
	LHR	197.1	476.1	41%	18%	17%	138.3	235.6	16%
BA Cityflyer	LCY	50.5	97.7	52%	5%	3%	48.1	93.0	5%
BA total		*337.4*	*790.1*	*43%*	*31%*	*27%*	*257.5*	*480.1*	*29%*
easyJet	LGW	87.3	325.7	27%	8%	11%	82.6	289.8	9%
	LTN	65.6	218.3	30%	6%	8%	64.6	215.9	7%
	STN	74.0	258.1	29%	7%	9%	72.5	242.1	8%
easyJet total		*226.9*	*802.1*	*28%*	*21%*	*28%*	*219.6*	*747.8*	*25%*
bmi	LHR	112.1	299.6	37%	10%	10%	88.3	184.4	10%
Others		0.3	0.6				0.3	0.4	
Amsterdam total		**1102.3**	**2873.8**	**38%**	**100%**	**100%**	**876.9**	**2001.0**	**100%**
Dublin									
Aer Lingus	LHR	355.0	1175.1	30%	36%	30%	295.8	802.9	34%
	LGW	86.1	416.2	21%	9%	10%	73.9	298.0	9%
Aer Lingus total		*441.1*	*1591.3*	*28%*	*44%*	*40%*	*369.8*	*1100.9*	*43%*
Ryanair	LGW	97.2	613.9	16%	10%	15%	88.8	554.5	10%
	LTN	80.9	345.5	23%	8%	9%	77.6	329.6	9%
	STN	154.0	786.7	20%	15%	20%	141.1	697.0	16%
Ryanair total		*332.1*	*1746.1*	*19%*	*33%*	*44%*	*307.5*	*1581.1*	*36%*
bmi	LHR	122.2	444.9	27%	12%	11%	82.5	207.7	10%
CityJet	LCY	85.9	152.0	57%	9%	4%	84.6	150.4	10%
BA	LGW	14.1	27.5	51%	1%	1%	11.2	21.3	1%
BA Cityflyer	LCY	4.5	7.7	58%	0%	0%	4.2	7.3	0%
BA total		*18.5*	*35.2*	*53%*	*2%*	*1%*	*15.4*	*28.5*	*2%*
Dublin total		**999.9**	**3969.5**	**25%**	**100%**	**100%**	**859.8**	**3068.8**	**100%**
Frankfurt (* = Hahn)									
LH	LHR	385.5	774.6	50%	50%	46%	277.6	470.1	45%
Augsburg	LCY	59.2	91.4	65%	8%	5%	52.9	74.9	9%
Lufthansa gp total		*444.7*	*866.0*	*51%*	*58%*	*51%*	*330.5*	*545.0*	*54%*
BA	LHR	198.5	427.2	46%	26%	25%	164.6	276.2	27%
BA Cityflyer	LCY	59.1	79.9	74%	8%	5%	57.8	75.7	9%
BA total		*257.6*	*507.1*	*51%*	*34%*	*30%*	*222.4*	*351.8*	*36%*
Ryanair*	STN	64.3	313.7	20%	8%	19%	62.2	294.6	10%
Frankfurt total		**766.6**	**1686.8**	**45%**	**100%**	**100%**	**615.0**	**1191.4**	**100%**
Paris (CDG & Orly)									
BA	LHR	230.8	676.6	34%	38%	39%	148.1	242.6	38%
Air France	LHR	247.1	661.8	37%	41%	38%	131.3	243.0	34%
CityJet	LCY	54.8	101.9	54%	9%	6%	42.9	70.4	11%
AF-KLM gp total		*302.0*	*763.7*	*40%*	*50%*	*44%*	*174.2*	*313.4*	*45%*
easyJet	LTN	69.3	297.8	23%	12%	17%	69.0	286.1	18%
Paris total		**602.1**	**1738.1**	**35%**	**100%**	**100%**	**391.2**	**842.1**	**100%**
Brussels									
BA	LHR	181.9	346.8	52%	59%	60%	82.8	104.0	49%
bmi	LHR	97.3	169.8	57%	31%	29%	63.5	85.6	37%
Brussels A/I	LGW	20.3	45.9	44%	7%	8%	12.6	19.6	7%
Lufthansa gp total		*117.5*	*215.7*	*54%*	*38%*	*37%*	*76.0*	*105.2*	*45%*
Others		11.2	13.2	85%	4%	2%	11.2	13.1	7%
Brussels total		**310.6**	**575.6**	**54%**	**100%**	**100%**	**170.0**	**222.4**	**100%**

Source: CAA Passenger Survey, 2009.

Notes: 'All passengers' includes those connecting at either end. 'Point-to-point passengers' excludes passengers connecting at either end or both.

Market shares of '0%' indicate that the actual percentage is less than 0.5%.

Characteristics of business traffic

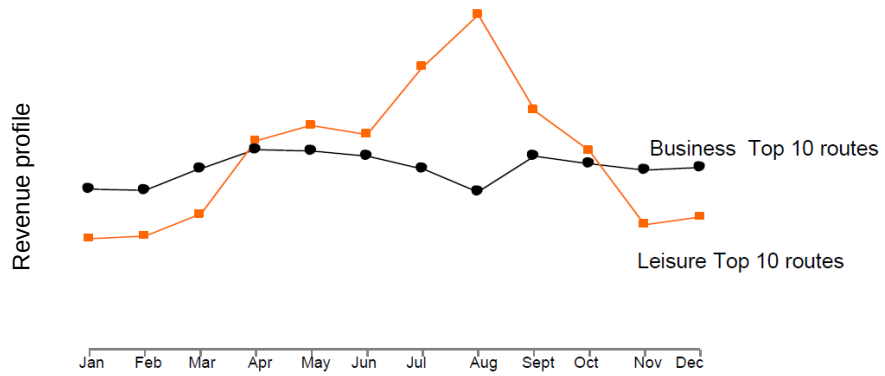
6.15 From the airline planning perspective, business travel demand is generally more volatile than leisure demand, and more likely to be affected by short-term factors.[250] When firms experience a shock to their business, the drop off in demand for business travel tends to happen quite quickly as the purse-strings tighten, trading and therefore the need for meetings declines, and trips are cancelled or deferred. Business travel also tends to be booked at relatively short notice. These characteristics mean that demand can evaporate very quickly, giving airlines little time to react. By the same token, business travel can return very quickly as well.

6.16 These characteristics can be contrasted with the leisure market, where an airline may have sold a considerable proportion of seats well in advance – at least for the summer season on long-haul routes, where many such sales would be made the previous winter/spring. The airline therefore has time to catch up with any fall off in demand by adjusting pricing and, where feasible, capacity. The consumer economy also lags the business economy, because it may take more time for the effects to flow through into consumer confidence and unemployment.

6.17 Fares bought by leisure passengers generally commit them to the booking, in that cancellation carries a penalty, and therefore the seat may only need to be sold once. A typical business traveller may book considerably closer to travel and, in some cases, at more flexible fares which allow reservations to be changed or cancelled. The recent trend for business travel bookings to be made further ahead, and on less flexible conditions, identified in Chapter 4, may give airlines greater scope to revenue manage their inventory better (see paragraph 6.65 below).

6.18 Business traffic is generally less seasonal than leisure traffic, but the seasonal effects are to some extent complementary. Business traffic will tend to dip in the summer when leisure traffic is at its peak. There is a similar effect, to some extent, during other holiday periods such as Christmas. The difference in the demand profiles of the two sectors is illustrated by Figure 6-1 below, which shows the revenue profile for the 10 biggest business and 10 biggest leisure routes on easyJet's network.[251] Note the flatter revenue profile for business traffic and the potential for taking advantage of the counter-seasonal effect by attracting a mix of business and leisure traffic.

Figure 6-1 easyJet revenue profile on business and leisure routes



Source: easyJet full-year results presentation for year ending 30 September 2009. http://corporate.easyjet.com/~/media/Files/E/easyJet/pdf/media/latest-news/2010/Final.pdf

250. Figure 2-3 and Table 2-1 show that numbers of business passenger at UK airports fell by around 20% in 2009, whereas total traffic fell by only 7%.
251. Since easyJet's business model is to achieve a target load factor, changes in demand are better illustrated by the revenue generated from a route rather than the passengers carried.

6.19 On short-haul routes, business travel demand also tends to peak in the morning and early evening so as to allow a full day's business, perhaps without the need for an overnight stop, creating trough periods in the middle and at the end of the day. There will also be significantly less demand at weekends. Airlines may be able to cater for this variation to some extent by using larger aircraft at peak times or using pricing to attract leisure passengers, but on thinner, business-oriented routes which cannot support off-peak services they may need also to use the aircraft on a leisure route where frequency or timings are less important, thus optimising aircraft utilisation. Operations on long-haul routes may pose different problems, requiring a mix of routes of different sector lengths to maximise utilisation of aircraft and crew, and to accommodate different time zones and airport night curfews. This is explored further in the CAA's 2007 study of long-haul air services.[252]

Price sensitivity

6.20 Chapter 4 explained that there has been increasing sensitivity to price apparent in corporate procurement of air travel, and that the degree of sensitivity may also vary depending on the size and type of the business concerned. But in terms of the decision by a firm for an employee to make a particular journey, airlines have traditionally regarded schedule and convenience as of greater concern to the business passenger than the price, as noted above.

6.21 Once the decision whether to travel has been taken, there remain two further decisions (how and when) where airlines experience more price sensitivity around the choice of airline and class of travel. Following the economic downturn, this sensitivity has been heightened, and the effect of choosing different ticket types and flight timings may also come into the consideration. Thus, in broad terms, airlines see business passengers as more likely to be priced off a product than out of a market, because the decision to travel is made by the firm, not by the individual (the curtailment of business travel during a shock such as the recent economic downturn being something of an exception). This is illustrated by some business passengers trading down from Business Class to Economy or Premium Economy as their companies have become more cost conscious.

6.22 Therefore, for a defined market, the airline will assume a low level of price elasticity for business passengers, because destinations are not competing. However, in terms of competing with other airlines, they set prices relative to the prevailing market level. Unlike leisure passengers, who by comparison travel relatively infrequently, the business passenger and corporate buyer, governed by company travel policy and possibly by the procurement contract periodically renewed with the airline, are likely to be more aware of the non-price elements of the airline product. The individual's choice may also be influenced by personal gain in terms of the points earned from the travel from airline frequent-flyer programmes.[253] This explains the continued business product enhancement and strong competition between airlines in premium product quality and frequent-flyer programmes. These subjects are explored further below.

Significance of network and frequency for penetrating the corporate market

6.23 In the context of Table 6-1 and Table 6-2, it was suggested that the ability of airlines to attract business traffic, and in particular corporate contracts, may depend on network and relative frequency. Airlines interviewed for this study stressed that these are important factors. At the route level, an airline operating a greater number of

252. Chapter 3, section 7 of *CAP 771 Connecting the Continents: Long-haul passenger operations from the UK*, CAA (2007). www.caa.co.uk/cap771

253. See paragraph 4.61 in Chapter 4.

frequencies should, in principle, be able to attract a greater proportion of (higher yielding) time-sensitive passengers. These passengers place a particularly high value on frequent service as it minimises their costs in terms of the difference between actual and desired flight timings.[254] Table 3-6 showed that 50% of short-haul business passengers interviewed at Heathrow in the survey undertaken for this study gave 'Timing of flights / Direct route / Availability' as a reason for choosing their airline.

6.24 As discussed in Chapter 4, companies tend to purchase travel on a number of routes, depending on business needs and may therefore invite bids for a 'bundle' of routes when negotiating for corporate discounts. Research for this study also suggests that, outside their home markets, even airlines of a significant size could struggle to 'get a foot in the door' in securing volume deals. Airlines offering the widest range of destinations are likely to be most attractive to large companies, and these are likely to be the airlines with operations based at airports in the same country as those companies. Regulatory restrictions may also give some airlines strength in a particular market from which they can leverage business on routes where their competitive position is weaker. For example, the huge US domestic market is effectively closed to non-US airlines, so even EU airlines with a good long-haul network will struggle to secure business from a global company which requires a lot of US domestic flying to be bundled in the deal – unless the EU airline is part of an immunised alliance[255] with a US airline.

6.25 The effect of one airline winning a substantial volume commitment from a large company on a given route will be commensurately to reduce the volume which a competing airline can attract on that route, unless it can compensate by attracting additional connecting traffic. It has been suggested that it can take a new entrant some time to penetrate the corporate market on a new route, because no matter how good the product, it may be difficult to secure business until a firm's existing contracts expire. The potential for larger airlines to take advantage of their widespread networks and strength in particular markets in a way that would make it difficult for smaller competitors to respond has raised some concerns in the past from a competition perspective, specifically in the case of corporate discounts, agency commission and frequent-flyer programmes.[256] Hence the significance for competition in the business market of the continuing consolidation of airlines into alliance groupings.

6.26 Although a company is likely to have a broad idea of its overall spend and the routes of the greatest importance to it, it may not know all its route requirements when the volume deal is negotiated. Network reach – which gives flexibility with regard to routes to be flown in future – may therefore be important in negotiating corporate deals. The European Commission noted in its 2004 decision on the Air France/KLM merger[257] that corporate customers generally agreed non-exclusive contracts with multiple airlines or alliances. The Commission also found that corporate customers were increasingly considering contracting with airlines on the basis of the geographic coverage of their network (including those of their partners). The Commission concluded that the demand from corporate customers was driven by network effects as well as origin/destination considerations.

254. There is an oft-quoted theoretical 'S' curve relationship between frequency and market share, such that an airline offering more than half the frequencies in a market is likely to have a market share higher than its share of frequencies. Greater frequency also offers flexible ticket holders more rebooking options. See, for example, Holloway S.: *Straight and Level: practical airline economics* (page 428), (2008).
255. As described in paragraph 6.27.
256. See footnote 197 in Chapter 4 regarding corporate discounts and footnote 230 in Chapter 5 regarding agency commission.
257. Case No. COMP/M.3280 – Air France/KLM, European Commission (11 February 2004).

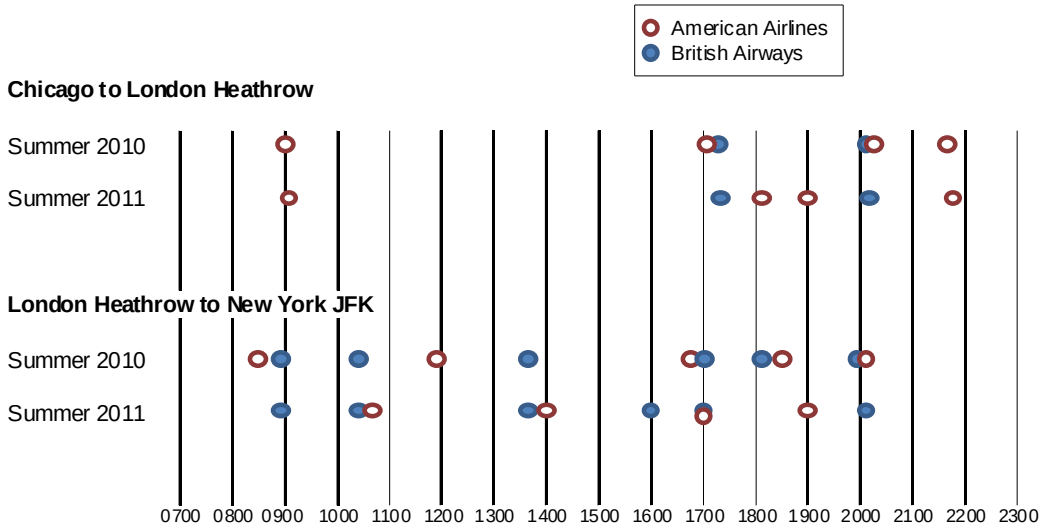
6.27 While many UK-based companies negotiate volume deals that focus on travel to and from the UK, some are on a regional or even global basis. Following the gradual formation of the three big airline alliances, airlines are able to agree pricing and capacity (including 'metal neutrality', or the pooling of aircraft within the alliance, where practical, to fly a particular route) where anti-trust immunity has been granted from the usual prohibitions in competition law. Anti-trust immunity therefore allows those airlines to offer corporate deals on an alliance-wide basis. As noted in Chapter 4, these are reportedly becoming more common. Without anti-trust immunity, airlines are confined to agreements on marketing initiatives such as codesharing, frequent flyer programmes, round-the-world or circle-trip fares, business lounges etc.[258]

6.28 Airlines usually link their frequent flyer programmes with those of alliance partners so as to broaden the options for 'earning and burning' points across a wide network.[259] In attracting traffic originating outside their home market, airlines face the challenge of competing with foreign airlines' frequent-flyer schemes. Therefore airlines which are members of alliances may have more success in using their scheme to compete in other markets. In a UK context it is not surprisingly the BA Executive Club scheme which is quoted most often; one foreign airline representative interviewed claimed that the BA scheme represented its single biggest challenge in accessing the UK business travel market "because everyone wants BA miles".

6.29 American Airlines, BA and Iberia launched a transatlantic joint venture in October 2010 following clearance by competition authorities. One aim is to offer a better choice of schedule, and from the summer 2011 season the schedules of the three airlines will be more closely aligned with flights re-timed to give a greater range of departure times.[260] Figure 6-2 illustrates changes in departure times from Chicago to Heathrow, showing that flights that were previously at similar timings are now spread more evenly.[261] The diagram also shows changes made in Heathrow to New York departure times. Here there seems to have been some rationalisation of late afternoon and evening flights, but flights earlier in the day are actually now more bunched.

258. The default position is that the IATA multilateral interline system facilitates all participating airlines in selling seats on one another's services irrespective of alliance affiliation or marketing agreements, using the Multilateral Prorate Agreement to divide the revenue. www.iata.org/workgroups/Pages/mita.aspx; www.iata.org/whatwedo/finance/Pages/proration.aspx
259. Particularly where employees experience a loss of personal benefit when directed away from their normal carrier of choice by company travel policy.
260. press.ba.com/wp-content/uploads/Factsheet-American-Airlines-British-Airways-and-Iberia-launch-joint-business.doc . Clearance by competition authorities allows the airlines to coordinate activities such as scheduling and pricing.
261. Also illustrated in BA'S first half results 2010/11 presentation, www.iagshares.com/.

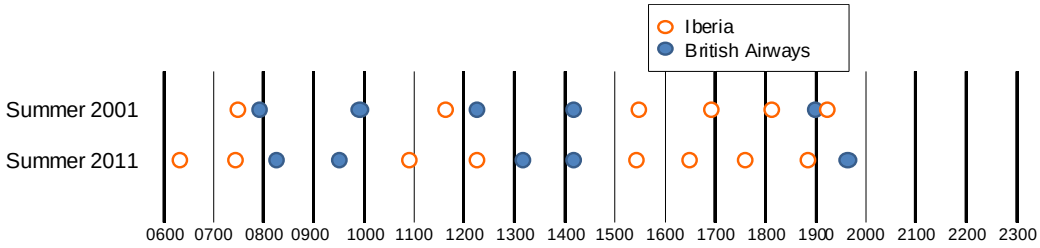
Figure 6-2 Examples of BA/American Airlines schedule changes 2010–2011



Source: Worldspan GDS, OAG Flight Guide July 2010.

6.30 BA and Iberia have been coordinating schedules since obtaining clearance from competition authorities in 2003. Figure 6-3 illustrates that this has resulted in a more even spacing of their services linking the two hubs of Heathrow and Madrid.

Figure 6-3 BA/Iberia Heathrow–Madrid schedule changes, 2001 and 2011



Source: Worldspan GDS, OAG Flight Guide July 2001.

Connecting passengers[262]

6.31 Network airlines interviewed for this study stressed the beneficial effects of a good mix of not just business and leisure traffic but also connecting and point-to-point traffic. An airline attracting a good proportion of connecting passengers is able to use the extra volume to support a higher frequency. Good frequency in turn attracts point-to-point business passengers and can allow significantly improved connecting possibilities – a virtuous circle. (Eventually there are diminishing returns from adding more frequency, but, from conversations with airlines, the optimum level is not necessarily easy to predict.)

6.32 Hence, Heathrow-based airlines in particular are competing with other hubs for connecting traffic, whether this be from domestic, European or long-haul services. Business passengers' prime focus will be on convenience of schedule in terms of flight timings and overall journey time. Even where a direct flight exists, they may be prepared to accept the inconvenience and longer air journey time of a connecting flight if the schedule and timings suit their needs better and potentially give them a

262. Further information can be found in *Connecting Passenger at UK Airports*, CAA (November 2008) www.caa.co.uk/docs/5/Connecting_Passengers_at_UK_Airports.pdf

longer business day or a shorter trip overall by avoiding an overnight stay. Thus, even where an airline is the sole direct operator on a particular route, there may be a significant proportion of business traffic which it does not capture, particularly in low-volume markets where a low-frequency direct service gives passengers few timing options, or where traffic is attracted away by a sufficiently strong product, brand, deal or price. The effect may be stronger where the indirect service offers a relatively short connecting time,[263] unless the passenger is wary of a greater risk of missing a connection.

6.33 Connecting passengers have some disadvantages for airlines in that they can be lower yielding than passengers flying direct, although connecting business passengers often realise higher yields than point-to-point leisure traffic. Airlines are bearing the costs of two sectors while charging a fare that is competitive with the direct fare, and may well have to offer a significant additional discount where a passenger is accepting a less convenient journey in exchange for a lower price. Facilitating interline connections between airlines will bring more complexity and cost from, for example, arrangements for through-checked baggage and the processes for apportioning revenue (such as Special Prorate Agreements).

Market liberalisation

6.34 The liberalisation of air markets seeks to create a framework within which competition can flourish. The resulting competitive spur has repeatedly been shown to give rise to a wider choice of airports, airlines and products for the user at lower prices, encouraging a more efficient aviation industry. Moreover, such liberalised markets are more likely to allow companies the flexibility to restructure and/or adapt their operations to changing circumstances in line with the requirements of the economic cycle.

6.35 When international scheduled routes were all highly regulated, fares and standards of service were closely controlled through the trade association IATA. In most countries the norm was a state-owned, relatively high-cost 'flag carrier' in each country, dominating its own market and home/hub airport, and often protected from competition in a position of government-supported monopoly or near-monopoly. Even in the UK, with the largest and most diverse airline industry in Europe, BA, in 1992, still accounted for 83% of UK airlines' scheduled revenue passenger kilometres. (In 2009 this had fallen to 48%.)

6.36 Against this background, it took many years for aviation markets to be liberalised and meaningful competition to develop. For the UK, the most significant development was the creation of the EU single aviation market which took effect in 1993 and which gave EU airlines freedom to operate any route and to set prices within the EU. The single market has continued to broaden with EU enlargement and EU-wide agreements with neighbouring states. As a result, the UK–Europe market has changed enormously: the entry and rapid expansion of no-frills airlines contributed to a highly competitive market impacting both leisure and business passengers.

6.37 Progressive liberalisation of long-haul markets from the UK, which is on-going, has allowed greater competition to develop there also. The most significant development was the entry into force of a liberalised EU–US market in 2008.[264] Other liberal EU-wide or bilateral agreements with third countries have been, or are being, negotiated.

263. Airlines operating at hubs less congested than Heathrow have more flexibility to arrange connecting flights into 'waves' so as to minimise connecting times.

264. The Bermuda II UK–US air services agreement previously in place restricted the number of UK and US airlines which could serve Heathrow–US routes to four and also imposed restrictions on the routes and capacity that could be offered.

Airline reactions to the economic crisis

6.38 Chapter 2 analysed the effects on business travel of the economic downturn. Paragraphs 2.30 to 2.39 considered the specific reactions to the crisis by airlines, including some detailed analysis of the impact on BA's and easyJet's business traffic.

Evolution of products and pricing: long-haul services

Business Class product[265]

6.39 Business Class emerged in the late 1970s[266] as a moderate product upgrade over Economy Class, not unlike Premium Economy today. Airlines aiming to cater for both business and leisure passengers in Economy Class perceived a conflict in seeking to attract business passengers with a high-quality product and leisure passengers with competitive fares. Essentially the concept was to create a separate cabin for business passengers paying the full economy fare, still with an Economy Class configuration (nine-abreast on a Boeing 747), but with a quiet working environment and superior catering.[267]

6.40 Airlines' long-haul Business Class products have been progressively upgraded ever since in terms of seat pitch and comfort, in-flight service, and improvements in ground facilities such as door-to-door limousines, airport lounges and dedicated check-in. The following narrative does not attempt to give a comprehensive history or analysis, but seeks to illustrate the progressive upgrades with some highlights of developments in the BA and Virgin Atlantic products, and some contextual comments about other airlines.

6.41 BA relaunched its Business Class cabin in 1984, rolling out an enhanced product (Super Club) across its network which it had already trialled on the North Atlantic. The nine-abreast 747 configuration was reduced to seven abreast and, in most cases, BA began charging a small premium on the full economy fare. BA rebranded the cabin Club World in 1988 (Table 6-3).

Table 6-3 BA typical long-haul configuration, 1988

	Number of seats				**(a) Proportion of seats (b) *Seats abreast***			
Aircraft type	**total**	**First**	**Club World**	**World Traveller**		**First**	**Club World**	**World Traveller**
747-200	364	18	88	258	(a)	5%	24%	71%
					(b)	*2-2[-2]*	*2-3-2**	*3-4-3*

Source: BA Worldwide Timetable 1988/89.

*Notes: * Main deck.*

Configuration is representative for the aircraft type, but there were other variations.

Club World = Business Class, World Traveller = Economy Class.

265. This section is drawn from a number of sources: BA Worldwide Timetable (issued each season), Shaw S.: *Air Transport, a marketing perspective,* (1982); Doganis R.: *Flying Off Course* (2002); *Atlantic Luxury*, Airline Business (June 2001); *Back to Business*, Airline Business (January 2002), *Travel Weekly Worldwide Business Class supplement* (1993)*; OAG First and Business Class Travel* (Summer 1996); *Virgin Hopes to Steal Market Share with new Lie-flat Seat*, Aviation Daily (18 July 2003); BA and Virgin websites; www.seatplans.com; www.seatguru.com.
266. British Caledonian was the first UK airline to adopt a three-cabin concept in April 1978, on the London–Houston route, which has a strong business content. The Boeing 707 aircraft was configured with 24 First, 54 Executive and 48 Economy seats. www.flightglobal.com/pdfarchive/view/1978/1978%20-%200500.html
267. It has also been suggested that higher fares following the sharp rise in fuel prices caused some downtrading from First Class.

6.42 Virgin Atlantic began transatlantic services in 1984, marketing its Upper Class as emulating other airlines' First Class products but at a Business Class price. Virgin upgraded its product in 1989, offering a sleeper-recliner seat with a seat pitch of 55 inches. At this time, Virgin's network was still in its early development stage and consisted of a daily service to New York and a four times a week service to Tokyo, both from Gatwick because of regulatory restrictions on access to Heathrow.

6.43 In late 1995, BA introduced a new cradle seat in Business Class with a 50 degree recline, increasing seat pitch from the previous 40 inches to 50 inches. In 1996, BA introduced a 6½ foot flat bed in First Class, in part in response to Virgin's Upper Class. A number of other airlines also offered flat beds in First Class.

6.44 In 2000, BA introduced the first-ever six-foot flat bed in Business Class, albeit not quite as long or wide as its First Class offering. Simultaneously, BA introduced a fourth cabin, Premium Economy, with wider seats than Economy and greater seat pitch (discussed at paragraphs 6.55 to 6.61 below). To accommodate the flat beds and new cabin, BA significantly reduced the number of economy seats (Table 6-4), so that a typical 747 configuration on a business route had 14 First, 70 Club World and 30 Premium Economy seats, comprising 39% of the 291 seats, but taking up a proportionately much greater cabin area.[268]

Table 6-4 BA fleet reconfiguration to accommodate lie-flat beds and Premium Economy, 2000

	Number of seats					**(a) Proportion of seats (b) *Seats abreast***				
Aircraft type (configuration variant)	**total**	**First**	**Club World**	**World Traveller Plus**	**World Traveller**		**First**	**Club World**	**World Traveller Plus**	**World Traveller**
747-400 (old)	393	14	55	n/a	324	(a)	4%	14%	n/a	82%
						(b)	*1-2-1*	*2-3-2**	*n/a*	*3-4-3*
747-400 (new 1)	291	14	70	30	177	(a)	5%	24%	10%	61%
747-400 (new 2)	359	14	38	36	271	(a)	4%	11%	10%	75%
						(b)	*1-2-1*	*2-4-2**	*2-4-2*	*3-4-3*
777-200 (old 1)	235	17	70	n/a	148	(a)	7%	30%	n/a	63%
777-200 (old 2)	267	14	56	n/a	197	(a)	5%	21%	n/a	74%
						(b)	*1-2-1*	*2-3-2*	*n/a*	*3-3-3*
777-200 (new)	227	14	48	40	125	(a)	6%	21%	18%	55%
						(b)	*1-2-1*	*2-4-2*	*2-4-2*	*3-3-3*

Source: BA Worldwide Timetable 2001/02.

*Notes: * Main deck.*

Configurations are representative for the aircraft type, but there are variations.

Club World = Business Class, World Traveller Plus = Premium Economy. World Traveller = Economy.

6.45 Virgin followed BA's move, launching in 2000 an 'angled' lie-flat seat in Upper Class that was longer and wider than BA's First Class. This was replaced in 2003 when a new, fully flat-bed product was installed across the fleet. On Virgin's Airbus A340-600, for example, the 50-seat Upper Class configuration changed from six-abreast to a 45-seat three-abreast with seats oriented in 'herringbone' configuration giving around twice the number of seat rows. BA upgraded its Business Class in 2006 and added

268. BA's current seat plans can be viewed at www.britishairways.com/travel/seatpl/public/en_gb.

another 14 seats to those 747-400 aircraft which previously had been configured (for less dense business routes) with only 38 seats (see Table 6-4), at the expense of 36 economy seats.

6.46 Figure 6-4 shows that BA's 2010 Club World Business Class cabin bears little resemblance to the 1984 Super Club.

Figure 6-4 BA Business Class 1984 and 2010

Super Club 1984

Club World 2010

Photographs courtesy of BA www.ba.com.

6.47 Table 6-5 shows the current aircraft configurations in Virgin Atlantic's fleet. It can be seen that broadly around 70% of seats are Economy Class with the remainder made up of Upper (Business) Class and Premium Economy. The exception is the Boeing 747-400 in configurations 1/2, which has only 14 Upper Class seats and more Economy seats. These aircraft are used on leisure routes from Gatwick and Manchester. The number of Premium Economy seats in Virgin's fleet has increased significantly compared with earlier configurations.

Table 6-5 Virgin Atlantic current fleet configurations

		Number of seats				*Proportion of seats*		
Aircraft type (configuration variant)	**Fleet**	**Total**	**Upper Class**	**Premium Economy**	**Economy**	**Upper Class**	**Premium Economy**	**Economy**
Airbus A340-300	6	240	34	35	171	14%	15%	71%
Airbus A340-600	19	308	45	38	225	15%	12%	73%
Boeing 747-400 (1 & 2)	7	451/452	14	58	379/380	3%	13%	84%
Boeing 747-400 (3)	5	367	44	62	261	12%	17%	71%

Source: www.virgin-atlantic.com/en/gb/allaboutus/ourfleet/index.jsp, CAA records.

6.48 In December 2009, Virgin announced[269] that from January 2010 it would begin reconfiguring its 747s based at Heathrow with a new upper deck layout to replace 10 Upper Class seats (total from 54 to 44) with 33 Economy Class seats (configuration 3).

6.49 A number of airlines followed BA and Virgin with lie-flat Business Class products. By 2007 there were reportedly around 10 airlines worldwide offering fully horizontal lie-flat business class seats and another 30–40 offering angled lie-flat seats.[270] Angled seats convert to a lie-flat bed but, to save space, the bed is not horizontal but set at a slight angle to the floor (examples are 7°, 10° or 13°).

269. *Virgin to cut business class capacity,* www.businesstraveller.com (3 December 2009).
270. *Flat out*, Airline Business (January 2007).

6.50 This trend has continued (Table 6-6). In some cases, notably US airlines, the upgrade to a lie-flat seat has happened relatively recently. This may appear surprising given the reported customer preference for a flat-bed product. The long lead times and cost of reconfiguring aircraft or introducing all-new cabin concepts mean that airlines can appear to react slowly to changing travel patterns. The lag has also been attributed to the poor financial position of US airlines over this period, and the fact that the UK market was ahead of other markets served by foreign airlines which need to maintain fleet commonality.

Table 6-6 Introduction of lie-flat Business Class seats (selected airlines only)

Date	Airline	Notes
2000	British Airways	
2000	Virgin Atlantic	Angled lie-flat until upgrade 2003
2001	Cathay Pacific	Angled lie-flat until upgrade 2007
2002	Singapore Airlines	Angled lie-flat until upgrade 2006
2002	Continental Airlines	Angled lie-flat on 777 until upgrade 2009
2003	Lufthansa	Angled lie-flat
2003	Qantas	Angled lie-flat, upgrade began 2008
2005	Air New Zealand	
2006	Emirates	Angled lie-flat, fully flat on A380
2006	American Airlines	Angled lie-flat
2006	Air Canada	
2006	Air France	Angled lie-flat
2007	United Airlines	
2008	Delta Air Lines	
2009	US Airways	

Source: Adapted and updated from Flat Out, Airline Business January 2007; US carriers go fully flat in business, www.businesstraveller.com*, 11 September 2009;* www.seatplans.com*;* www.buyingbusinesstravel.com*;* www.flatseats.com.

Notes: Seat adapts to horizontal, fully flat bed except where stated. Dates are approximate as roll-out across the fleet may be spread over an extended period.

6.51 On some of its fleet, Singapore Airlines introduced the widest Business Class seat in the industry (30 inches), in a configuration which increased the floor space per person by 25%–30% compared with the previous configuration. The airline was acting on feedback from customers that they wanted more privacy, comfort, a fully flat bed and aisle access, and were prepared to pay extra for it (or at least their companies were).[271] In contrast, when announcing its own introduction of flat beds in 2008, Continental Airlines said it would keep the same number of *BusinessFirst* seats and would not increase fares.[272]

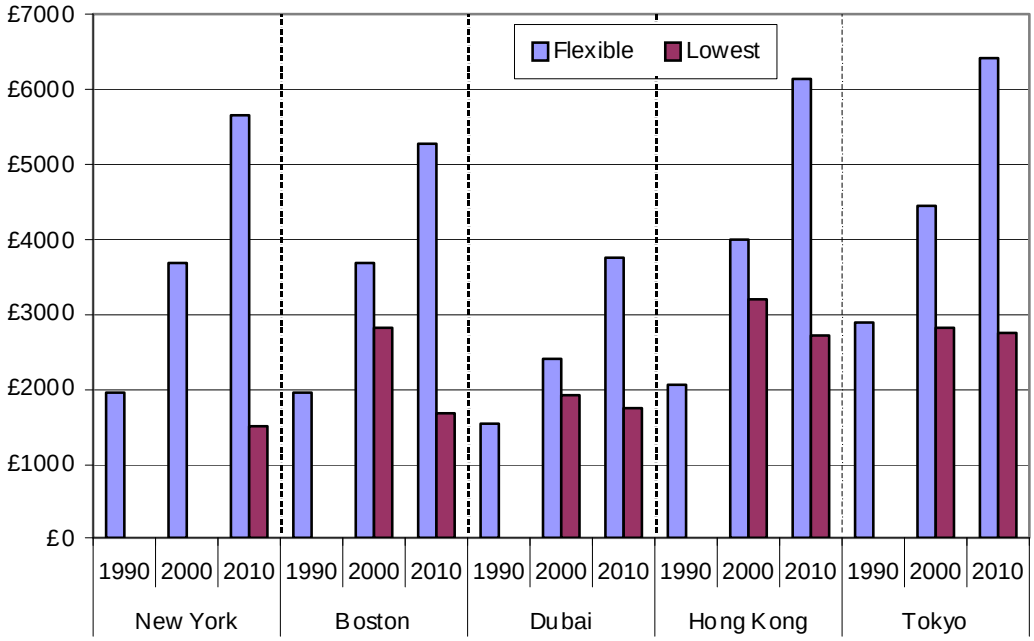
271. *ibid*. The latest SIA A380 Business Class seat is "the widest in its class" at 34 inches wide. www.singaporeair.com/en_UK/flying-with-us/business-listing/.

272. Continental's Chairman/Chief Executive is quoted as saying "Beyond lie-flat, the biggest thing that came up from our corporate customers was you've got to make sure you stay price-competitive." *Continental joins flat-bed brigade*, www.businesstraveller.com (29 July 2008).

6.52 There seems to be general agreement in the industry[273] that a flat bed is becoming the minimum requirement for longer or overnight Business Class flights. Compared with travelling economy, employees are more likely to arrive in reasonable shape and with less need for a recovery period with associated hotel costs. The flat bed has therefore been a key differentiator for BA and Virgin competing against foreign carriers in UK long-haul markets. As discussed earlier, other product considerations also influence choice, as well as network, schedule, pricing etc, but research for this study suggests that an airline without a flat-bed product would potentially lose business (or would need to price more cheaply).

6.53 These product upgrades represent a significant investment by airlines in new product. Not surprisingly, flexible fares in Business Class appear to have risen substantially, as shown by Figure 6-5, although much lower conditioned fares are also available. It should be noted that these are 'published' fares and do not reveal the overall picture once – often very significant – corporate discounts are taken into account.

Figure 6-5 BA Business Class fares on top five long-haul business routes, 1990, 2000, 2010



Source: Airline Tariff Publishing Company, Worldspan GDS, CAA records.

Notes: Fares are published fares excluding IATA fares used for interlining. Fares are not adjusted for inflation. They include fuel and insurance/security surcharges but not airport/passenger service charges or government taxes.

Fare levels are shown as at December each year. The lowest fare includes any short-term fares on sale in early December.

273. For example, Delta's sales director for UK and Ireland is reported as saying that the comfort of a flat-bed seat with direct aisle access is a must-have for frequent business travellers on flights to London. *US carriers go fully flat in business*, www.businesstraveller.com (11 September 2009).

6.54 Changes to the Business Class product should also be viewed in the context of other cabins. For some years there have been instances of various airlines discontinuing a separate First Class cabin in favour of an enhanced Business Class. An increasing number have also introduced a Premium Economy cabin. For example, of the 15 airlines shown in Table 6-6, five do not have a separate First Class product,[274] while six now have a Premium Economy cabin.[275]

Premium Economy

6.55 Premium Economy was first introduced in the UK in 1992 by Virgin Atlantic, which originally branded it as Mid Class. The concept appears similar to the first Business Class products introduced in the late 1970s, discussed earlier, except that a greater standard of comfort was offered, such as a 38-inch seat pitch. Initially, Virgin seated all passengers buying a flexible economy fare in the new cabin, a clear indication that the product was originally aimed at differentiating the economy product to attract business passengers constrained by cost or company travel policy from travelling Business Class. Virgin rebranded the cabin as Premium Economy in 1994 as the term Mid Class was being misinterpreted as meaning Business Class,[276] in doing so Virgin claimed that at least half of its business passengers were using the cabin.[277] EVA Air of Taiwan also offered a Premium Economy cabin at this time, but in general other airlines did not immediately react to the new concept.

6.56 BA first introduced a Premium Economy product (World Traveller Plus) in 2000, coincident with its introduction of flat beds in Business Class. The widening gap between the quality and price of UK airlines' Business and Economy products seems likely to have been a factor in creating a niche for this product, and the timing of BA's introduction of the new cabin probably reflects this.[278] On routes such as New York, Hong Kong and Johannesburg, for example, BA set the flexible fare in the new cabin around 25% to 30% higher than the equivalent flexible fare in Economy, with a restricted advance purchase fare at a 30% discount. By this time Virgin was also offering flexible fares in both Premium Economy and Economy cabins, but not a conditioned fare[279] in Premium Economy.

6.57 Premium Economy remained largely a UK phenomenon for some years. In 2006, when introducing an updated Premium Economy seat, Virgin drew attention to significant growth in demand for the cabin, noting that on Heathrow routes the proportion of leisure and business passengers using the cabin was around equal.[280] Despite the competitive advantage which UK airlines were enjoying, it is only relatively recently that some foreign airlines have launched their own Premium Economy products in various forms (and many still do not offer it). This is because these airlines saw little demand for this product in non-UK markets. Offering it would have meant configuring aircraft specifically to operate to the UK, which was unlikely to be a rational use of the fleet in terms of the additional revenue generated.

274. Air Canada, Air New Zealand, Continental, Delta, US Airways and Virgin. In addition, other airlines have removed First Class from some aircraft in their long-haul fleet.
275. Air France, Air New Zealand, BA, Qantas, United and Virgin.
276. Travel Weekly 28 September 1994.
277. Such passengers might also include employees of smaller companies without the buyer power to achieve any significant discount on Business Class fares.
278. Company Barclaycard annual *Travel in Business* surveys of more than 1000 UK business passengers each year found that in 1998 only 24% of respondents believed business class products provided good value for money, and that this proportion had fallen to just 15% in 2004. Mason K.J.: *Observations of fundamental changes in the demand for aviation services*, Journal of Air Transport Management 11, 19–25 (2005).
279. That is, a fare with restrictions on booking or travel, see Table 6.8.
280. *New Virgin Premium Economy Seat,* www.businesstraveller.com (28 September 2006). CAA passenger survey data shows that the proportion of Virgin's Premium Economy passengers travelling for business purposes was 63% in 2007 but had fallen to 42% by 2009, partly as a result of a general shift in the route mix, in particular fewer passengers on the New York route.

6.58 Table 6-7 compares the seat pitch of the main Premium Economy offerings in the UK market by reference to Economy and Business Class. Business Class offerings vary quite widely, but in terms of seat pitch at least, most Premium Economy offerings are similarly positioned in relation to Economy Class.

Table 6-7 Premium Economy seat pitch compared with long-haul Business and Economy Classes (selected airlines only)

Airline	**Business** **Seat pitch or flat bed length (inches)**	**Premium Economy** **Seat pitch (inches)**	**Economy** **Seat pitch (inches)**
Air France	55–61	34–38	32–33.5
Air New Zealand	flat bed 79.5	35–40	31–34
All Nippon Airways	62–63 flat bed TBA	38	31
British Airways	flat bed 73	38	31–33
bmi British Midland	flat bed 78–80	49	31–32
EVA Air	61	38	33
Japan Airlines	58–62	38	30–32
KLM	60	34–35	31
Qantas	60 flat bed 80	38–42	31
SAS	79	38	32
Thai Airways Int.	55–61	42	32–34
United Airlines	54–55 flat bed 74–77	34–36	31
Virgin Atlantic	flat bed 79.5–82	38	31–32

Source: Buying Business Travel (January/February 2010) and The Business Travel Magazine (May/June 2010) updated from www.seatplans.com and www.seatguru.com July 2010.

Notes: The table is intended to illustrate, for each airline, the positioning of Premium Economy relative to other cabins in terms of seat pitch. However, the table should only be regarded as a guide as published information can vary, complicated by airlines having a variety of configurations, aircraft types and ongoing product roll-outs. Not all airlines shown offer Premium Economy on services to the UK. The table omits some short-haul services and airlines/aircraft types which are unlikely to serve Europe.

Seat pitch is the distance from one seat to the same point on the next seat. For fully flat beds the length of the bed is given as this is the more relevant measure.

6.59 With a range of flexible and restricted fares, Premium Economy could be seen as attracting both cost-constrained business passengers who would otherwise travel in Economy and leisure passengers seeking more comfort for a much smaller fare premium than Business Class. Premium Economy may be attractive where Business Class is not permitted by a company travel policy, either generally or on shorter or daylight routes where a flat bed is not deemed essential. It also offers the possibility of mixing Business Class in one direction with Premium Economy in the other, depending on schedule or other considerations. The product can therefore be a useful part of the proposition by airlines to attract corporate custom. Several airlines have introduced a new Premium Economy cabin during the downturn, and research for this study indicated some instances where Premium Economy has attracted passengers

trading down from Business Class following a tightening of travel policies. However, lead times mean that airlines would have made the decision to introduce a new cabin two to three years earlier, i.e. well before the downturn.

6.60 From the airline's perspective, the relative seating densities combined with a good load factor means that revenue per square foot of cabin space from Premium Economy can be quite favourable in comparison with both Business and Economy Classes. However, the level of demand for Premium Economy is reported as quite route-specific, with less acceptance in some inbound business markets (Africa was given by one airline as an example). Conversely, where demand is high, the relatively small number of Premium Economy seats offered may mean that the product is not always available for business travellers booking close to departure.

6.61 The range of fares offered by airlines in Premium Economy has widened to include both flexible and conditioned fares (see Table 6-8 later in this chapter). A sample of BA and Virgin short-term tactical fares[281] suggests that it is common for a fare in Economy Class to be mirrored by an equivalent fare in Premium Economy, set a suitable amount higher, but that there is little linkage in terms of timing or fare level with tactical fares introduced for Business Class travel.

Pricing developments

6.62 Air fares have evolved considerably over the years alongside changes in the products on offer. The original concept of two cabins, First and Economy, with a single flexible fare available in each cabin, plus perhaps an additional economy excursion fare, has given way to a complex mix of products (including the introduction of separate Business and Premium Economy cabins) and fare types covering a broad spectrum of passenger requirements. During the 1990s there was a general shift away from the previous rigid adherence to fares set through airline negotiation at IATA conferences.[282] Airlines began introducing more fares unilaterally, restricted to travel only on their own flights (or those of their alliance partners), and travel at IATA fares became relatively uncommon.

6.63 The result was that published fares in the market began to show some variation as airlines began to compete on price as well as product. Coupled with this was the gradual removal of government restrictions on fare levels, allowing greater innovation, for example in indirect fares, which for many years were artificially held at the level of the direct fare, forcing any price competition into a 'grey' market. The internet has also had a significant impact in allowing the passenger to make quick and easy price comparisons which, in turn, has influenced the way airlines price.[283]

6.64 On long-haul routes there is generally a range of fares offered in each cabin catering for passengers requiring tickets with varying degrees of flexibility. Fare levels may vary according to the days of travel, time of year, booking class, and fare conditions such as advance purchase, minimum stay, or penalties for reservation changes. Most will be round trip fares, requiring return on the same airline. Depending on the competitiveness of the market, levels of the lowest fares in particular may change quite frequently as airlines seek to match demand with supply.

281. From the Airline Tariff Publishing Company database.
282. Such fares were relatively flexible in that they could be used for travel on any IATA airline. Some governments required that fares be set through IATA. The exemption from EU competition law for IATA passenger tariff coordination conferences was removed in 2007.
283. Accepting that Global Distribution Systems have always made fare levels reasonably transparent to travel agents – although on many long-haul routes price competition in published fares was in any case fairly limited until the last decade. Fare developments in the UK market are explored in more detail in the CAA's 2006 consultation document on removing the regulation of air fares www.caa.co.uk/docs/589/20060803ConsultationDocument.pdf .

6.65 Airlines control how much of their seat inventory is released at any particular price point by dividing each cabin of the aircraft (First, Business, Premium Economy and Economy) into a number of booking classes to which individual fare types are assigned. This revenue management allows them to differentiate passengers (and thus segment the market) according to the price that each passenger is willing to pay.[284] Factors influencing the airline's revenue management decisions and therefore the prices offered include the days remaining until departure, the booked load factor, the forecast of total demand by price point, and competitors' pricing. The revenue management system will decide at what point inventory is closed off to passengers that are likely to be lower yielding.

6.66 In the last decade, airlines have been revenue-managing premium cabins more carefully, introducing lower fares to encourage passengers wanting extra comfort to trade up, marking something of a change in strategy. Airlines are aiming to fill premium seats on more lightly loaded flights that might otherwise have remained unsold, boosting load factor and maximising revenue. In order to protect yield from existing premium cabin passengers who might trade down, thereby diluting revenue, the booking classes for these fares are subject to capacity controls to ensure that sufficient seats to meet late-booking business demand are available, albeit at higher prices. The fares are also conditioned to make them less attractive to business passengers, for example penalising reservation changes and requiring advance purchase and a Saturday-night or seven-day stay.

6.67 BA, followed by other network airlines, including Virgin, broadened its published fare offering in long-haul premium cabins in 2000, moving from one or two flexible fares in each cabin to a range of flexible and conditioned fares, which has continued to broaden since then. Table 6-8 shows the evolution of Virgin Atlantic's published fare structure on London–New York, which is typical of long-haul fare structures from the UK generally. (The table shows only 'published' fares, that is, fares visible to all subscribers to Global Distribution Systems. There is also a range of confidential negotiated fares available only to selected corporates or travel management companies, so the table shows only part of the picture.)

6.68 The table illustrates how the fare structure has broadened over time and the wide span in fare levels, not just between Upper Class and Economy cabins, but also within the cabins themselves. In Upper Class, for example, Virgin has moved from two booking classes in 2000 (J, D) to four by 2009 (J, D, R, Z). The different fare levels within a cabin are distinguished by both the reservation booking class and more onerous conditions attached to the lower fares. For example, all fares in the table except those in J, W and Y classes, and some in D class, require a Saturday-night stay. Therefore, the fare quote for an itinerary which does not include a Saturday-night stay will exclude such published fares irrespective of whether the class in question has seats available for those flights.

6.69 This is illustrated by Table 6-9, which compares sample fare quotes for a long-haul trip the following week, one including a Saturday night stay and one not, repeating this for a trip several weeks ahead to capture any additional fares which have an advance purchase requirement. Although only a snapshot, the results are typical of the wider picture.

284. With fares fluctuating over time, some bookings made long in advance, sales in third countries, through fares for multi-sector journeys and so on, a typical network airline has to manage a wide variation in revenue from bookings on any given flight. This sort of complexity is largely avoided by the one-way pricing model of no-frills airlines (described in the third section of this chapter). Internet booking has driven simplified long-haul fare structures to some extent, so as to allow the website to display a simple choice of price options for A to B journeys (for example, cabin choice and flexible or non-flexible conditions) and the ability to combine one option with a different option on the return leg.

Table 6-8 Virgin Atlantic London–New York fare structure

Cabin	Fare type		1990	1995	1997	1999	2001	2003	2005	2007	2009	Round trip fare level 2010
Upper	flexible (interlineable)					✓	✓	✓	✓	✓	✓	£6197
Class	flexible		✓	✓	✓		✓	✓	✓	✓	✓	£5560 & £5766 (1)
	Apex 1 (7D)						✓	✓	✓	✓	✓	£4873 & £5079 (1)
	Apex 2 (14D)										✓	£3890
	Apex 3 (30D later 28D)	☒					✓	✓	✓	✓	✓	£3340 & £3546 (1)
	Apex 4 (28D)	☒									✓	£2636 & £2749 (2)
	Apex 5 (42D later 28D)	☒						✓	✓	✓	✓	£1929 & £2157 (2)
	Apex 5 (28D)	☒										£1498 (3)
Premium	flexible (interlineable)			✓	✓	✓	✓	✓	✓	✓	✓	£2999
Economy	flexible			✓	✓	✓	✓	✓	✓	✓	✓	£1918 & £2068 (1)
	Apex 1 (7D)	☒						✓	✓	✓	✓	£1582
	Apex 2 (21D)	☒					✓	✓	✓	✓	✓	£1242 to £1469 (1)(2)
	Apex 3 (21D)	☒									✓	£892 to £1119 (1)(2)
Economy	flexible		✓	✓	✓	✓	✓	✓	✓	✓	✓	£1196
	types/tiers of leisure fare	☒	4	5	5	6	6	6	5	6	5	£392 to £939 (1)(2)

Source: *Airline Tariff Publishing Company, CAA records.*

Notes:
Fare structure applicable for travel as at July each year.
Fares are published fares excluding inclusive tour, group, student fares etc.
Fare levels include all taxes, fees and charges rounded to nearest £.
Apex fares show minimum advance purchase period in brackets.

☒ Saturday night minimum stay required.
(1) Supplement applies for weekend travel.
(2) Fare level varies by season.
(3) Limited selling and travel period; similar fares were available in 2007 and 2009 but selling in June.

Table 6-9 Lowest BA Business and Economy Class fares for a five-night trip Heathrow–San Francisco–Heathrow

Date of booking: 10 Nov 2010		Stay	Class of travel	Fare level	Fare code	Comments
Travel out	**Travel back**					
Mon 15 Nov	Sat 20 Nov	5 nights	Lowest Economy Class fare (return)	£1765	Y2	No Saturday-night stay means quote defaults to flexible Y2 fare even though lowest fare was requested
			Lowest Business Class fare (return)	£5962	C2BAD	Lower D2BAD fare requires advance purchase of seven or more days
Wed 17 Nov	Mon 22 Nov	5 nights incl Sat night	Lowest Economy Class fare (return)	£523	NLXRCGB	Lowest published fare for this itinerary and booking date
			Lowest Business Class fare (return)	£4411	D2BAD	Lower Business fares require advance purchase of 28 or more days
Mon 6 Dec	Sat 11 Dec	5 nights	Lowest Economy Class fare (return)	£1765	Y2	No Saturday-night stay means quote defaults to flexible Y2 fare even though lowest fare was requested
			Lowest Business Class fare (return)	£4411	D2BAD	Lower Business fares require a Saturday-night stay
Wed 8 Dec	Mon 13 Dec	5 nights incl Sat night	Lowest Economy Class fare (return)	£523	NLXRCGB	Lowest published fare for this itinerary and booking date
			Lowest Business Class fare (return)	£3017	IHAPGB	Itinerary qualifies for 28-day advance purchase fare

Source: ba.com, Worldspan GDS, and Airline Tariff Publishing Company, 10 November 2010.

Notes: Fares include all taxes, fees and charges rounded to nearest whole £.

A quote was requested for the lowest fare, not a flexible fare.

6.70 Accepting that this snapshot is taken in the off-peak, the table shows that the lowest published fare available of just over £500 is not just available several weeks ahead but also the week before travel,[285] providing a Saturday night is included in the itinerary. If a Saturday night is not included, the quote defaults to the fully flexible 'Y2' economy fare because all the lower fares on this route, being aimed at leisure passengers, require a Saturday-night stay.

6.71 The prices for Business Class show a pattern of fares declining the further ahead the trip is booked because of advance purchase conditions on the fares. Both a Saturday-night stay and a 28-day advance purchase are required in order for the lowest Business Class fare to be quoted (the last example). All these quotes are for the lowest fares available, and except for the flexible Y2 fare, all have penalties for rebooking or cancellation.

6.72 Chapter 4 suggested that take-up of conditioned fares relative to flexible fares has been increasing. Travel management companies are encouraging business travellers to consider the potential savings from conditioned fares[286] through booking early, locking-in travel to fixed flight times and dates, and, if feasible, staying a Saturday night. Booking the lowest fare available on the day could be more cost-effective than the company-negotiated fare.

285. In the summer peak it is unlikely that the cheapest fare would be available so close to departure.
286. For example, Carlson Wagonlit Travel's *Smart Travel Guide* containing tips for companies to manage travel costs.

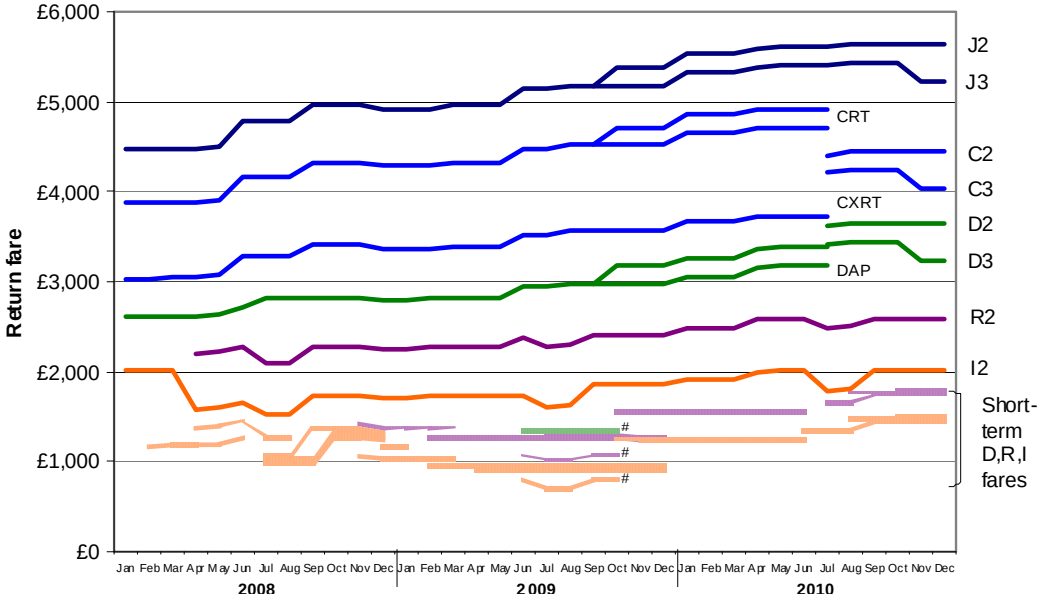
6.73 There is also some evidence that airlines have been offering more of these conditioned fares in premium cabins, or reducing the price of those already offered, usually for relatively short selling periods only, in order to attract more premium cabin business during the economic downturn. Figure 6-6 shows how BA has changed Business Class fares between 2008 and 2010 on the London–New York route. This chart only shows published fares, but anecdotal evidence is that airlines were also active in offering lower negotiated fares. The fare types range from the fully flexible fare in the highest booking class (J), which will give access to the last seats available, to the I Class fare which has conditions requiring advance purchase (initially six weeks, later four weeks), a Saturday-night stay, fixed bookings and no refunds.

6.74 What is apparent is that published year-round fare levels continued to rise during the downturn until a restructuring of fare types in mid-2010, but that there were numerous 'tactical' fares at considerably lower levels offered for short periods at a time. These fares can be attributed to the effect of the decline in premium traffic during the downturn, as discussed in Chapter 2.

6.75 Short-term tactical reductions of the most restrictive, I Class, fare were already on sale for specific periods during 2008 (indicated by orange shading in the chart). Short-term reductions in the less restrictive R Class fare (indicated by purple shading) appeared in late 2008, and in the D class fare (indicated by green shading) in the summer months of 2009 when the lowest fares of all were on offer. Although the summer months are the peak season for leisure travellers (and therefore when leisure fares would tend to rise significantly), they are the low season for business travel. Thus, these Business Class fares – albeit that the number of seats at these fares was strictly controlled – were not that much higher than the peak season economy fares over that period.

6.76 It is also apparent from the table of fare conditions that the restrictions on non-flexible Business Class fares are now less onerous than they were in January 2008, making these fares more attractive to, or accessible by, business passengers, although availability of any particular fare will be governed by inventory controls.

Figure 6-6 BA London–New York Business Class fares 2008–2010



Source: Airline Tariff Publishing Company, Worldspan GDS, CAA records.

Notes: Fares are published fares excluding IATA fares used for interlining. Fares are not adjusted for inflation. They include fuel and insurance/security surcharges but not airport/passenger service charges or government taxes.

Fare levels are shown by travel date. Short-term fares were on sale for relatively short periods (a few weeks or even days) and then repeated with slight variations in fare level and travel date.

 # Companion fares available June to October 2009 for two persons travelling together.

Short-term D, R, I fares are denoted by shaded lines, coloured by booking class.

Fare conditions as at January 2008 and December 2010 are shown in the table below:

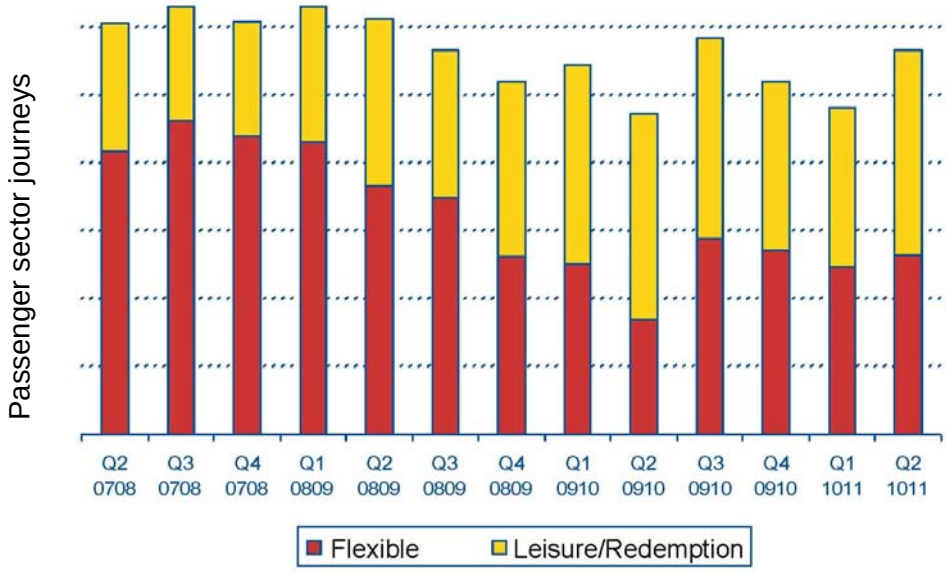
	capacity controlled	advance purchase		minimum stay		reservation changes/ cancellation	
		as at Jan 2008	as at Dec 2010	as at Jan 2008	as at Dec 2010	as at Jan 2008	as at Dec 2010
J		-	-	-	-	flexible	flexible
C	✓	7 or 14 days	3 days	-	-	❖	£200 penalty
D	✓	28 days	7 days	Sat. night	-	not permitted	£200 penalty
R	✓	n/a	28 days	n/a	Sat. night	n/a	not permitted
I	✓	42 days	28 days	Sat. night	Sat. night	not permitted	not permitted

J3, C3, D3 not available on peak flights

❖ 20% penalty for cancellation before departure, reservation changes require upgrade to J on payment of difference in fare plus £100

6.77 The greater use of conditioned fares in long-haul premium classes is also illustrated by Figure 6-7, which shows the proportion of BA First and Business Class journeys sold at flexible fares.

Figure 6-7 BA long-haul premium passengers by fare type 2007–2010



Source: BA first half results 2010/11 presentation, www.iagshares.com/.

Note: Precise figures or percentage values are not available.

6.78 Figure 6-7 shows that the proportion of BA long-haul premium traffic travelling at flexible fares steadily declined between the third quarter of 2007/08 (when it appears to have formed around three-quarters) and the second quarter of 2009/10 (when it appears to have fallen to around 40%), and that subsequently it has partially recovered, hovering around 50%. This is broadly in line with the recovery in the overall volume of BA premium traffic, allowing for seasonal effects.[287]

6.79 Given the much higher level of flexible fares (Table 6-8 and Figure 6-6), the challenge for airlines is whether, as demand picks up again, customer behaviour unwinds post-recession, or whether yields have ratcheted down a notch and do not return to where they were. If there remains a corporate memory of the potential for lower fares from booking ahead and accepting conditions on rebooking, or if company travel policies remain more restrictive on the use of Business Class, airlines which are reluctant or unable to reduce capacity in the short term may need to rely on more leisure traffic to fill the Business Class cabin.

6.80 Research for this study revealed mixed views about how strongly yield would return.[288] On long haul, some saw continued pressure from companies seeking greater value for money. However, there was also some agreement that it was ultimately a question of supply and demand and that airlines had to increase yield to survive, because, given the significant investment in upgrades to the product in recent years, the offering of heavy discounts in Business Class is unlikely to be sustainable. Assuming that the airline is competitive on product, they will achieve higher yields only by continuing to keep a check on capacity and taking advantage of any market strengths. There seems to be a generally held expectation that yields will return to 2007 levels in due course, although higher fuel prices remain a potential threat to containing costs.

287. Traffic for the first quarter of 2010/11 was depressed by the disruption from volcanic ash and industrial action.
288. Possibly reflecting differing timeframe perceptions of those interviewed.

Business-Class-only services

6.81 Some airlines have sought to identify a niche in the business travel market for services with only a Business Class cabin and no Economy Class. In the UK market there was significant new entry between 2005 and 2007 by airlines using this business model.[289] These airlines each targeted the London–New York route, the UK's densest long-haul business market (Table 6-1). However, they were prevented from operating to and from Heathrow (and potentially also to and from Gatwick) by restrictions in the UK–US air services agreement then in force.[290] Two US new entrant airlines, Eos and Maxjet, began Business-Class-only services between New York JFK and London Stansted in October and November 2005 respectively. Maxjet later commenced services to Stansted from Washington and Las Vegas as well. In January 2007 they were joined by Silverjet, a UK Business-Class-only airline, which operated between New York Newark and London Luton. Silverjet also began services between Dubai and Luton in November 2007.

6.82 The airlines offered slightly different in-flight products and prices. Maxjet and Silverjet products were similar to Business Class or Premium Economy products on larger airlines, whereas Eos saw its product as more comparable with First Class.[291] Eos Boeing 757s were fitted with 48 seats (fewer than one third of a typical mixed-class scheduled service 757 configuration), while Maxjet and Silverjet Boeing 767-200s were fitted with 102 and 100 seats respectively (broadly half the seats of a typical mixed-class scheduled service 767 configuration).[292] Fully flexible fares were set well below the level of the incumbent network airlines' published fares, not taking into account corporate discounts.

6.83 Between December 2007 and May 2008 all three airlines failed in succession (Maxjet suspended services in December 2007, Eos in April 2008 and Silverjet in May 2008). Meanwhile, in January 2008, BA announced a Business-Class-only service to New York JFK operating, uniquely, from London City, which commenced in September 2009. (This service is discussed further below.)

6.84 Each of the failed new-entrant airlines attributed its demise principally to high fuel prices, the economic slowdown and an inability to secure further investment in the prevailing global financing environment. They were also competing against bigger airlines that had the advantage of higher frequency, attractive frequent-flyer programmes, larger fleets which allowed cover in the case of operational difficulties, and hub locations which could draw on significant connecting traffic. Even if the new entrants were offering an attractive product and fares which were competitive with other airlines, it is likely that it would take time to attract business from companies which might be committed to some extent by existing corporate deals with more traditional airlines. Compared with Heathrow, the use of Luton and Stansted may have brought some advantages in terms of punctuality, cost (in that they would otherwise have had to purchase or lease suitable Heathrow slots on the secondary market) and service (for example, Silverjet offered a dedicated terminal at Luton). However, some business passengers may have regarded these airports as less convenient than Heathrow.

289. A more detailed description appears in Chapter 5, section 5 of *CAP 771 Connecting the Continents: Long-haul passenger operations from the UK*, CAA (2007). www.caa.co.uk/cap771
290. Irrespective of whether they could have acquired the necessary slots.
291. Eos was targeting the highest level of traveller with a very high standard of service, whereas Silverjet and Maxjet were targeting smaller businesses and affluent leisure passengers more accustomed to travelling Economy or Premium Economy. *Premier Upstarts*, Flight International (19–25 June 2007); *Business Flair*, Airline Business (August 2007).
292. Equating to a seat pitch of 60 inches (Maxjet), 66 inches (Silverjet) and 78 inches (Eos). Source: *All Business Airlines Grow Beyond Atlantic,* anna.aero (27 November 2007).

6.85 In catering for just one segment of demand, this business model is relatively exposed to shocks, in particular economic recession. For example, the model involves a relatively small number of passengers compared with an equivalent leisure offering, with fewer opportunities for growth; high costs of providing a product attractive to business passengers; providing last-minute seat availability for late booking passengers; and a need to attract passengers during the traditional trough periods for business traffic. Even if these airlines had survived high fuel prices, they would have been significantly affected by the recent sharp fall in business traffic. The model does not enjoy the flexibility of having revenue generated from multiple product offerings, and this includes, where narrowbody aircraft are used, less scope than widebody aircraft for bellyhold cargo carriage.

6.86 One conclusion might be that if this model fails in the dense London–New York market then it may be even less likely to work elsewhere.[293] However, BA is reporting that, based on the performance of its London City service, it is considering expanding the operation to add further all-Business-Class services to US East Coast destinations.[294] The all-Business-Class model has also been used on a number of long-haul services from Continental Europe dating back to 2002, and some of these have continued to operate despite the downturn. Arguably it could be significant that those still operating are by major EU network airlines, mostly using wet-leased aircraft.[295] (Ironically, the more successful the service, the more likely it will be upgraded from a niche product to a standard widebody operation, adding economy passengers to balance the traffic mix.)

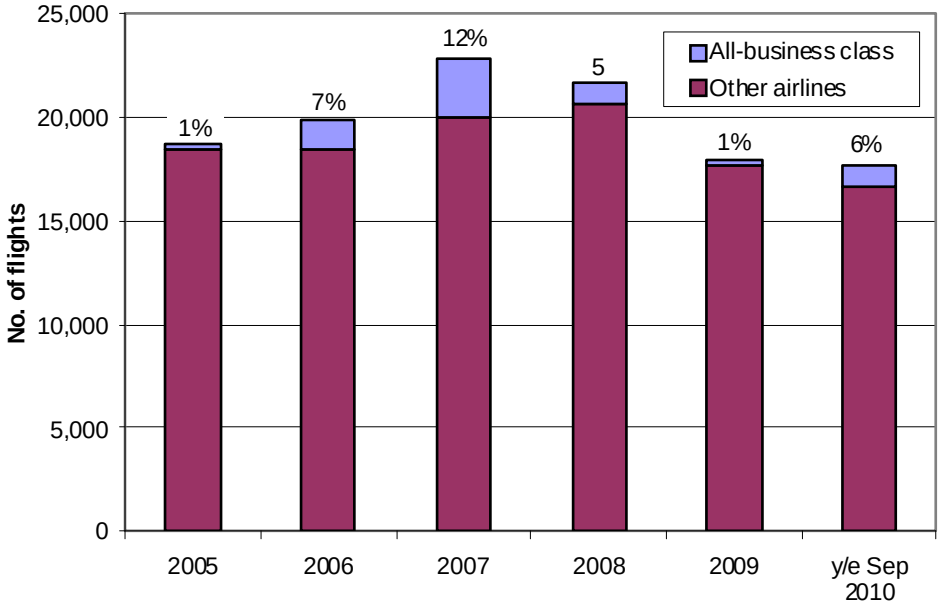
6.87 The signature of an EU-US 'Open Skies' agreement in 2007 led both BA and Virgin Atlantic to announce their intention to use the new freedoms to begin services from Continental Europe to the US, and that these services would consist of all or mostly premium class seats. Virgin has not pursued this idea, but BA set up a subsidiary branded as OpenSkies, which began services in June 2008 and which acquired French Business-Class-only operator L'avion the following month. OpenSkies currently operates between Paris (Orly) and both Newark and Washington using Boeing 757s in a two-class Business and Premium Economy configuration.[296]

293. Silverjet's Chief Executive suggested that Maxjet withdrew from the Stansted–Washington route within a few months because legacy airlines were more prepared to lower their fares on a route of that size than in the London–New York market where lowering fares would have too great an impact. *Creating a new premium market at Silverjet*, Airline Business (February 2007).
294. See for example www.breakingtravelnews.com/news/article/bas-willie-walsh-delivers-powerful-key-note-speech-at-business-travel-marke/ ; www.thisislondon.co.uk/standard-business/article-23874461-british-airways-boss-identifies-12-potential-takeover-targets.do
295. In the last few years these services have included KLM Amsterdam–Houston, Swiss Zurich–Newark, and Lufthansa Frankfurt–Libreville–Pointe Noire, Frankfurt–Pune, and Munich–Tashkent. Lufthansa started but suspended Business-Class-only services between Newark and Dusseldorf, Frankfurt and Munich, Munich and Chicago, and Munich and Dubai. All are/were operated by Privatair under a wet-lease arrangement using 44–56 seat Boeing 737-700/800 or 48-seat Airbus A319 aircraft. Lufthansa also offers Private Jet, an executive jet service. L'avion commenced services between Paris (Orly) and Newark in January 2007 using a 90-seat Boeing 757 and was subsequently acquired by OpenSkies (see paragraph 6.87). Eurofly operated an A319 for eight months between Milan and New York JFK in 2006. Source: various including *Premier Upstarts*, Flight International (19–25 June 2007), *Business Flair*, Airline Business (August 2007), Air and Business Travel News www.abtn.co.uk (31 January 2007), *All Business Airlines Grow Beyond Atlantic*, www.anna.aero (27 November 2007).
296. Business Class with 12 to 24 lie-flat bed seats, and Premium Economy with 40 to 72 seats at 52-inch seat pitch (L'avion's 757 was configured with 90 seats at 47-inch seat pitch) www.flyopenskies.com. OpenSkies also offered an Economy Class during the first season of operation. The airline began an Amsterdam–New York JFK service in October 2008 but suspended it in August 2009 after experiencing a significant fall in business traffic. Source: Air and Business Travel News www.abtn.co.uk (14 December 2009). Its Washington service commenced May 2010. Flights operate with both BA and OpenSkies codes.

6.88 BA's London City–New York JFK service commenced in September 2009, and currently operates twice daily on weekdays, using two dedicated Airbus A318 aircraft, the biggest aircraft that can fly into London City, configured with 32 flat-bed seats. Operational restrictions require the aircraft to stop at Shannon westbound to refuel (where the opportunity is taken to clear passengers in advance through US immigration). The service is aimed at a specific target market in the City of London and offers 15-minute check-in at London City. Passengers are able to combine London City flights in one direction with Heathrow in the other.

6.89 Figure 6-8 shows that all-Business-Class services formed 12% of total London–New York flights in 2007, before falling back to only 1% in 2009 as the airlines based at Stansted and Luton went out of business. In the twelve months to September 2010, BA's London City–New York JFK service has increased the proportion of all-Business-Class flights on the London–New York route to 6%.

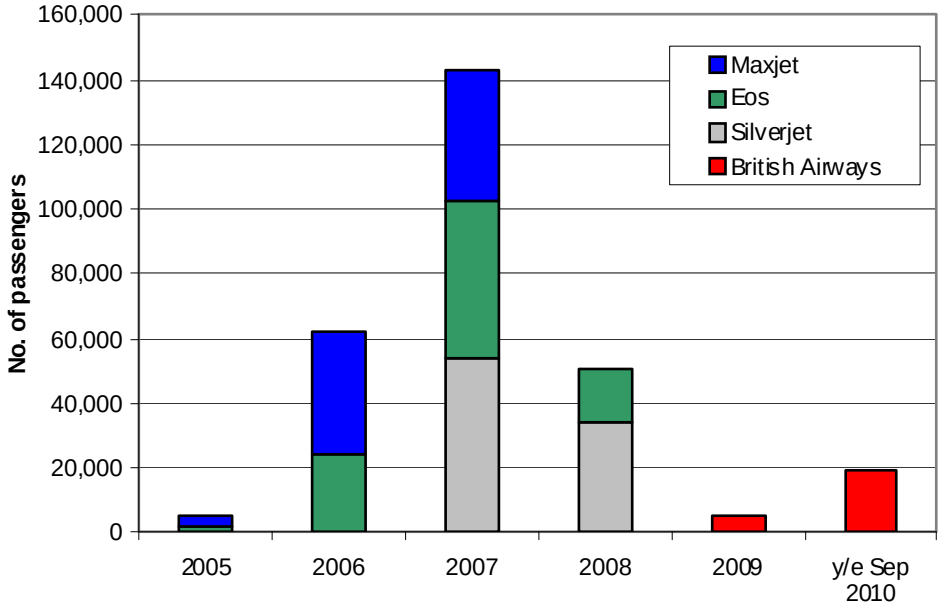
Figure 6-8 Proportion of London–New York flights operated by Business-Class-only airlines, 2005–2010



Source: CAA Airport Statistics

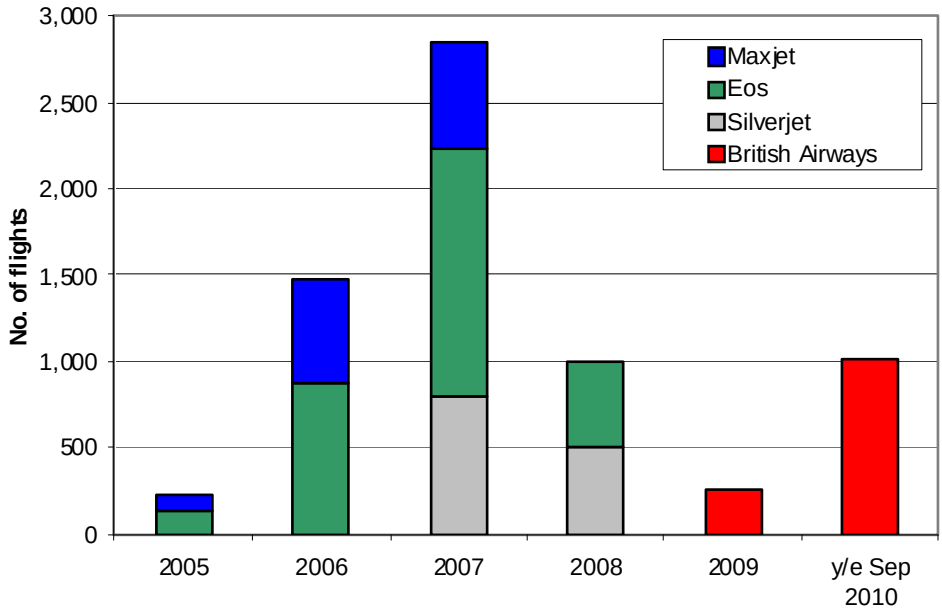
6.90 Figures 6-9 and 6-10 show the number of passengers carried and flights by all-Business-Class airlines since 2005.

Figure 6-9 London–New York passengers carried by Business-Class-only airlines, 2005–2010



Source: CAA Airport Statistics.

Figure 6-10 London–New York flights operated by Business-Class-only airlines, 2005–2010



Source: CAA Airport Statistics.

6.91 Figure 6-9 shows that the amount of New York traffic carried by the failed Business-Class-only airlines reached 143,000 in 2007, the only year when all three were operating simultaneously. This was relatively small (3.4%) compared with the total passengers who travelled on London–New York services in 2007 (4.1m). However, to the extent that the products are comparable, the three airlines represented a much

higher proportion, around 28%, of the 0.5m First and Business Class passengers[297] carried on the route in total in 2007, excluding connecting passengers. Figure 6-10 shows the number of flights operated and illustrates that Eos operated at a higher frequency than the other airlines.

6.92 With only 64 Business Class seats in each direction per day, fewer than the Business Class seats on one 747 flight in the configuration BA normally operates on the route from Heathrow, the impact of the London City service in terms of seats in the London–New York market is not that great. However, based on CAA survey data, the passengers it carried in the year ending September 2010 represent around 5% of the total number of First and Business Class passengers on the route in 2007 and 2008 (and 10% in 2009[298]) and 2% of passengers travelling for business purposes in 2007 and 2008 (and 4% in 2009), excluding connecting passengers in each case.

Evolution of products and pricing: short-haul services

Business Class product developments

6.93 There have been fewer changes in the cabin product on short-haul services in Europe than on long-haul services. The main change occurred in 1981 when BA replaced First Class with Business (Club) Class, with a moveable divider segregating the cabins allowing maximum flexibility to alter the configuration depending on the traffic mix.[299] This concept was also adopted by other European airlines. The middle seat of three would generally be left free.

6.94 BA subsequently introduced convertible seats which allowed a five-abreast configuration (on narrowbody aircraft) in Business Class through a substantial part of the aircraft, and six-abreast in Economy, adjusted for each flight as necessary. These seats were also used by other European airlines including Air France and Swissair.[300] Since then BA has reverted to blocking the middle seat in Business Class on narrowbody aircraft, thus giving four abreast.[301]

The impact of no-frills airlines[302]

6.95 The competitive impact of no-frills airlines on the short-haul market, including business routes, was explored in CAA reports on no-frills airlines and regional air services in 2006 and 2007.[303] No-frills airlines began to attract increasing amounts of business traffic,[304] leading network 'full service' airlines to adopt elements of the no-frills model (for example reducing costs, restructuring fares, increasing load factors and encouraging internet sales).

297. Including the 143,000 passengers carried by the three all-Business-Class airlines.
298. The higher figures from the 2009 survey data may represent airlines carrying more connecting premium / business passengers in this year, or more passengers being upgraded at the airport (which may not be fully captured in the survey).
299. Demand for Club Class was sufficient on some peak flights on prime business routes for the whole aircraft to be Club Class. Source: House of Lords debate, 17 March 1983. Some airlines were critical of the moveable divider www.youtube.com/watch?v=mbedmF4UMSIAirLibertéClasseAffaires.
300. Source: Doganis, R.: *Flying Off Course* (2002).
301. Air France and Lufthansa also use this approach but use moveable armrests to widen the effective seat width.
302. The distinction between network and no-frills airlines has become blurred, to the extent that the term 'no-frills airline' is looking increasingly inappropriate, although it is used in this study for want of a better term. Although Flybe does not class itself as a no-frills airline, its business model is included in the discussion.
303. *CAP 770 No-frills carriers: evolution or revolution?* (November 2006), www.caa.co.uk/cap770. *CAP 775 Air services at UK regional airports* (November 2007), www.caa.co.uk/cap775.
304. For example, the *Barclaycard Travel in Business Survey* (2001/02) recorded that 62% of respondents had travelled on low-cost airlines in 2001/02 compared with 53% in 2000/01, 39% in 1999/00 and 28% in 1998/99. The 2001/02 survey was based on a sample of 2,500 cardholders.

6.96 In the UK, no-frills services were initially focused on airports with ample spare capacity (Luton, Stansted and regional airports), bringing new services to these airports, including business routes, and therefore a wider range of options for business travellers. Since then, no-frills services have developed strongly at Gatwick also,[305] and in the Summer 2010 season made up more than 40%[306] of commercial flights there, in some cases competing directly with network airlines' services from Gatwick.[307] As for business traffic from regional airports, no-frills services are more likely to compete with network airlines carrying both point-to-point traffic and traffic connecting via a hub, such as Heathrow, Amsterdam or Paris. Links between UK regional airports have also improved; for example Flybe's network includes routes where its main competitors are surface modes. Flybe has adopted a hybrid variant of the no-frills model, combining a low-fares approach with appropriate frequency and schedule to attract business passengers to a route such as Exeter–Newcastle where a day trip is not realistic by rail.

6.97 A common factor which continues to link most no-frills airlines is that they operate a 'point-to-point' model and do not facilitate passengers making connections, because of the complexity this adds. In contrast, airlines using a network model operate short-haul flights carrying not just point-to-point passengers, but also feed for other flights on their (or another airline's) network. Connecting passengers and their baggage generally travel on through bookings and fares, and airlines will take responsibility for missed connections in the event of delay or cancellation. No-frills passengers may choose to build their own connection by buying separate tickets, but entirely at their own risk in the event of disruption. That said, there are hybrid business models using elements from the no-frills concept while also embracing interlining with other airlines, as in the Flybe example noted above. Flybe has codeshares with BA, Air France and Etihad, while Air Berlin has gone further and announced that it is joining the oneworld alliance, including codesharing with partner airlines. Flybe offers tickets in bulk[308] and reportedly also volume discounts tailored individually to larger corporate customers. It also has a frequent-flyer scheme. Frequent-flyer schemes are offered by various airlines using a point-to-point model,[309] but not the two largest in the UK market, easyJet and Ryanair.

6.98 No-frills airlines have, to varying degrees, 'unbundled' the short-haul product, as explained in paragraphs 6.106 onwards, and some, while staying with the low-cost philosophy, have introduced optional frills, giving the passenger a menu of chargeable options to choose from. Some no-frills airlines bundle these extras into a product aimed at business passengers. For example, easyJet has recently re-launched a separate flexible fare (see the case study below); while Flybe's Economy Plus product is inclusive of fully changeable tickets, advance seat selection, hold baggage, dedicated check-in, fast-track security, executive lounge and in-flight catering.

6.99 As network carriers have sought to contain costs, some have reduced the standard of in-flight service or introduced separate charges. An emerging model adopted by

305. For example, see *EasyJet to make Gatwick its main base*, www.ft.com (21 December 2001).
306. The main operators making up this figure are easyJet, Ryanair, Aer Lingus, Monarch (scheduled), Norwegian and Cimber Sterling. Including Flybe would add a further 9%.
307. It is worth noting in this context that the European Commission 2010 merger decision on Iberia/BA found that Heathrow, Gatwick and London City airports were substitutable for time-sensitive passengers flying between London and Madrid/Barcelona, and that a significant competitive constraint is exerted by no-frills airlines on BA and Iberia on these routes. Paragraph 25 notes that the average revenue per ticket coupon yielded by passengers flying on BA from those three London airports to Madrid broadly overlapped and followed the same pattern over time. Paragraph 83 records that one of Iberia's biggest corporate customers recently shifted a proportion of its London–Madrid travel from BA/Iberia to easyJet "and thus forced Iberia to offer it a special tariff". Case No. COMP/M.5747 – Iberia/British Airways, European Commission (14 July 2010).
308. www.flybe.com/flying_flybe/business_express.htm.
309. Examples in the UK market are Air Berlin, bmibaby, Flybe, Jet2, Monarch, Norwegian and Vueling.

airlines such as bmi (see case study below) and Brussels Airlines is to bundle additional services with a flexible fare, but with few frills for restricted economy fares. Apart from the ability to interline with other airlines, the product could be seen as not that different from the flexible product offered by airlines such as easyJet and Flybe.

6.100 It is therefore increasingly difficult to categorise short-haul airlines, as the distinction between network and no-frills (as well as charter) models continues to blur. Each airline has been seeking to adapt to the challenge posed by competing business models and to find its unique selling proposition. From the business passenger perspective, there is a realisation that by accepting a more basic, unbundled product, there is the potential for substantial savings, as discussed in Chapter 4, and therefore an expectation of lower fares on short-haul routes (on all airlines) compared with the position before no-frills airlines entered. From the supplier perspective, it has resulted in a rich mix of dynamic, competitive airlines and air services with a range of different offerings in the UK market.

Case Study: easyJet building its appeal to business travellers

easyJet was born out of the liberalisation of the intra-EU air services market, innovating with a low-cost business model, internet sales and transparent pricing. It has grown from bases in London and the UK regional airports to develop a significant presence in mainland Europe including operations at slot-constrained airports. easyJet sees market share in the business segment as a very important focus for the company, and managed to increase this share in 2009 despite the tough economic environment, based on a model of offering low fares to convenient airports. In 2010 it is adding new routes to business destinations, improving frequencies and increasing the proportion of flights at peak times of the day. Around 18% of its passengers network-wide are travelling on business and easyJet believes that between 21% and 23% is possible within five years. CAA Passenger Survey data shows that in 2009, 20% of easyJet's passengers on London routes were travelling for business purposes.[1]

Part 1 of this study showed that in 2007, 36% of easyJet international routes from London were to primary airports, which may be more attractive to business passengers, compared with 7% of Ryanair's. easyJet has continued to add to its route network from Gatwick and now holds nearly one third of slots there (around twice the number held by BA) compared with only 7% in 2002. easyJet's previous Chief Executive has said that moving the main base to Gatwick had encouraged business passengers to switch to easyJet.

easyJet's standard product allows rebooking up to two hours before a flight (for a fee), switching at the airport to seats available on an earlier flight (without penalty) or to seats available on the next flight if the original was missed (for a flat fee of £43), lounge access (for a fee), priority boarding, including an annual pass for frequent travellers (for a fee), and no hand baggage weight limit.

In November 2010 easyJet re-launched a separate flexible fare specifically aimed at business travellers. The new fare, priced at £99 or higher, one-way including taxes, and intended to undercut the flexible fares of network airlines, will allow unlimited changes to travel dates within a four-week window of the original booked travel date (one week before and up to three weeks after). Flexible fares are 'bundled' with priority boarding and one hold bag without extra charge and have no booking fees. However, easyJet has announced no plans to offer an enhanced on-board product specifically for business passengers.

1 Only certain UK regional airports were surveyed in 2009.

easyJet recognises that the business travel market has different booking requirements to other markets, in that large corporates have strict travel management policies and manage their travel through agents/travel management companies (TMCs) using Global Distribution Systems (GDSs).

In 2008 easyJet made bookings available via the GDS and other aggregator systems (claiming to be the only no-frills carrier in Europe to be connected to Galileo, Sabre and Amadeus). Its flights are therefore now listed on agents' GDS screens alongside other carriers to capture 'best fare on the day' bookings (rather than the TMC having to use 'screen-scraping' technology and booking via the easyJet website). By September 2009, easyJet says that around 15% of business passenger bookings were through this channel, and that the yield premium per seat from such bookings can be around 20%. Until early 2011, the new flexible fare will only be available through this channel to allow any fine-tuning to the fare.

In September 2008 the Guild of Travel Management Companies (GTMC) reached agreement with easyJet to reduce the cost of a GDS booking from €12 to €8 per round trip and to charge passengers booked through a GDS £5 rather than up to £9 for priority boarding and check-in, and in some cases a lower rate for carriage of hold baggage. Therefore, bookings via a TMC which include priority boarding would be cheaper than if booked direct.

In April 2010 easyJet underlined its commitment to the business travel market by joining GTMC's partnership scheme for travel suppliers. easyJet does not negotiate volume discounts in the traditional way. This is because its business model already relies to a great extent on driving volume through offering low fares and undercutting the competition. However, it has recently begun one-to-one discussions with individual companies and TMCs on why the carrier should form part of a corporate programme. This has resulted in easyJet starting to sign preferred carrier agreements with a limited number of corporate clients. easyJet is encouraging them to follow a 'best fare on the day' policy. easyJet claims that its on the day fares will be lower than net corporate rates on around 80% of occasions, with the saving exceeding £100 per one way short-haul segment on 43% of occasions. With many companies questioning value for money on short-haul flights, easyJet's Head of Corporate Sales has observed that the airline is particularly attracting attention from organisations in the public sector and companies that have openly committed to cutting their travel costs.

Source: *Part 1 of this study (Table 3.4); CAA interview with easyJet; www.easyjet.com (press releases, 2009 annual report and 2010 full-year results statement); GTMC press releases;* easyJet cashes in on search for value*, The Times (22 January 2010);* easyJet gets down to business with flexible fares*, The Times (17 November 2010); www.businesstravelnews.com/Business-Travel/Travel-News-UK/Articles/EasyJet-Stepping-Up-Corporate-Travel-Offerings/; www.flightglobal.com/articles/2010/11/16/349760/easyjet-targets-business-travellers-with-flexible-fares.html.*

The decline in demand for short-haul Business Class

6.101 Table 2-4 shows that the proportion of business passengers travelling in a premium class on short-haul flights to and from London has fallen dramatically from 41% in 1996 to only 5% in 2009. Association of European Airlines figures show that there have been significant falls in premium short-haul passengers across Europe in the last few years, even before the recession. Compared with the previous year, premium passengers within Europe fell by 4% in 2006, 8% in 2007, 11.5% in 2008 and 19% in 2009, a cumulative fall of 36.7% since 2005.[310] While some premium short-haul travel is expected to return after the recession, overall there appears to have been a continuing structural shift in the market, which shows little sign of unwinding,

310. *Cabin sickness*, Airline Business (May 2010).

towards accepting 'best fare on the day' in Economy Class.[311] The change in fares is particularly stark for journeys from regional airports, where there has been a significant expansion in the range of direct services to business destinations. A business trip which may previously have required a connection over a hub, and possibly also an overnight stay, can now often be done as a day return.[312]

6.102 As noted in Chapter 4, some travel buyers are commenting that the short-haul market has become more commoditised and is now largely driven by price. This may represent a challenge for airlines seeking to maintain some brand loyalty. It remains to be seen whether and where Business Class remains in place on short-haul routes. BA continues to offer Business Class on short-haul routes to Europe, whereas it has never offered a separate cabin on domestic routes. bmi no longer offers a separate Business Class on its remaining short-haul routes except where operating in conjunction with another Star Alliance airline (see the case study below). What seems likely is that business passengers are now more likely to demand value from a premium product, and airlines will have to adapt their strategy for attracting business passengers in the light of changes in company travel policy.

Case Study: bmi short-haul Business Class

bmi discontinued its separate Business Class cabin on most short-haul routes in August 2005, keeping it on key short-haul routes from Heathrow to Belfast City, Brussels, Dublin, Edinburgh and Glasgow.[1] From January 2010 bmi removed it on these routes also.[2] In its place is a single cabin which includes a flexible economy product.

The new flexible economy product (booking classes C, D, J and Y) includes fully flexible tickets, advance seat selection, access to executive lounges, and free food and drink in-flight. It also guarantees passengers a seat at the front of the aircraft, but with no curtain separating economy and flexible economy passengers, this product does not attract the higher rate of Air Passenger Duty that the previous Business Class did. bmi says it is has made the decision "to meet changes in our customers needs; with many corporate customers currently no longer being able to afford to fly in Business Class, this new product will mean customers can receive preferential treatment at an affordable price."

All passengers travelling in standard Economy on Heathrow short-haul routes are charged for food and drink, including frequent flyers in standard Economy for whom food and drink was previously complimentary.

bmi remains committed to a separate Business Class on its medium-haul routes, and also offers it on short-haul routes where operating in conjunction with another Star Alliance airline, such as London–Berlin and –Vienna.

Source: bmi drops remaining short-haul business class cabins*, Business Traveller (18 January 2010), and bmi press releases.*

1 Also Heathrow–Jersey introduced in 2007 but discontinued in 2009.

2 *bmi discontinued the Brussels service altogether.*

311. It has been suggested that a decade ago, corporate travel policies requiring travel on 'preferred' airlines acted as a shield against business passengers 'defecting' to no-frills airlines, whereas, today, stricter travel policies are actually preventing travel in short-haul Business Class. A general drop in demand in the recession may also have meant that cheaper economy fares were still available for late-booking business passengers, making the effective fare premium for Business Class that much greater and more difficult for a business passenger to justify. *Cabin sickness*, Airline Business (May 2010).
312. Although the effects are largely positive for business passengers, it should be recognised that there are cases where an existing direct service from a regional airport has been displaced by a no-frills service with lower frequency or less convenient timings, because the no-frills airline operates a larger aircraft type and schedules that maximise aircraft utilisation.

6.103 The short-haul product for business passengers on both network and no-frills airlines seems likely to continue to adapt. BA's Chief Executive acknowledges that Europe is seeing a structural decline in short-haul business traffic, and that such traffic is moving from Business to Economy Class, but says that there is no evidence of it moving to no-frills airlines. He says that there remains a case for short-haul Business Class and that increasingly a critical issue will be customer service and the value proposition to customers.[313] The analysis of BA and easyJet traffic between 2007 and 2009 in Chapter 2 (paragraph 2.36) suggests that both airlines have experienced a similar dilution of their short-haul business traffic mix during the downturn (if new routes added by easyJet since 2007 are excluded), but that in terms of absolute numbers, BA has lost proportionately more short-haul business passengers over this period than easyJet. However, the greater decline cannot necessarily be attributed to BA passengers switching to easyJet.

6.104 Air France's Chief Executive has been quoted as saying that the airline is not evolving towards a low-cost service concept on its medium- and short-haul network, but that "passengers are moving toward the low-cost. We will continue to offer a classic service, though with certain adaptations. We do not intend to remove the front of the cabin [Business Class]. There are still passengers that wish more comfort." However, during 2010 it did move from three classes on short-haul services to two,[314] while Air France-KLM subsidiary CityJet, which is a major operator of business routes at London City, has replaced its Business Class with a Premium Economy product, offering some frills but removing the curtain divider and guaranteeing an empty middle seat of the three seats either side of the aisle. Other examples are Aer Lingus, which transitioned to more of a no-frills model on short haul and exited the oneworld alliance in 2007; Iberia, which has suggested relaunching its short-haul operations with a new subsidiary, but not as a low-cost operator;[315] and Lufthansa, which is reportedly following Austrian Airlines by increasing the number of seats on its short-haul fleet without degrading legroom by using a new seat. Lufthansa is also upgrading its in-flight catering (in contrast to the downgrading seen on other network airlines).[316]

6.105 BA has continued to expand its network at London City, which it sees as an important feature of its business in London and complementary to Heathrow.[317] This has allowed it to maintain and develop its short-haul network without using valuable slots at Heathrow, which it can then use for long-haul growth. BA's services from London City include major European business destinations, some at relatively high frequency.[318]

313. ATW Online (4 May 2010) http://atwonline.com/airline-finance-data/news/walsh-blasts-eu-authorities-airspace-closures-0503. *Cabin sickness*, Airline Business (May 2010).
314. Air France Chief Executive reported in ATW Online (24 September 2009). http://atwonline.com/airline-financedata/news/af-klm-targets-april-2010-breakeven-0309. Air France is planning to restructure its point-to-point operations at French regional airports, offering a standard short-haul product but increasing aircraft utilisation in a clear reaction to the expansion of no-frills airlines. www.flightglobal.com/articles/2010/11/19/349976/air-france-to-create-provincial-bases-in-network-overhaul.html.
315. www.guardian.co.uk/business/2009/oct/22/iberia-european-revamp.
316. www.businesstraveller.com/news/lufthansa-set-to-revamp-european-product; www.businesstraveller.com/news/new-short-and-medium-haul-economy-class-seat-fo.
317. BA Q2 2010 Earnings Presentation phx.corporate-ir.net/External.File?item=UGFyZW50SUQ9Njg0MDR8Q2hpbGRJRD0tMXxUeXBlPTM=&t=1
318. For example (January 2011 typical weekdaily frequencies in brackets): Edinburgh (seven, rising to eight), Glasgow (four, rising to five), Amsterdam (four, rising to six), Barcelona (one), Copenhagen (two), Frankfurt (three), Madrid (two), Stockholm (two), Zurich (four). Source: Worldspan GDS, www.londoncityairport.com/AboutUs/ViewRelease.aspx?id=1250 .

Unbundling

6.106 Prior to the entry of no-frills airlines, it was generally accepted that air travel came 'bundled' with no extra charges for baggage, meals, etc. Uniform IATA fares included unlimited international routing permutations within a maximum mileage. As price competition evolved, airlines developed a range of fares outside the IATA system. Cheaper fares were introduced but these had restrictions on choice of flight, reservation changes, refunds, minimum/maximum stay, and/or advance purchase, so passengers requiring flexibility paid extra.

6.107 No-frills airlines took the principle of unbundling a step further. Although the degree of unbundling varies between airlines, the principle is to reduce the base fare to a minimum, and to have a menu of value-added ancillary items that can be purchased for an extra charge and which airlines would once have bundled with the fare. This strategy also allows airlines wanting to differentiate their product from competitors to add optional frills, not just for business passengers but anyone requiring additional comfort, facilities or flexibility. These might include at-airport (rather than on-line) check-in, credit-card payment, no weight limit on hand luggage, hold baggage,[319] points in a frequent-flyer programme, business lounge access, switching to earlier or later flights, priority boarding, advance seat allocation, extra leg-room seat rows, and in-flight entertainment or catering.

6.108 Thus, for example, a business passenger seeing value in priority boarding or a particular seat row may be able to opt to pay for those services, but may make a saving where travelling without hold baggage (and, it could be argued, is therefore not covering the costs of passengers that do want to take hold baggage). This makes unbundling attractive to corporate procurement departments whose focus is on price and not paying for unwanted extras. From the airline's perspective, unbundling allows it to reduce its base 'headline' fares to appear more competitive. It also brings a cost saving by incentivising against the carriage and handling of unnecessary baggage, catering, etc.

6.109 The concept has become widespread among no-frills airlines and a significant source of airline revenue. To a more limited extent, it has spread to some network airlines. The biggest impact has been on short-haul routes and the Economy cabin (fares in premium classes tend to remain bundled), but it has resulted in significant changes in the way network airlines manage seat assignments and hold baggage allowances. Some airlines incorporate the extras (or offer them for an annual charge) for frequent flyers or as part of corporate deals.

6.110 However, unbundling does currently create problems for company travel managers and travel management companies (TMCs). It makes it more difficult for them to benchmark and compare fares and track travel spend because the degree of unbundling varies between airlines. Extra services like seat assignment or hold baggage have not been bookable through the Global Distribution Systems (GDSs) used by TMCs. They have therefore required additional processes to book them through the airline's website or call centre, including a second invoice and separate accounting through the TMC data management processes, adding to transaction costs. Thus some of the value of booking through the GDS – the ability to track bookings, produce reports, etc – has been lost. At the time of writing, GDS technology has just caught up and should now be able to handle the booking of ancillary items.[320]

319. Although there have always been charges for baggage in excess of a free allowance.

320. *Airlines and ATPCO agree on step to create better fee comparisons*, Aviation Daily (4 November 2009); www.atpco.net/atpco/products/sfees_dc.shtml#optional; *Infrastructure in place to display ancillary services in an estimated 90% of travel sales channels*, ATPCO press release, www.atpco.net/atpco/media/pr12oct10.shtml.

Pricing developments

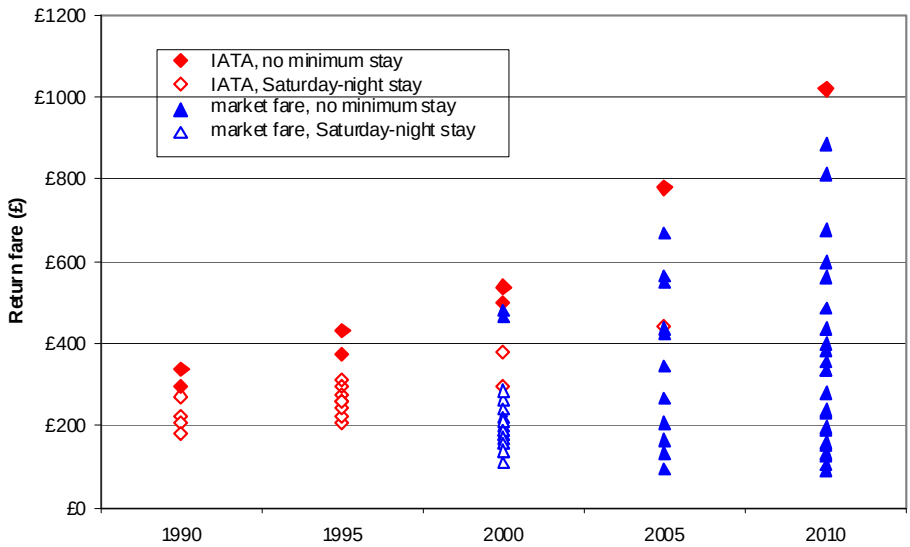
6.111 In the last 15 years there have been significant developments in pricing on European routes, largely driven by the entry of no-frills airlines and the more intense competition that resulted. The CAA published three reports analysing developments in the first five years following the liberalisation of the EU market in 1993.[321] The most recent report in 1998 noted that fully flexible fares discussed at IATA conferences had continued to rise in the five years after liberalisation, most clearly on routes operated by only one or two national carriers, and that on many such routes the full Business Class fare was the only fare available to passengers wanting a flexible product. In the context of the UK market, it also noted that price competition had become established on routes from Heathrow to other EU cities where British Midland (now bmi) had entered as a third carrier with Business Class fares lower than IATA fares, a process which had begun some years earlier.[322] Even as early as 1998, the report also noted that the spread of no-frills airlines was one of the most striking post-liberalisation developments in airline competition.

6.112 The last part of this chapter gives a summary of how pricing structures have developed on short-haul routes, how the network airlines' pricing model differed from that introduced by no-frills airlines, and how it has subsequently been adapted.

Changes in network airlines' short-haul fare structures

6.113 Figure 6-11 illustrates how BA's short-haul fare structure has changed since the EU market was liberalised. The route shown, London–Milan, is broadly representative of other routes, although the sequence of changes differs slightly between routes depending on competitive effects during the 1990s, in particular routes where bmi had entered.

Figure 6-11 BA return fares London–Milan, 1990–2010



Source: Airline Tariff Publishing Company, CAA records.

Notes: The chart shows published fares for the city-pair and are not adjusted for inflation. They include UK Passenger Service Charge and fuel/insurance/security charges, but exclude government taxes.

321. CAP 623 Airline Competition in the Single European Market (November 1993); CAP 654 The Single European Aviation Market: Progress So Far (September 1995); CAP 685 The Single European Aviation Market: The First Five Years (June 1998). These publications are available in printed form only. www.caa.co.uk/default.aspx?catid=5&pagetype=90&pageid=2748

322. Although the report showed that even the innovative Business Class fares introduced by British Midland bore some relation to fares discussed at IATA conferences, in which it was a participant.

6.114 Figure 6-11 shows that, in 1990 and 1995, all BA fares were set following discussion with other IATA airlines. Consequently, there was virtually no price competition. At the upper end of the range was a flexible Business Class fare, and a Eurobudget fare in Economy Class, which had some penalties for rebooking. There were two lower conditioned fare types, with different levels according to whether travel was low or high season or midweek or weekend. The conditions of these fares included penalties for cancellation or rebooking, but most significantly required a minimum stay of a Saturday night, making them less attractive to business passengers. Hence the lowest fare available for a day trip or midweek overnight stay was Eurobudget, at just under £300 round trip in 1990.

6.115 The chart shows that, by 2000, BA had introduced a wider range of fares outside the IATA process and therefore confined to BA services only, including slightly lower Business Class and Eurobudget fares. Although such fares were initially confined to specific routes during the 1990s, in December 2000 BA restructured its higher fares on all European routes so as to introduce a flexible fare in both the Business and Economy Class cabins, confined to BA services only.[323]

6.116 The lowest fares in the 2000 structure represented a significant reduction on 1995 fares, even taking into account the introduction of Air Passenger Duty in 1994 (which is excluded from the chart). These fares still required a Saturday-night stay.

6.117 The most significant change from the UK business passenger's perspective occurred in 2002, when BA (and bmi) removed the Saturday-night minimum stay from most European fares. At a stroke this made the full range of cheaper fares available to business travellers who were prepared to accept the other fare conditions (such as reduced choice of flights, booking early, and penalties for changes) but whose travel plans could not include a Saturday-night stay. BA (and bmi) also mirrored the conditioned fares in Economy Class with similar fares at a suitable premium in Business Class. They also allowed greater flexibility in combining different fare types on the outward and inbound sectors, potentially allowing more attractive fares to be offered. bmi also made these cheaper fares available on a one-way basis, allowing travel to be on different airlines for the outward and return legs, and BA followed suit in subsequent years.

6.118 BA acknowledged that the changed strategy – including cost reductions, fare restructuring, increasing load factors and aircraft utilisation, and encouraging internet sales – was to build a more efficient and robust airline, including competing more effectively with no-frills airlines.[324]

6.119 Figure 6.11 shows that between 2000 and 2010, the price range continued to widen, with the lowest fare less than half the lowest fare in 1995 (albeit that the availability of cheaper fares would have been confined to early bookings or off-peak flights) and flexible fares continuing to rise. This pattern is similar to that which occurred in the US domestic market following deregulation in the late 1970s. Flexible fares did not generally fall, but instead barriers such as the Saturday-night stay requirement were removed, and a wider range of fare types evolved, allowing US domestic passengers that would previously have bought flexible fares to buy cheaper, albeit more restricted, fare types.[325]

323. IATA fares remained in place for itineraries involving travel on another airline. The level of IATA fares is now set by reference to fares prevailing in the market and not through discussion between airlines, following the withdrawal of the exemption from competition law.
324. Following BA's *Future Size and Shape* review of its business, unveiled in 2002 (BA Press Release 13 February 2002). It should not be forgotten that BA set up its own no-frills airline, Go, in 1998; following a management buyout in 2001 the airline was acquired by easyJet in 2002.
325. See, for example, Holloway S.: *Straight and Level: practical airline economics* (page 148) (2008). In specific cases this could depend on the extent of competition on the route, and whether a no-frills carrier was operating.

Table 6-10 Business Class flexible fares on top eight business routes

Route Heathrow to:	Airline	Return fare in GBP November 1995 flexible	lowest without Sat. night stay	lowest*	November 2010 flexible
Dublin	bmi	292	190 **	65	464 ***
Amsterdam	BA	290	214	88	594
Paris	BA	336	205	59	663
Frankfurt	BA	386	280	110	774
Brussels	BA	322	225	59	659
Copenhagen	BA	452	378	160	870
Milan	BA	432	372	133	891
Geneva	BA	378	342	129	771

Source: Airline Tariff Publishing Company, CAA records.

*Notes: * Lowest published fare for any flight or travel date which may have many restrictions.*

*** Fare of GBP112 available for a three-night minimum stay.*

**** Flexible economy fare (bmi no longer offers Business Class on the route).*

Fares are published fares only and not adjusted for inflation.

Fares include UK Passenger Service Charge and fuel/insurance/security charges (which were not levied separately in 1995), but exclude government taxes.

6.120 Table 6-10 shows that Business Class flexible fares in the eight biggest short-haul business markets have risen significantly (faster than general inflation[326]) since 1995 when no-frills airlines were just emerging. The CAA published a report on no-frills airlines in 2006, which concluded that average fares paid by business passengers on EU routes had fallen significantly faster than those paid for leisure travel.[327] Given that in 1995 few business passengers would have been able to accept a Saturday-night stay, it could be concluded from Table 6-10 that the fall in average fare stems from business passengers being more likely to travel at conditioned fares than fully flexible fares. This accords with the assertions earlier that business passengers are much more likely to take advantage of the potential savings from buying 'best fare on the day', even if this means accepting penalties for rebooking.

No-frills airlines' fare structures

6.121 Fares offered by the emerging no-frills airlines generally departed significantly from the conventional structure – which had its roots in the IATA system – offered by other airlines up until that point.[328]

6.122 easyJet's first services between Luton and Scotland (1995) and Luton and Amsterdam (1996) had the simplest structure, consisting of four fares with identical conditions (no changes or refunds, no discounts for children) sold on a one-way basis (for example £35 to £65 to Amsterdam). These fares were therefore innovative not just in terms of level but in being free of any minimum stay restriction and not requiring return travel on the same airline. Unlike conventional fare structures then

326. Although oil prices have risen faster than general inflation since 1995, CAA airline financial statistics show that UK airlines' unit costs per available seat kilometre remained roughly constant.
327. See Figure 4.12 of *CAP770 No-frills carriers: evolution or revolution?*, CAA (November 2006).The average fare has since stabilised, as illustrated earlier in Figure 2-4 of Chapter 2.
328. A detailed description of fare developments between 1992 and 1997 appears in *CAP 685 The Single European Aviation Market: The First Five Years* (June 1998), in particular Appendices I, J and K.

prevailing, only one fare would be on offer at any time for a given flight, and the price increased as the lower fares sold out, the fares not having the fixed advance purchase requirement that network airlines applied to some lower fares. By 1998 easyJet had expanded the number of price points to eight (£17.50 to £109) with the lowest only on offer for limited periods, and reservations could be changed for a fee. By 2003 a typical easyJet route had 15 price points.[329]

6.123 Ryanair had been in existence for some years before changing its business model to a no-frills approach. Consequently, unlike easyJet, in the mid 1990s it was selling commissionable fares through travel agents, its services were bookable through a GDS, and it retained recognisable elements of the traditional fare structure on its network of Ireland/UK routes. By 1995 it had discontinued its Business Class, removed some Saturday-night stay restrictions,[330] and was reportedly selling the bulk of seats at the lowest fare levels in the structure.[331] Ryanair's pricing subsequently became significantly more innovative and simplified as it embraced direct sales via the internet, and withdrew from travel agency sales and GDSs.[332] Other no-frills airlines such as Buzz, Debonair, Go and Virgin Express adopted pricing models which, with some variations,[333] had similarities to the easyJet-type model.

6.124 Today, the no-frills pricing model, based around internet sales, is well established. While the no-frills model is to charge higher prices on peak flights or as the departure date approaches, they will not generally hold seats back for late bookers.[334] This can be compared with the traditional approach of network airlines which fine-tune their inventory to maximise revenue so that, close to departure, the last few seats are available for high-yielding passengers travelling on relatively high flexible fares switching or making reservations at the last minute.

6.125 It is therefore an interesting development that easyJet, which has been increasingly focusing on the business market, decided to introduce a separate, flexible, fare alongside its existing pricing model, which it later withdrew and relaunched in November 2010 (see earlier case study).

6.126 The next chapter looks forward to some possible future trends in the UK business air travel market.

329. Source: Tariff filings with the CAA.
330. Source: Travel Trade Gazette (23 February 1994).
331. Although as late as 1999 a typical Ryanair fare structure had a range of higher fares with different conditions, including a fully flexible fare, some with a minimum stay (of two nights or a Saturday night). Source: Tariff filings with the CAA.
332. The first GDS from which Ryanair withdrew was Galileo in 2000. Source: Ryanair press release (19 May 2000).
333. In particular by offering a flexible fare option and requiring a minimum stay on lower fares. Buzz, for example, started with such a fare structure in 2000, but switched to the easyJet-type model of one-way fares in 2001 (before being purchased by Ryanair in 2003). Source: Tariff filings with the CAA.
334. This reportedly leads some corporates, on heavily travelled routes, to book tickets speculatively on no-frills airlines, which are then discarded if unused (as they are non-refundable).

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Part 2 Chapter 7 Future trends in UK business air travel

Chapter summary

- The longer term outlook for business air travel is still expected to be strongly related to economic growth and trade. Globalisation and economic integration facilitates the growth of trade in goods and services, fuelling the demand for business travel. Like other advanced economies, the UK economy has undergone a long-term structural change from manufacturing towards services. The rapid economic growth of certain countries[335] is expected to become an increasingly important driver for UK business air travel. Other sectors of UK demand for business travel may be slower to recover from recession.
- Improved international communications is likely to encourage globalisation and, therefore, business travel – by making long-distance communication easier, business networks become more widespread and new travel opportunities arise. However, improved communications may also allow businesses to reduce their travel budgets. Indications to date suggest that companies are loathe to replace face-to-face meetings with external clients, but may seek to reduce travel for internal company business, a distinction which seems unlikely to change, despite advances in videoconferencing technology.
- Some technological advances may make dwell time in airports and aircraft more productive, and work to reduce some of the disadvantages of business travel. New developments in hand-held mobile devices, social media networking and connectivity to communications networks may enhance flexibility for, and productivity of, business travellers.
- Improved access to rail bookings, national government policy on public sector travel and expansion of high-speed networks are likely to increase competition from rail in the short-haul corporate travel market. However, since travel time is a main driver of modal choice for the business traveller, significant diversion from air to high-speed rail is only likely on the shortest air routes.
- Environmental concerns and an awareness of corporate social responsibilities may accentuate the effects noted above. However, where travel is client-focussed, it is likely to be considered a necessary business activity. Companies are therefore likely to focus mainly on mitigation of greenhouse gas emissions related to travel through activities such as offsetting, and through increased pressure on airlines to reduce such emissions where possible.

Introduction

7.1 Previous chapters considered how business air travel to and from the UK has developed and how airlines and travel management companies have tailored their offering up to and including the recent global recession. This chapter looks forward to some possible future trends in the UK business air travel market. It considers a

335. For example, the BRICs (Brazil, Russia, India and China) or the Next-11 (Bangladesh, Egypt, Indonesia, Iran, South Korea, Mexico, Nigeria, Pakistan, the Philippines, Turkey and Vietnam).

number of factors that may have an increasing influence on the post-recession business travel market: UK and global economic growth (particularly for some emerging economies), technological development, environmental concerns and alternative modes of travel.

7.2 While business travel will continue to grow fuelled by globalisation and financial integration, a number of uncertainties, such as growing concern about environmental issues and increased awareness of corporate social responsibilities, the rising price of oil and development of alternative non-travel technology (for example videoconferencing) may influence companies' travel policy and slow this trend.

7.3 However, some advances in information and communication technologies (ICT) such as hand-held mobile devices and in-flight Wi-Fi internet systems may encourage more rather than less business travel by making dwell time in airports and aircraft more productive while enabling travellers to remain connected at any part of their business trips.

7.4 Future business travellers, who feel more at ease with mobile technology, may demand higher levels of control, security and personalisation from their journey. The growing sophistication of ICT will facilitate a more personal travel experience from booking to baggage collection, with real-time information available about the journey when and where needed, streamlining the whole travel process.

7.5 The following sections consider in more detail the factors that may shape future demand for UK business air travel.

Globalisation and the changing world and UK economy

7.6 As the world recovers from the recent economic recession, global and UK business travel will continue to increase. However, prospects for future growth and the profile of UK business air travel will be shaped by the changing economic structure of the world and UK economy.

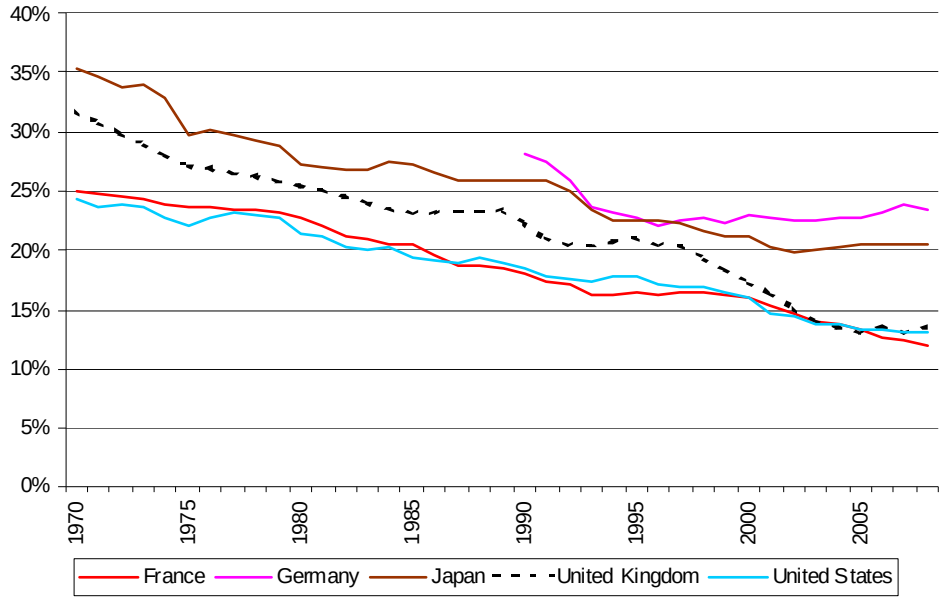
7.7 As explained in Chapter 3, the continuing process of globalisation and economic integration has facilitated the rapid growth of trade in goods and services, the flow of capital, people and ideas across borders, all fuelling the demand for business travel. This has been underpinned by the rapid development of ICT that has significantly reduced transport and communications costs and increased the tradability of many goods and services.

7.8 The rise of developing, low wage economies (such as China and India) and associated growth in global supply chains, whereby firms locate various parts of the production process in different countries according to relative cost advantage, has not only led to an increase in international trade in intermediate inputs but also contributed to a change in many advanced economies' structures.[336]

7.9 Manufacturing globally has experienced strong productivity growth, resulting in the price of manufactures falling relative to that of services sector outputs. The fall in the relative value and level of manufacturing output has led to a shift in the composition of both (current price) output and employment towards the services sector in many developed economies, including the UK. Figure 7-1 shows that manufacturing's share of total output declined after 1970 before levelling off in the last few years.

336. BERR: Globalisation and the changing UK economy (February 2008).

Figure 7-1 Manufacturing's share of total output, 1970–2008



Source: UNCTAD. Pre-1990 data for Germany are unavailable.

7.10 Table 7-1 shows the percentage share of UK national output (in GVA) by broad industry sector and highlights the decline of manufacturing and other non-service industries' output share from 33.7% in 1996 to 21.9% in 2009, a fall of almost 12 percentage points. This contrasts with the increasing significance of the financial and other business services sector with a rise of 10.8 percentage points in the share of national output over the same period.

Table 7-1 Output (GVA in £bil current prices) and percentage share per UK industry

Industry group	1996	% share	2008	% share	2009	% share	Ppt change 1996–2009
Services industries							
Financial intermediation (excl. FISIM[1])	18.3	2.7%	116.8	9.0%	111.9	9.1%	6.4%
Real estate, renting and business services	129.1	19.0%	303.2	23.4%	288.9	23.5%	4.4%
Wholesale and retail trade	79.3	11.7%	147.2	11.4%	141.6	11.5%	-0.2%
Health and social work	42.7	6.3%	93.8	7.2%	95.6	7.8%	1.5%
Transport, storage and communication	53.7	7.9%	91.3	7.1%	85.7	7.0%	-1.0%
Education	37.0	5.4%	76.5	5.9%	77.1	6.3%	0.8%
Public administration and defence	40.3	5.9%	65.1	5.0%	66.6	5.4%	-0.5%
Other social and personal services	30.0	4.4%	65.6	5.1%	60.6	4.9%	0.5%
Hotels and restaurants	20.3	3.0%	36.4	2.8%	34.6	2.8%	-0.2%
Total Services	*450.7*	*66.3%*	*995.8*	*76.9%*	*962.7*	*78.1%*	*11.8%*
Manufacturing & Non-Services industries							
Manufacturing	146.1	21.5%	150.3	11.6%	134.4	10.9%	-10.6%
Construction	34.6	5.1%	80.8	6.2%	71.9	5.8%	0.7%
Mining and quarrying	19.8	2.9%	37.7	2.9%	34.2	2.8%	-0.1%
Electricity, gas and water supply	16.3	2.4%	21.3	1.6%	19.5	1.6%	-0.8%
Agriculture, hunting, forestry and fishing	12.1	1.8%	9.7	0.7%	9.2	0.7%	-1.0%
Total manufacturing and production	*228.8*	*33.7%*	*299.8*	*23.1%*	*269.3*	*21.9%*	*-11.8%*

Source: ONS Blue Book 2004 and 2010.

Note: [1]FISIM = Financial intermediation services indirectly measured.

7.11 In 2008, the Department for Business, Enterprise and Regulatory Reform (BERR) noted[337] that the UK had been able to take advantage of technological developments and become a world-leading exporter for many services (particularly in financial, insurance, ICT and other knowledge-based business services)[338] which have become significant contributors to UK's overall export volumes in recent years (from 11.1% in 1996 to 26.2% in 2009), as shown in Table 7-2.

Table 7-2 Volume (in £bil) and percentage share of exports of goods and services by sector

Industry group	1996	% share	2008	% share	2009	% share	Ppt change in share 1996–2009
Services							
Financial	7.3	3.3%	52.8	12.5%	43.9	11.3%	8.1%
Insurance	2.7	1.2%	7.6	1.8%	8.3	2.2%	1.0%
Computer and information	1.1	0.5%	7.3	1.7%	6.9	1.8%	1.3%
Other business	13.7	6.1%	44.7	10.6%	42.2	10.9%	4.8%
Transportation	10.8	4.8%	20.9	4.9%	20.7	5.4%	0.5%
Travel	13.7	6.1%	19.6	4.6%	19.3	5.0%	-1.1%
Royalties and license fees	4.3	1.9%	8.0	1.9%	7.6	2.0%	0.1%
Communications	1.1	0.5%	4.3	1.0%	4.5	1.2%	0.7%
Government	1.3	0.6%	2.2	0.5%	2.1	0.5%	0.0%
Personal, cultural and recreational	0.8	0.3%	2.3	0.5%	2.0	0.5%	0.2%
Construction	0.2	0.1%	1.2	0.3%	1.6	0.4%	0.3%
Total Services Export	*56.8*	*25.3%*	*170.8*	*40.4%*	*159.1*	*41.2%*	*15.8%*
Total Goods Export	*167.2*	*74.7%*	*251.6*	*59.6%*	*227.5*	*58.8%*	*-15.8%*

Source: ONS Pink Book 2004 and 2010.

Shift to service industries and impact on business air travel

7.12 This long-term shift of UK output towards services has implications for the UK business travel market. There is some evidence to suggest that business travellers from finance-related sectors, such as investment banking, tend to have a higher propensity to travel than those from manufacturing industries.

7.13 Table 7-3 shows that, while banking and finance-related industries constituted only a small proportion of the UK's total work force (3.7%) in 2009, they provided the highest proportion of business trips per employee across all industries (column 'E' in Table 7-3).

7.14 More crucially, since these passengers also tend to have a higher propensity to travel in premium classes than business travellers from other industries (column 'D') and represented more than a quarter of the premium travellers in 2009, airlines are keen to capture them by competing on frequency, service quality, network connectivity and even personalised services.

7.15 Table 7-3 also shows that business travellers from the non-service industries of mining, quarrying, agriculture, forestry and fishing had similar propensities to travel (on a per employee basis and in premium classes) as those from the banking/finance industries. Given the routes being used by these passengers, it is likely that they represent managerial and technical experts. However, these industries were much less significant than the banking/finance sector in terms of the proportion of business travellers, the workforce and GVA.

337. BERR: *Globalisation and the changing UK economy* (February 2008).

338. Business services include a diverse range of activities, from the creative and technical, such as advertising, designs, legal services, accountancy, computing, information and communications, to industrial cleaning and call centres.

Table 7-3 Proportion of business travellers and propensity to travel per industry group in the UK in 2009

Industries	%Business passenger (A)	%Premium class (B)	%Work force (C)	%Premium class/ %Business passenger (D)	%Business passenger/ %Work force (E)
Banking/Finance/Insurance	14.2%	26.4%	3.7%	1.9	3.8
Health/Education/Public Services	17.6%	9.4%	41.5%	0.5	0.4
Transport & Communications	12.9%	12.2%	8.5%	0.9	1.5
Wholesale, Retail, Hotel & Catering	10.5%	7.4%	21.8%	0.7	0.5
Other Business	14.1%	12.2%	6.8%	0.9	2.1
Total Service Industries	*69.2%*	*67.7%*	*82%*	*1.0*	*0.8*
Manufacturing Industries	20.3%	19.4%	8.4%	1.0	2.4
Mining/Quarrying/Agriculture/Forestry	5.0%	8.9%	1.5%	1.8	3.5
Construction	3.2%	1.8%	7.0%	0.6	0.5
Energy & Water Supply Industries	2.4%	2.3%	0.8%	0.9	3.0
Manufacturing & Other Non-Service Industries	*30.8%*	*32.3%*	*18%*	*1.0*	*1.7*

Source: CAA Passenger Survey, 2006–2009 and ONS Labour Market Statistics, October 2010.

7.16 As Table 7-2 indicates, the UK banking/financial sector grew more rapidly than the economy overall between 1996 and 2009. Indeed, the profits of financial intermediaries reached 15% of the whole economy's profits in 2008, up from 1.5% in the 1970s. This growth spurt of financial activities (and profits) has been one of the main drivers for business travel from this sector, especially for travel in premium classes.

7.17 However, the financial sector's prospects in the post-recession era remain uncertain, with new rules governing capital requirements for financial institutions involved with trading, derivative and securitization activities,[339] and a recent study[340] cast doubts on prospects of a return to previous financial sector returns on equity. This could have a negative impact on the prospects for business (particularly premium) travel from this sector, which has been a major revenue and profit generator for many airlines, particularly on routes connecting London with the major global financial centres like New York, Hong Kong and Shanghai.

The rise of BRICs and other emerging markets

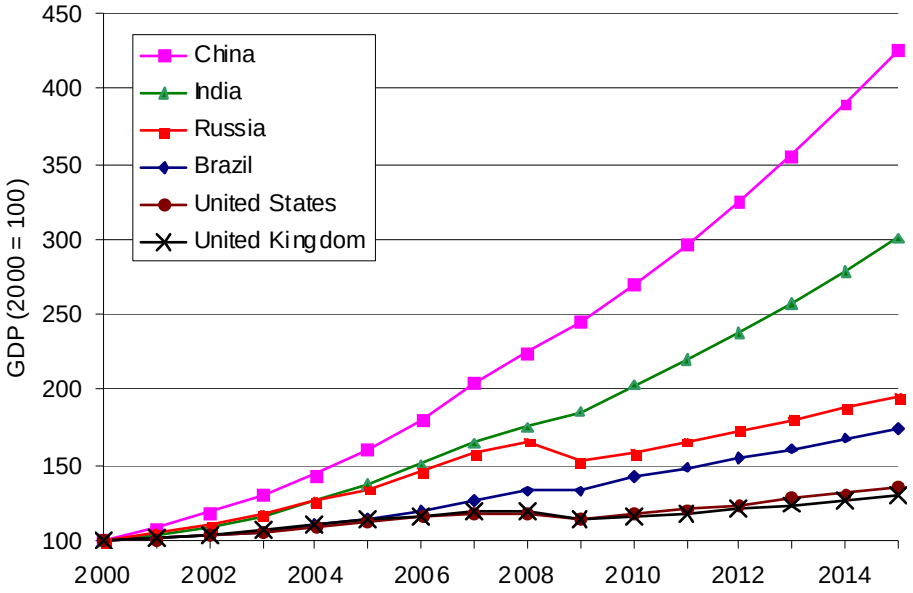
7.18 An important trend arising from the continuing process of globalisation is the growing importance of BRICs compared with G7[341] countries in the global economy. Between 2000 and 2008, the BRICs contributed almost 30% to global economic growth (in US dollar terms) compared with 16% in the previous decade.[342]

339. Agreed by the Basel Committee on Banking Standards in September 2010. These rules aim to rein in the high level of risk-taking and credit expansion by the financial sector that caused the latest global financial crisis.
340. By Andrew Haldane and others at the Bank of England. See Adair Turner and others: *The Future of Finance:The LSE Report*, London School of Economics and Political Science (2010).
341. The BRIC countries (Brazil, Russia, India and China) were named in 2003 by Goldman Sachs as the economies with the greatest development potential to 2050 on the basis of positive economic fundamentals, large and growing populations, and the ability to exploit resource assets, such as oil. G7 (Great Seven) refers to the US, UK, France, Germany, Italy, Japan and Canada.
342. In contrast, the contribution from G7 countries fell from more than 70% in the 1990s to around 40% during the 2000s.

7.19 In 2009, BRICs collectively reached 16% of global GDP and, as a group, could surpass the US by the end of this decade and become as big as the G7 by 2032 according to projections by Goldman Sachs.[343] Much of the growth in international business travel in the future will therefore be influenced by these countries' economies.

7.20 While advanced economies have lagged in the recovery from the economic crisis, the BRIC and the 'Next-11'[344] emerging economies are expected to remain the main engine of global growth for the foreseeable future as their resilience to the global economic downturn has demonstrated.[345] Figure 7-2 below shows the economic outlook, according to the IMF, for the BRIC countries up to 2015 compared with the US and the UK.

Figure 7-2 GDP outlook of BRICs, the US and the UK



Source: IMF World Economic Outlook, October 2010.

7.21 The rapid growth of these emerging economies has implications for the future demand for UK business air travel. IATA has continued to report strong premium traffic growth on routes linked to Asian markets as trade activities within and without these regions continue to boost business travel to and from these economies.[346]

7.22 Although Europe and the US remain the most important trade partners and markets for UK exporters, accounting for around 50% and 14% respectively of total trade with the UK in 2009, the percentage share of total trade with the BRICs increased by almost five percentage points to 7.4% between 1996 and 2009 while business traffic between UK and the BRICs rose by 80% over the same period. This compared with a corresponding reduction of five percentage points in trade share and an increase of 21% in business passengers between Europe/US and the UK over the same period. Although the strong growth in trade and business passengers with BRICs was from a relatively low base, business traffic on these longer haul flights tend to attract a higher proportion of premium travellers than flights to and from shorter haul destinations.

343. Goldman Sachs: *Is this the 'BRICs Decade'?*, BRICs Monthly, Issue No. 10/03 (May 2010); Goldman Sachs: *The long-term outlook for the BRICs and Next-11 post crisis*, Global Economics Paper No. 192 (December 2009).
344. In 2005, Goldman Sachs suggested BRIC successors, known as the Next-11, as comprising Bangladesh, Egypt, Indonesia, Iran, South Korea, Mexico, Nigeria, Pakistan, the Philippines, Turkey and Vietnam.
345. Apart from Russia, Iran, Mexico and Pakistan which are still experiencing sluggish recovery at the time of writing.
346. IATA: *Premium Traffic Monitor* (August 2010).

7.23 More importantly, given the sheer size of their populations, rising incomes in the BRICs and other emerging economies is expected to create a massive new middle class that will increase consumer demand for imports of high value added goods and services (such as pharmaceutical products, financial and other knowledge-based services). While the UK continues to have a comparative advantage in the provision of such services, it will benefit from the associated economic growth and consequent growth in business air travel.

Effect of public sector spending cuts on future business travel

7.24 Table 4-5 showed that for many UK airports, public sector employees made up 5%–10% of all business travellers, and, combined with those from the health and education sectors, often constituted 15%–25% (with the London airports typically at the lower end of the range).

7.25 The UK coalition Government has announced plans to cut public spending by more than £80 billion by 2015 which, according to the Office for Budget Responsibility, could lead to a reduction in up to 330,000 public sector employees.[347] The increase in VAT to 20% from January 2011 and the announced budget cuts have led the Office for Budget Responsibility to downgrade its latest UK GDP forecasts for 2011 and 2012 by 0.2 percentage points each to 2.1% and 2.6% respectively. The impact of the Government's fiscal consolidation will likely have a direct dampening effect on business air travel demand from the public sector and an indirect impact on demand from the private sector.

Information and communication technology (ICT) development

7.26 Technological advance has been an important driving force in the evolution of travel supply, demand and management in the past decade. Improved international communications, whether via telephone, email or the internet has, in the past, done at least as much to increase the pace of globalisation and the demand for business travel as it has to suppress the need to travel to meet clients or colleagues.

7.27 During the recent global economic recession, airlines and travel buyers have been forced to find ways to reduce costs and increase productivity. For example, certain business trips for in-house meetings, training and continuing education have been replaced by web-based technologies (such as 'webinars' and videoconferencing) as travel buyers are increasingly turning their attention to emerging technologies for cost-effective solutions.

7.28 According to the National Business Travel Association, almost a quarter of companies responding to the American Express Business Travel 2010 survey replaced business air trips with some kind of virtual-meeting technology in 2009. As technology improves and telepresence systems become less expensive, such alternative non-travel solutions will become more palatable.

7.29 However, improved ICT will also increase the pace of globalisation and the demand for business travel. For example, new virtual-meeting technology could help companies acquire customers from a wider geographic area and allow development of a larger customer base than before, opening up more opportunities for business travel.

7.30 In addition, advances in new mobile technology such as smartphones that enhance the flexibility and productivity of travellers while on the move would reduce some of the disadvantages of business travel.

347. Office for Budget Responsibility: *Economic and Fiscal Outlook* (November 2010).

Videoconferencing

7.31 Research over the past two decades has, for the most part, found only a modest substitution effect between business air travel and videoconferencing (VC).[348]

7.32 Most survey results indicate that ICTs such as VC are likely to be used as a substitute for business trips involving internal meetings and meetings with well-established partners. However, face-to-face meetings are still preferred for contexts such as business development discussions or marketing sales and demonstrations.[349] Other research[350] has suggested that ICT development is only a supplement to face-to-face meetings and could even induce additional travel, as technology can enhance interactions and relationship building, leading to a greater customer base and an increased volume of business travel.

7.33 Most stakeholders interviewed by the CAA for this study have expressed the view that VC is expected to grow over time, but that it will largely remain supplementary to face-to-face meetings. There is no strong evidence to date to suggest that this view is likely to change in the near future. However, further increase in the up-take of VC will obviously depend on technological advance and ease of access (for example, the associated installation and operating costs involved, the ability to rent equipment and compatibility of different solutions), while increasing concerns about the environmental impacts of air travel may also encourage corporates to turn to non-travel solutions for internal company business as opposed to meetings with external clients.[351]

Mobile technology

7.34 In recent years, more business travellers have been using mobile devices to stay connected when away from the office.

7.35 While airlines have always tried to appeal to business travellers by allowing them to use time at the airport and in flight for work purposes (for example through the availability of business lounges), mobile technologies are increasingly making such practices accessible to non-premium business travellers.[352] In combination with other trends in the office, such as more flexible working hours, this may continue to counter some of the negative effects of increased security and congestion at airports lengthening overall travel times for business passengers.

7.36 Mobile technology can also enable TMCs to communicate more effectively with their clients at every stage of the travel process, provide the latest available travel information and also help corporates track the movement and safety of their employees in case of an adverse event such as a terror attack or disruption by a natural disaster.

348. See Denstadli, J.: *Impacts of videoconferencing on business travel:the Norwegian experience*, Journal of Air Transport Management 10, 371–376 (2004) – which finds that VC replaced 2.5%–3.5% of domestic business air travel in Norway between 1998 and 2003; Roy and Filiatrault: *The impact of new business practices and information technologies on business air travel demand*, Journal of Air Transport Management 4, 109–118 (1998) – which predicts 1.8% of business air travel in Canada would be replaced in the long term. Mason, K.: *Project Icarus – Final Report*, Business Travel Research Centre, Cranfield University (2008).
349. For example, Mason, K.: *Future trends in business travel decision making*, Journal of Air Transportation, Vol. 7, No.1 (2002); Harvard Business Review: *Managing across distance in today's economic climate: the value of face-to-face communication* (2009).
350. For example, Saffo, P.: *The future of travel*, Fortune Autumn, 112–119 (1993); Salomon, I.: *Telecommunication and travel relationships: a review*, Transportation Research 22A, 283–289 (1998).
351. There is large uncertainty over the scope for substitution of VC for business travel. The Committee on Climate Change (CCC) in a 2009 report cited a range from very limited substitution effect to a reduction of 30% in business demand in 2050. CCC: *Meeting the UK aviation target – options for reducing emissions to 2050* (December 2009).
352. For example, Air France and KLM have launched mobile websites which allow users to check themselves in, book seats with extra legroom, buy more baggage allowance, cancel or change their bookings up to latest check-in time and receive a boarding pass by text or email.

7.37 Over the last few years, an increasing number of corporate travellers have used internet-enabled hand-held mobile devices such as Blackberry or iPhone for policy compliance, pre-trip approval, travel booking and expenses reporting according to some TMCs.

7.38 As the capabilities of mobile technologies increase, and business travellers become ever more comfortable with working outside the traditional office environment, the demand for business travel will be affected both by the benefit of being more in touch while travelling, and the challenges of improved alternatives to travel.

Role of social media in corporate travel

7.39 Social media, unlike the other topics addressed in this chapter, is unlikely to directly affect the future level of demand for business travel. Rather, it may affect the experience of business air travel and the way it is marketed and purchased.

7.40 Unlike traditional media (such as newspapers and television) or websites of travel companies and airlines, social media uses web-based technologies to turn communication into interactive dialogues,[353] enabling users to interact or collaborate with each other as creators of user-generated content in a virtual community – as opposed to websites where users are limited to the passive viewing of content that was created for them.

7.41 Social networking in a corporate context has become more popular over the last two years and the development of social media has provided a new platform for airlines, TMCs and travellers to interact with each other and influence the booking behaviour of business and corporate travellers.[354]

7.42 The Spring 2010 survey by American Express Business Travel[355] found that 50% overall and 59% of surveyed mid-sized companies use social media to support travel management while 42% use social networking to find travellers' preferred suppliers and services.[356] Among those using social media, 41% of them monitor social media sites to ensure corporate travel policy while 45% actively engage with a public community. Thus, social media has not only been used by companies and travel buyers to engage and communicate with their travellers, but also to enhance business functions and contribute to cost controls.

7.43 With increased popularity among travellers who use traveller review sites and social networks to help them make more informed purchase decisions, social media sites such as Facebook, Twitter, LinkedIn and Plaxo[357] have become increasingly important for airlines and travel companies to monitor and measure brand perception, and respond on a real-time basis to manage their brand reputation and influence customers' purchase behaviour.[358]

353. Social media can take many different forms, including internet forums, weblogs, social blogs, microblogging, wikis, podcasts, picture or video-sharing, rating and social bookmarking.
354. Airlines and TMCs have also used social media to distribute real-time information to and engage with their customers during recent incidents of terrorist attacks (such as the failed Christmas Day 2009 terrorist attack on a Delta Air Lines flight) and natural disaster (the Icelandic volcanic eruption in April 2010).
355. American Express Business Travel: *Social Media in Business Travel Management*, (22 June 2010).
356. Caution needs to be taken in interpreting these results as the small sample survey was based on less than 100 respondents who are actively involved in corporate travel management. Nevertheless, another survey in June 2010 by AirPlus International also showed a significant increase in the usage of social network platforms by corporate travel professionals and travellers compared with a year ago. AirPlus International: *Social Media Making Inroads for Managing Travel*, The Wire….from AirPlus (June 2010).
357. Popular consumer social networking sites include Facebook, Twitter, MySpace, Flickr and YouTube while sites such as LinkedIn, Spoke, Plaxo, TripIt and Yammer are more business-oriented.
358. According to BA's head of UK and Ireland sales and marketing, BA now spends at least half of its marketing budget on social media which is used as a means to engage with its customers, get feedback from them and improve BA's product and customer loyalty. Source: www.travelmole.com/stories/1144749.php?news_cat=&pagename=searchresult

7.44 While social media has become an integral part of the communication and marketing strategies of many airlines, TMCs and travel buyers, it is also increasingly being used by business travellers at every stage of their travel processes, from choosing the airline and making the reservation to finding out where to eat or where to stay.[359] Thus, in the future, social media may become an important communications channel and information-sharing platform for business and corporate travellers affecting both their booking behaviour and the way travel buyers manage their corporate travel.

Competition with high-speed rail

7.45 Demand for corporate rail travel has increased significantly in the last few years. Surveys of TMCs conducted by the Guild of Travel Management Companies (GTMC) show that although business travel fell in 2008 and 2009, and corporate use of air and car travel with it, corporate rail travel continues to show significant growth (see Figure 5-1).

7.46 High-speed rail services are increasingly common in Europe, and, while the UK's only line currently connects London to the Channel Tunnel, a high-speed line north of London has been proposed, initially to Birmingham and then on to Manchester and Leeds. In Europe, there are plans to expand the provision of high-speed rail lines over the next 20 years, particularly in France, Germany and Spain.

7.47 For shorter journeys, high-speed rail can be particularly attractive for business passengers, who are more likely to be travelling between city centres, and for whom travel time (and the ability to work while travelling) may be at least as important as price. However, rail is only likely to be preferable to the business passenger where travel times are comparable to air. Even with expanded high-speed services in the future, this is only likely to apply to routes between London and mainland UK destinations or between Southern England and near Europe.

7.48 For example, High Speed 2, the company set up by the Government to investigate the options for future UK high-speed rail, reported[360] that a high-speed line between London and Birmingham would reduce travel times between these cities and to onward destinations by more than 30 minutes. In addition, extending high-speed rail services further north could mean journey times of around 1hour 20minutes between London and Manchester or Leeds, and around 2hours 40minutes between London and Glasgow or Edinburgh.

7.49 German train operator Deutsche Bahn intends to run direct high-speed services from London to a variety of European destinations,[361] with regular services beginning in 2013. However, its plans, which all include stops at Brussels where the train will divide, will entail London to Frankfurt journey times of just over five hours. Table 7-4 compares the proposed times and frequencies of these services with existing air services.

359. For example, a new 'Facebook-based' social media application for Rail Europe, called Travel Comparator, allows travellers to compare travel times via air, train or car between European cities, book fares, communicate with Rail Europe representatives and share travel-related information with other users. Source: www.eyefortravel.com/news/marketing/new-social-media-application-raise-awareness-european-rail-travel
360. High Speed Two Ltd: *High Speed Rail: London to the West Midlands and Beyond, A Report to Government* (March 2010).
361. www.deutschebahn.com press release 081-2010.

Table 7-4 Comparison of proposed high-speed rail and existing air services to selected destinations

Route	Proposed high-speed rail		Existing air		Business passengers 2009 (air)
	Time	Frequency	Time	Frequency	
London–Manchester	1hr 20m	> 50 / day	1hr	19 / day	0.5m
London–Edinburgh	2hrs 40m	> 35 / day	1hr 25m	46 / day	1.4m
London–Amsterdam	4 hrs	3 / day	2hrs 15m	46 / day	1.1m
London–Cologne	4 hrs	3 / day	2hrs 20m	8 / day	0.2m
London–Frankfurt	5 hrs	3 / day	2hrs 30m	26 / day	0.7m

Source: CAA Passenger Survey, 2008–2009, OAG September 2010, HS2 report to Government and Deutsche Bahn press release.

Notes: All journey times between station/airport pairs only. Air frequencies as at 15 September 2010.

7.50 It is not straightforward to predict how many business passengers would use high-speed rail services rather than air. While frequency and speed of services are important, other factors, such as total journey time (which could depend on how conveniently located stations and airports are for the trip, and the speed with which travellers can pass through them) and scheduled departure or arrival times may be just as significant. Even so, in the context of more than 50 million total business passengers using UK airports, the table indicates that future competition from high-speed rail is only likely to be relevant to a small proportion of business journeys by air.

7.51 On the other hand, the appeal of rail to business travellers has been enhanced by the recent development of online booking engines such as thetrainline.com and Evolvi which have simplified bookings for TMCs and their corporate clients. The ability to access the whole of the UK rail inventory via the GDSs and for travellers to print tickets in their office have also attracted corporate travellers to rail.

Environmental considerations and sustainable business travel

Corporate environmental and sustainable travel policies

7.52 Issues of climate change have been featuring on both political and business agendas in recent years, and are likely to continue to do so for the foreseeable future. Although environmental considerations may have slipped down the corporate agenda somewhat because of the state of the economy, they are expected to become important again once the global and UK economies have recovered to a more 'normal' trend growth.

7.53 There was a general agreement among the stakeholders interviewed as part of this study that, in the future, companies' travel policies would focus more on environmental impacts and a corporate duty of care[362] to their employees. Actions such as data collection through the TMC in order to track emissions from company travel, carbon offsetting, and mandating alternatives to air travel (for example, using

362. Although the focus was largely around safety and the quality of the chosen supplier, duty of care could also extend to the issue of whether a company had a duty to ensure that an employee used the most appropriate form of travel for their well-being, giving a reasonable level of safety and comfort such that they are sufficiently refreshed and comfortable. The company's travel policy determines whether this can allow no-frills carriers short-haul, Business Class for journeys over a certain duration etc, bearing in mind that the employee may be going straight to a meeting on arrival, or flying straight back after a meeting.

rail for trips less than a certain distance, or substituting internal meetings with videoconferencing) were thought likely to become more common.[363]

7.54 Stakeholders also agreed that environmental credentials were increasingly considered in negotiations between buyers and suppliers, to the extent that airlines' environmental credentials are sometimes validated by a third party. These credentials could therefore give an airline a competitive advantage, and form part of a wider corporate sustainable business framework.[364]

7.55 However, for many companies, travel to meet clients face-to-face is still likely to be seen as a necessary business activity, and there is no evidence to suggest that this will change significantly in the foreseeable future. For manufacturing, retail or production companies, business travel is likely to form only a small fraction of their overall carbon emissions, and therefore future efforts to be more environmentally responsible may be concentrated on activities other than business travel.[365]

7.56 For some large corporations and multinational enterprises (such as banks, consultancies and some high value-added service industries), business related travel accounts for up to 50% of their total carbon emissions.[366] Stakeholders thought that extra pressure is likely to be put on business travel by air by such companies in the future, particularly where it is unnecessary for the core business (as has already happened during the recent recession) and where alternatives exist. However, action is likely to focus more on mitigation of emissions through activities such as offsetting, and through increased pressure on airlines to reduce emissions where possible.

Airline response to climate change concerns

7.57 In the UK, the need to reduce national CO_2 emissions has now become a legal requirement through the Climate Change Act which provides both challenges and opportunities for the transportation sector (including air, rail, car and sea transport). The UK aviation sector accounted for 6.4% of national carbon emission in 2008[367] and is projected to contribute 34.5% by 2050.[368]

7.58 For airlines, fuel is a significant cost, and, more so than other costs, an unpredictable one. As a percentage of UK airlines' operating costs, fuel expenditures increased from around 15% on average in the mid-90s to more than 30% in 2008 when the oil price peaked at around US$145 per barrel. While oil prices fell back during the recession, there is considerable uncertainty about the levels they will reach once stable world economic growth returns. Thus, it is already in airlines' interests to reduce fossil fuel usage, and hence carbon emissions, as much as possible. In the future, there will be even more of a competitive advantage to airlines in becoming more fuel efficient, arising from increased EU legislation on emission trading and, most likely, pressures from consumers.

363. For example, around 40% of HSBC's carbon emissions were travel related in 2004. In an effort to reduce its environmental impacts, HSBC has planted trees, used 'green' electricity supplies, reduced energy usage, and traded voluntary carbon credits to cut its carbon emissions. It has also implemented global supply chain metrics to measure carbon emissions across 16 different corporate activities, including business travel, and seeks to contract with suppliers (including airlines) that support its environmental initiatives by performing sustainability assessments.
364. For example, Project Icarus led by Institute of Travel and Meetings is designed to create an environmental impact reduction toolkit and introduce an accreditation process through which travel buyers and their suppliers can drive carbon-reducing strategies through their travel purchase decisions.
365. This does not preclude companies from reducing emissions from business travel if cost-effective and more environmentally sustainable alternatives to business air travel can be easily adopted. However, major reduction of carbon emissions from these industries have to come from activities other than business travel.
366. Cranfield University Business Travel Research Centre: *A carbon reduction framework for buyers of business travel*, Project Icarus – Final Report (November 2008).
367. Department of Energy and Climate Change: *Final UK Greenhouse Gas Emissions* (2008).
368. These forecasts are obtained from Table K1a of Department for Transport: *UK Air Passenger Demand and CO_2 Forecasts* (January 2009), which assumes that international aviation is additional to UK domestic obligations, which is to reduce domestic emissions by 80% below 1990 levels by 2050.

7.59 The EU emissions trading scheme will commence in 2012, requiring airlines to surrender allowances covering the CO_2 their operations incur on all flights to and from EU countries, plus Iceland, Norway and Lichtenstein. While there will be some free allocation of allowances, any increase in flying will need to be funded through purchase of allowances. Historically, allowance prices have remained relatively low, but airlines will face the risk that prices could become much higher in the future.

7.60 Although there is no evidence of environmental concerns having a significant impact on air travellers' behaviour, for example making a choice based on the environmental credentials of an aircraft type, the more consumers base their purchasing decisions upon environmental issues,[369] the more economic pressure will begin to bear on airlines to make efficiencies over and above those already instigated by fuel cost and tax reasons. As higher yielding (and usually more frequently flying) customers, any such pressure brought to bear by business travellers (or their corporate buyers) in the future is likely to have a greater impact on airline behaviour than that from leisure passengers.

7.61 Indeed, many airlines are now promoting their carbon credentials by highlighting their investment in a more fuel-efficient fleet, and the practice of publishing sustainability or CSR reports, which typically include sections on the efficiency of airline fleets and their operations, has also become increasingly common, especially among larger airlines.[370] Airlines also fund and support umbrella organisations, such as Sustainable Aviation or Greener by Design, to research – and advise policymakers on – ways to encourage sustainable growth in the aviation industry. Airlines that do not invest in more fuel-efficient aircraft or adopt new alternative fuel technologies (such as bio-fuels)[371] may risk a loss of competitive advantage or face an increased risk of reputational damage.

7.62 In addition to incentives to environmental performance from cost reduction and legislation, airlines will also need to better cater to the needs of those higher yield business and corporate travellers whose travel decisions are influenced by their companies' sustainable travel policy.

369. For example if more passengers begin to use websites that allow comparison of carbon emissions per trip by different airlines.
370. For example, BA, Air France/KLM, Lufthansa, Cathay Pacific, American Airlines, Delta and Qantas have all published a CSR report on their websites.
371. For example, BA, Virgin, Air New Zealand, Cathay Pacific and others have invested in lower carbon alternative fuels from sustainable, second and third generation feedstocks, such as biomass waste or algae.

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Part 2 Annex 2.A CAA survey of business passengers

Interviewer ID | Shift ID | Date/Time

Q1 What is the size of the company that you work for? ***(Business passengers only)***

Number of employees

Q2 Thinking about this trip and your last **business/leisure** trip, did you make any changes to the original flight bookings on either occasion? ***(Please circle)***

Yes No

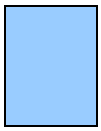
Q3 How long ago was this trip originally booked? ***(Please tick)***

Less than 1 week

Between 1 to 2 weeks

Between 3 to 4 weeks

Between 1 – 3 months

More than 3 months 

Q4 What method was used to book today's flight? ***(Please circle code or write in)***

Self-booking via internet (airline website)….11 Self-booking via internet (other website)….13

Travel agency branch office……..2 Self-booking via internet (website n/k)…….9

Corporate travel office (in house)……7 Corporate travel office (implant)……6

Other (write in)……

Q5 Please list up to THREE reasons why you chose to fly with a*irline* from this airport today? ***(Please rank order of importance)***

1……

2……

3……

Part 2 Annex 2.B Econometric analysis and results

The general form of the demand function for the directional international business passenger traffic for market i by country of residence j is expressed as:

$$Business\ pax_{ij} = f\left(GDP_j, Fares_{ij}, Volume\ of\ trade_{ij}, dummy\ variables\right) ----(1)$$

$$where\ \ i = EU25, North\ America\ or\ Rest\ of\ the\ World$$

$$j = UK\ or\ Foreign$$

Prior to the econometric estimation, all the variables in equation (1) above were transformed logarithmically to reduce skewness in the data, making the distribution more uniform. Furthermore, the estimated coefficients from the resulting log-log model can be interpreted as elasticities, which are assumed to be constant over time.

To empirically analyse the long-run relationships and short-run dynamic interactions among the variables of interest, the six demand models (segmented by country of residence: UK/Foreign and geographical regions: EU25, NA and RW) were estimated based on the two-staged ARDL approach to cointegration advanced by Pesaran et al.(1995).[372] The two-staged ARDL procedure involves first testing for the existence of the long-run relationship between the variables under consideration. If so, the long-run coefficients and the associated error correction model of the underlying ARDL model are estimated in the second stage by the OLS method.

There are three advantages offered by this bound test approach over other cointegration analysis. First, it can avoid the problem of pre-testing whether the variables included in the model have unit roots or not as required by standard cointegration analysis such as the Johansen approach. Second, endogeneity problems and inability to test hypotheses on the estimated coefficients in the long run associated with the Engle-Granger residual-based method are avoided. Third, the test is relatively more efficient in small sample data as is the case in this study.

The ARDL representation of equation (1) in the form of an unrestricted error correction model is as follows:

$$\Delta Traffic_t = \beta_0 + \sum_{j=1}^{k} \beta_j^* \Delta Traffic_{t-j} + \sum_{j=0}^{k} \phi_j^* \Delta Fares_{t-j} + \sum_{j=0}^{k} \tau_j^* \Delta Trade_{t-j} + \sum_{j=0}^{k} \pi_j^* \Delta GDP_{t-j} + \lambda ECM_{t-1} + \varepsilon_t$$

where λ is the speed of adjustment for short run discrepancy to the long-run equilibrium and ECM_{t-1} is the error correction term defined as :

$$ECM_{t-1} = Traffic_{t-1} - (\beta_0 + \propto_1 Fares_{t-1} + \propto_2 Trade_{t-1} + \propto_3 GDP_{t-1} + dummy\ variables)$$

where αi's are the long run elasticities. The dummy variables are included to control for seasonal variations and impacts of the 11 September attacks and the recent economic downturn where appropriate.

372. Pesaran, M.H. and Shin, Y.: *An autoregressive distributed lag modelling approach to cointegration analysis* (1995), in S. Strass, A. Holly and P. Diamond (eds.), Centennial Volume of Rangar Frisch, Econometric Society, Cambridge University Press, Cambridge.

Without an appropriate and consistent index for globalisation, the volume of trade measure is used as a proxy for the extent of globalisation over time.[373] It is posited that as the world economy becomes more globalised, cross-border trade in goods and services will increase over time which, in turn, is expected to drive the demand for business travel.

To ensure the estimated relationships between business travel and its demand drivers are non-spurious and there exists meaningful long-run relationships between them, the model above was estimated based on the two-staged ARDL approach to cointegration that allows both long-run equilibrium relationship and short-run dynamics to be estimated.

Quarterly traffic and fares data for the six UK business air travel segments spanning the period 1993Q1–2010Q2 were obtained from the International Passenger Survey (IPS)[374] and the macroeconomic data were taken from various publications by the Office for National Statistics and from IMF's World Economic Outlook database.

The results of the estimated long- and short-run coefficients using the ARDL approach for UK/ Foreign business passengers to and from the three geographical markets are shown in Table B1. Due to the small number of observations since the onset of the recent recession, the impact of the recent global recession on business travel demand is investigated in three-steps in this study. First, models based on data in the pre-recession period (from 1993Q1 to 2008Q3) are used to forecast traffic between 2008Q4 and 2010Q2. The results suggested the presence of a structural break in the data as performance of the models in forecasting the out-of-sample business travel demand was generally very poor (see Table 3-8). In the second step, the impact of the recession was modelled by including an intercept dummy that takes the value of one from 2008Q4 and onward and zero otherwise (i.e. the impact is assumed to cause a 'step down' in demand around the end of 2008). The results in Table B1 show that the intercept shift dummies are highly significant across the six markets. Next, the stability of this enhanced model is then evaluated by inspecting the cumulated sum of recursive residuals (CUSUM) and the cumulated sum of squares of recursive residuals (CUSUMSQ).

Table B1 Business passenger model estimations

	EU25		**North America (NA)**		**Rest of the World (RW)**	
Variable	**UK resident**	**Foreign resident**	**UK resident**	**Foreign resident**	**UK resident**	**Foreign resident**
Long run						
GDP	1.80*** [0.55]	1.16*** [0.22]	1.96*** [0.22]	0.65* [0.25]	1.40*** [0.32]	1.27*** [0.26]
Fares	0.18 [0.24]	-0.13** [0.06]	0.28 [0.26]	-0.28** [0.14]	-0.61* [0.33]	0.23 [0.18]
Trade	0.03 [0.38]	0.12 [0.09]	0.004 [0.01]	0.53** [0.24]	0.33* 0.19]	0.10 [0.11]
Intercept shift	-0.50*** [0.20]	-0.26*** [0.04]	-0.32*** [0.05]	-0.13** [0.06]	-0.34*** [0.10]	-0.19*** [0.06]

373. Foreign direct investment, another potential driver for business travel, is not included in the model as quarterly data split by the three geographical markets are not available.
374. This is a questionnaire-based survey and as such may be subject to a number of sources of error.

Table B1 Business passenger model estimations (continued)

	EU25		North America (NA)		Rest of the World (RW)	
Variable	**UK resident**	**Foreign resident**	**UK resident**	**Foreign resident**	**UK resident**	**Foreign resident**
Short run						
$\Delta Traffic_{t-1}$	-.0.27** [0.13]	--	0.32*** [0.11]	0.27** [0.12]	--	--
$\Delta Traffic_{t-2}$	0.01 [0.14]	--	--	--	--	--
$\Delta Traffic_{t-3}$	-0.22* [0.13]	--	--	--	--	--
ΔGDP_t	0.65** [0.29]	1.16*** [0.22]	1.58*** [0.34]	2.62 [2.02]	2.45* [1.47]	0.85*** [0.20]
ΔGDP_{t-1}	--	--	--	2.33 [2.08]	-5.89*** [1.58]	--
ΔGDP_{t-2}	--	--	--	2.17 [1.94]	--	--
ΔGDP_{t-3}	--	--	--	5.64*** [2.10]	--	--
$\Delta Fares_t$	-0.26 [0.21]	0.22* [0.13]	0.13 [0.13]	-0.16 [0.11]	-0.006 [0.12]	0.16 [0.11]
$\Delta Fares_{t-1}$	0.46** [0.20]	0.47*** [0.13]	-0.29* [0.17]	-0.02 [0.14]	0.39** [0.16]	--
$\Delta Fares_{t-2}$	--	--	-0.10 [0.15]	-0.07 [0.13]	0.19 [0.12]	--
$\Delta Fares_{t-3}$	--	--	-0.28 ** [0.11]	-0.26** [0.10]	--	--
$\Delta Trade_t$	0.01 0.14]	0.12 [0.09]	0.003 [0.01]	0.62** [0.26]	0.18 [0.12]	0.07 [0.08]
ecm(-1)	-0.36** [0.14]	-1.0 [0.0]	-0.81*** [0.15]	0.83*** [0.17]	-0.56*** [0.13]	-0.67*** [0.11]

*Notes: Asterisks indicate statistical significance: *=10%; **=5%; ***=1%.*

Figures in square brackets indicate standard errors of the estimated coefficients.

Figure B1 below shows the actual and forecast values of UK-resident business passengers to and from rest of the world (UKRWBP) based on the enhanced model. Figure B2 shows the recursive residuals (CUSUM and CUSUMSQ) from the enhanced model which lie well within the 5% critical bounds in the post-break period, suggesting model stability in the coefficients of the enhanced model over the sample period which includes an intercept shift dummy. These plots are similar for all the six modelled business travel markets in this study.[375]

375. The plots and the results presented in Table B1 were generated by MICROFIT 4.0.

Figure B1 Actual and fitted values of UK resident business passengers to/from rest of the world (UKRWBP)

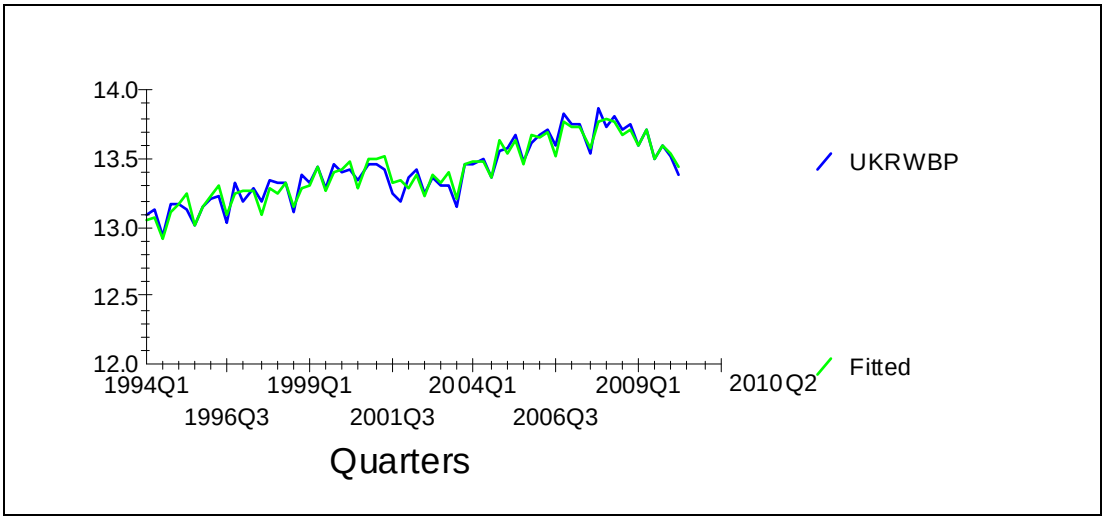
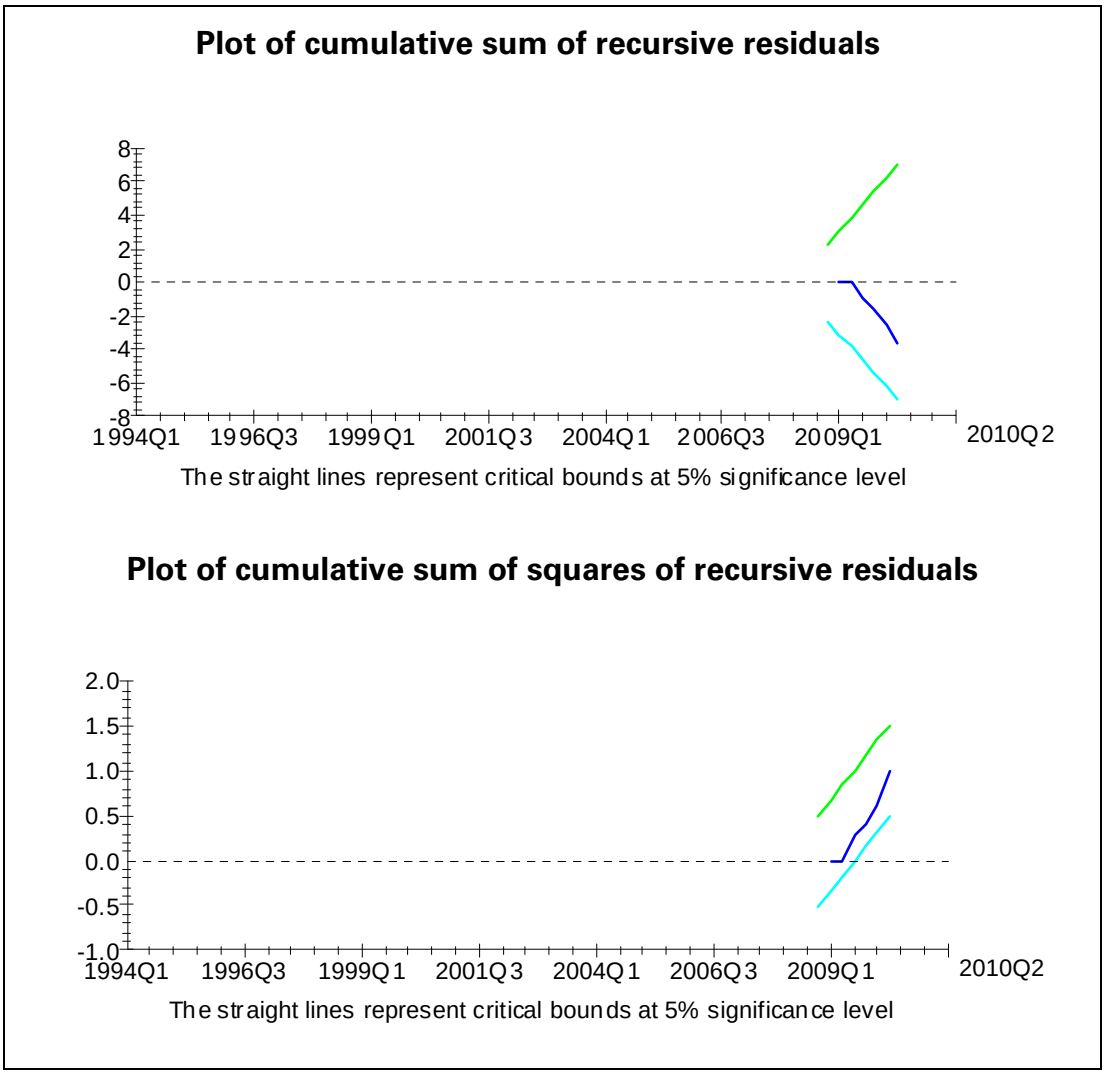


Figure B2 Plots of recursive residuals from the enhanced UKRWBP model



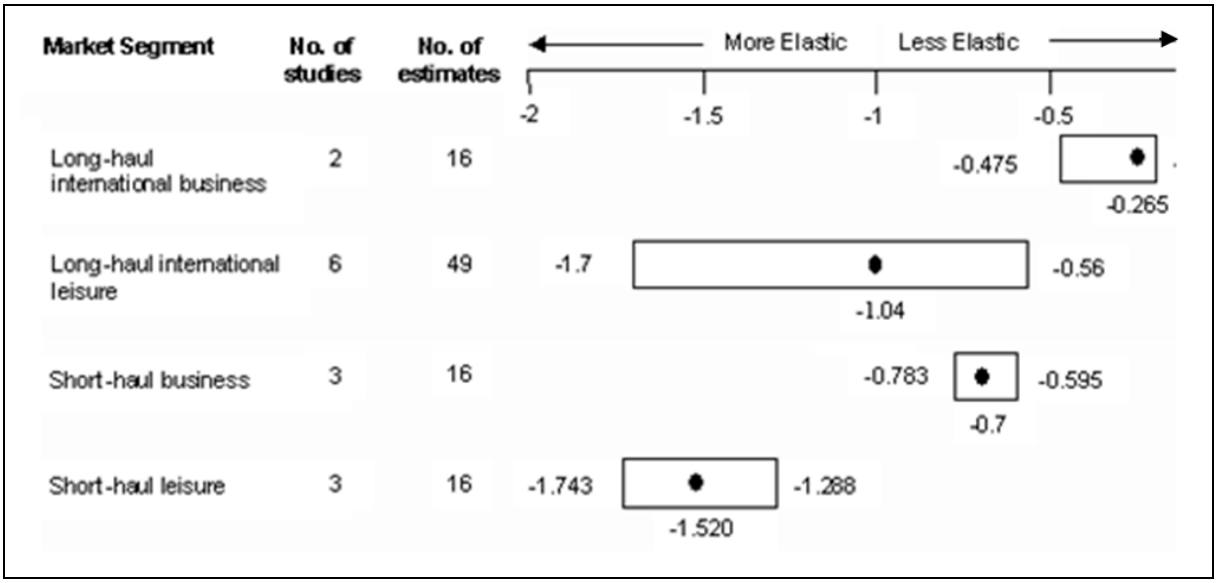
Part 2 Annex 2.C Review of income and fare elasticities of travel demand

In contrast to leisure demand elasticity, empirical estimates of business demand elasticity are relatively scarce, particularly with reference to the UK business travel market. Figure C1 below indicates the range of estimated values of own-price elasticities of demand for air travel by Gillen et al (2003) based on 21 Canadian and international empirical studies.[376]

There are two important caveats to the interpretation of the results presented in Figure C1. First, the median (represented by the black dots) and range of values are based on a small number of estimates and studies, particularly for the business markets. Second, only one[377] out of the 21 studies has referenced to the UK which gives the lowest estimate (-2.0) of own-price elasticity for Australian business travellers to the UK.[378]

Figure C1 suggests that demand for air travel is generally less price elastic for longer flights than for shorter flights and business travel is less price elastic than leisure travel.

Figure C1 Own-price elasticities of demand



Source: Gillen D. et al:, Air Travel Demand Elasticities: Concepts, Issues and Measurement, Department of Finance, Canada (2003).

Note: The ranges of values shown capture the middle one-half of the estimates and encompass the median values, represented by the black dots.

376. Gillen D. et al: *Air Travel Demand Elasticities: Concepts, Issues and Measurement*, Department of Finance, Canada (2003). A note of caution in interpreting these results is that 15 of the 21 studies were completed before 1990 and, apart from one study, none of them considered business travel to and from the UK.
377. Department of Transport and Communications and Economics, Bureau of Transport Economics: *Demand elasticities for air travel to and from Australia, Working Paper 20* (1995).
378. Another study that considers UK business travel is Dargay and Hanly: *The determinants of the demand for international air travel to and from the UK*, Paper presented at the 9th World Conference on Transport Research (2001). While they find business travel demand by foreign residents to the UK has a long-run fare elasticity of –0.32, fare elasticity by UK residents going abroad is insignificantly different from zero.

Similarly, Figure C2 shows the wide range of income elasticities based on 132 estimates from 14 studies. It varies from the minimum of –1.21 (leisure travel from US to Australia) to the maximum of 11.58 (leisure travel by Australian residents to Taiwan).[379] The median estimate is around 1.4.

Figure C2 Histogram of aggregate income elasticities

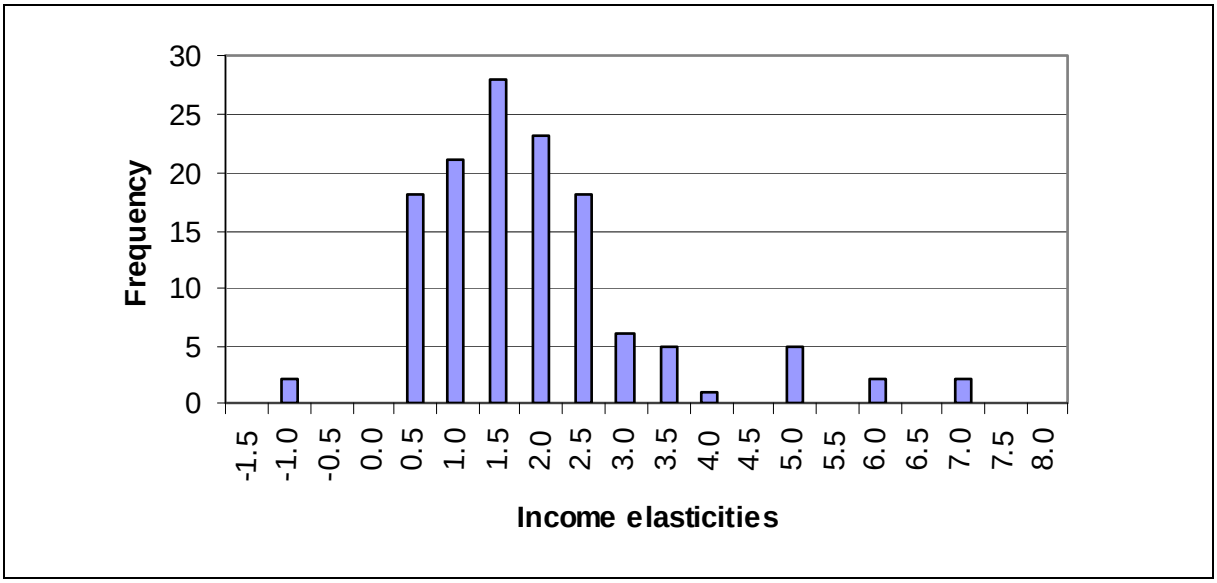


Table C1 shows estimates of income and fare elasticities related to the UK market.

Table C1 Estimated elasticities for leisure and business travel to/from the UK

Reference	Leisure		Business
	Income elasticity	Fare elasticity	Fare elasticity
Dargay and Hanly (2001)			
UK residents going abroad	1.05	-0.58	–
Foreign residents to the UK	1.8	-0.33	-0.32
PriceWaterhouseCoopers (2005)	1.1 to 2.5	-1.5	-0.73
DETR (2000)	0.4 to 0.8	-1.3	-0.5
DfT (2009)	0.4 to 2.1	-0.2 to -1.0	–
CAA (2005)	1.5 to 1.8	-0.7 to -1.5	n/a

379. The maximum is not shown in the figure. See Gillen et al (2003) for further detail.