

## APPENDIX D

# Evidence and analysis on market definition

---

- D1 This appendix sets out the CAA's analysis of evidence relating to the definition of the market(s) in which Stansted Airport Limited (STAL) operates.
- D2 This analysis covers only the detail on the CAA's assessment on the market for airport operation services for passenger services at Stansted. Given the focus of cargo operations at Stansted on the use of freighter aircraft and the limited available bellyhold (due to the significant low cost carrier (LCC) presence, which do not generally carry cargo), the CAA has considered airport operation services provided to cargo only operations separately.
- D3 This appendix is structured as follows:
- Section 1 sets out the legal and analytical framework under which the CAA has undertaken its analysis.
  - Section 2 sets out the conclusions from the CAA's "Stansted market power assessment, Developing our 'minded to' position" (the minded to Consultation). It also sets out the key points raised by stakeholders in response to the minded to Consultation.
  - Section 3 sets out the CAA's formal market definition analysis.
  - Section 4 sets out the CAA's conclusions on market definition.

## Section 1: Legal and analytical framework

---

- D4 Market definition is a key component of the market power test in section 6 of the Civil Aviation Act 2012 (the CA Act) and is relevant for assessing whether STAL, as the operator of Stansted, has substantial market power (SMP) for the purposes of Test A. The test is applied by reference to the relevant market, i.e. a market for one or more types of airport operation services within the airport area.
- D5 In reaching its decision, the CAA has had regard to its own guidance for the assessment of market power of airports (the Guidelines)<sup>1</sup> as well as

---

<sup>1</sup> The Guidelines can be accessed via the CAA's website at:  
<http://www.caa.co.uk/docs/5/Final%20Competition%20Assessment%20Guidelines%20-%20FINAL.pdf>.

the applicable Office of Fair Trading (OFT) and European Commission (EC) competition law notices and guidance to which it must have regard under section 6(10) of the CA Act.<sup>2</sup>

- D6 Market definition is a useful tool for identifying, in a systematic way, the competitive constraints which the relevant operator faces in the market and whether those constraints prevent it from operating independently of effective competitive pressure.<sup>3</sup> However, there may be characteristics of the airport sector that make it difficult to define the market precisely. As explained in the Guidelines, the market power assessment should seek to analyse all the competitive constraints faced by an airport operator, regardless of whether they arise from within or outside the relevant market(s).<sup>4</sup>
- D7 The CAA does not regard market definition as an end in itself, but rather as an economic framework within which to analyse the competitive effects of market definition to support and inform the CAA's regulatory policy.<sup>5</sup> The exercise of market definition consists, in essence, of identifying the effective alternative sources of supply for the customers of the relevant operator in terms of the products or services supplied and their geographical location.<sup>6</sup>

### Hypothetical monopolist test

- D8 The Guidelines state that, wherever feasible, the hypothetical monopolist test should be adopted as a useful starting point for defining the relevant market.<sup>7</sup>
- D9 The hypothetical monopolist test involves starting with the narrowest possible bundle of products or services and the smallest geographical area (normally those supplied by the operator in question) and assessing marginal customers' switching reactions to a hypothetical monopolist making a small but significant non-transitory increase in price (SSNIP),

<sup>2</sup> See the OFT's Competition Law Guideline on Market Definition, dated December 2004 (OFT 403) and the EC's Notice on the definition of relevant market for the purposes of Community competition law (OJ 97 C 372 p. 3) (EC Market Definition Notice).

<sup>3</sup> EC Market Definition Notice, paragraph 2.

<sup>4</sup> The Guidelines, paragraph 3.5. This is consistent with the approach adopted in the Competition Commission's (CC) report on the supply of airport services by BAA in the UK 19 March 2009 (CC's 2009 BAA Report), paragraphs 2.48 to 2.49.

<sup>5</sup> The Guidelines, paragraph 1.4 and paragraphs 3.3 to 3.4. See also OFT 403, paragraphs 2.1 and 2.6 and the EC Market Definition Notice, paragraph 2.

<sup>6</sup> Guidelines, paragraphs 3.6 to 3.9 and EC Market Definition Notice, paragraphs 7 to 9 and 13.

<sup>7</sup> The Guidelines, paragraphs 3.10 to 3.12; OFT 403, paragraphs 2.5 to 2.13 and EC Market Definition Notice, paragraphs 15 to 19.

above the competitive price level (generally considered as being 5 to 10 per cent).

- D10 If the price increase is unprofitable due to marginal customers switching away to substitute products/services and areas or new suppliers entering the market and competing away any potential profits, then the test is repeated by widening the set of products/services and geographic area to include the closest substitute until the price increase is profitable. What is then left is the narrowest set of products/services and geographic area over which a hypothetical monopolist could profitably sustain prices 5 to 10 per cent above competitive levels.
- D11 Although the SSNIP test is a useful starting point, it requires a significant amount of information about the market, including the supply and demand conditions. The test is also not mechanistic as it requires judgement to be applied at a number of points in the analysis. In addition, the test is intended to be carried out by reference to the competitive price level, with the result adjusted where the prevailing price levels observed in the market are not reflective of the competitive price.<sup>8</sup> It also assumes that competitors' pricing strategies are competitive.
- D12 In addition, there may be other external considerations that might affect the uniformity and/or the profitability of the price increase.<sup>9</sup>
- D13 As a result, and as noted in the Guidelines, it is rarely possible to apply a SSNIP test in a precise manner due to data and evidential restrictions.<sup>10</sup> Therefore, a SSNIP should be considered as a way to frame the market definition process rather than be used as a mechanistic process for producing a market definition.
- D14 Given the particular circumstances relating to the historical regulation and common ownership of Heathrow, Gatwick and Stansted, the CAA has been unable to carry out a formal SSNIP test. However, it has gathered a range of evidence, including catchment area analysis, passenger surveys, documentary evidence and the views of airlines and relevant airport operators on substitutability. This has been interpreted, as far as is possible, within the hypothetical monopolist framework.

---

<sup>8</sup> As the OFT observes, the test assumes that the hypothetical monopolist is not subject to economic regulation that might affect its pricing behaviour.

<sup>9</sup> OFT 403, paragraph 2.10 to 2.11 and 5.4 to 5.6. See also Guidelines, paragraphs 3.15 to 3.16 and 3.24 to 3.25.

<sup>10</sup> The Guidelines, paragraph 3.13. See also the CC's 2009 BAA Report, paragraph 2.1.

## Product market

- D15 As defined in both EC<sup>11</sup> and OFT<sup>12</sup> guidance, a relevant product market comprises all those products and/or services that are regarded as interchangeable or substitutable by the consumer by reason of the products' characteristics, their prices and their intended use.<sup>13</sup>
- D16 The CAA has looked at demand side substitutability for each user group individually, while accounting for interactions between the different groups, to determine whether services to each group constitute a distinct product market or whether they form part of a two-sided market with inter-related demand.<sup>14</sup>

## Geographic market

- D17 The geographic market '*comprises the area in which the undertakings concerned are involved in the supply of products or services and in which the conditions of competition are sufficiently homogeneous.*'<sup>15</sup>
- D18 The area can be distinguished from neighbouring areas because the conditions of competition are appreciably different. In addition, as airports serve a number of different users, there may be different relevant geographic markets for different groups of users.<sup>16</sup>
- D19 The assessment of competitive constraints for geographic market definition will include an analysis of the ability of airlines to switch away from an airport as well as the potential for passengers to switch between airports, whether independently or by following a particular airline. With respect to this, the EC notice on market definition states:<sup>17</sup>

*Firms are subject to three main sources or competitive constraints: demand substitutability, supply substitutability and potential competition. From an economic point of view, for the definition of the relevant market, demand substitution constitutes the most immediate and effective disciplinary force on the suppliers of a given product, in particular in*

<sup>11</sup> Commission Notice on the definition of relevant market for the purposes of Community competition law OJ C 372, 9.12.1997, pp. 5 to 13, available at:[http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=CELEX:31997Y1209\(01\):EN:HTML](http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=CELEX:31997Y1209(01):EN:HTML).

<sup>12</sup> OFT, Understanding Competition Law: Market Definition, 2004, available at: [http://www.of.gov.uk/shared\\_of/business\\_leaflets/ca98\\_guidelines/of403.pdf](http://www.of.gov.uk/shared_of/business_leaflets/ca98_guidelines/of403.pdf).

<sup>13</sup> The Guidelines, paragraphs 3.7 and 3.27.

<sup>14</sup> The Guidelines, paragraphs 3.29 to 3.33.

<sup>15</sup> The Guidelines, paragraph 3.8 and EC Market Definition Notice, paragraph 8.

<sup>16</sup> The Guidelines, paragraph 3.59.

<sup>17</sup> EC Market Definition Notice, paragraph 13.

*relation to their pricing decisions. A firm or a group of firms cannot have a significant impact on the prevailing conditions of sale, such as prices, if its customers are in a position to switch easily to available substitute products or to suppliers located elsewhere. Basically, the exercise of market definition consists in identifying the effective alternative sources of supply for the customers of the undertakings involved, in terms both of products/services and of geographic location of suppliers.*

## Supply side substitution

D20 As noted in the Guidelines<sup>18</sup> (and the OFT Guidelines<sup>19</sup>), supply side substitution is a key part of the market definition analysis. The EC also highlights this where it notes:

*Supply-side substitutability may also be taken into account when [defining markets], in those situations in which its effects are equivalent to those of demand substitution in terms of effectiveness and immediacy. This means that suppliers are able to switch production to the relevant products and market them in the short-term without incurring significant permanent changes in relative prices. When these conditions are met, the additional production that is put on the market will have a disciplinary effect on the behaviour of the companies involved. Such an impact in terms of effectiveness and immediacy is equivalent to the demand substitution effect.<sup>20</sup>*

## Temporal markets

D21 OFT guidance<sup>21</sup> states that a possible third dimension to market definition is time. The Guidelines also state that a time dimension may be appropriate where it is not possible for customers or suppliers to substitute between time periods.

## Section 2: Minded to consultation process

### Minded to Consultation

D22 In the minded to Consultation, the CAA suggested that airport operators supply a broadly generic product in the form of a bundle of airport operation services. However, the CAA also observed differences in the product market with respect to the facilities required to service particular

<sup>18</sup> The Guidelines paragraphs 3.27 and 3.56 to 3.58.

<sup>19</sup> OFT 403 paragraphs 3.12 to 3.18 and 4.5.

<sup>20</sup> EC market definition notice, paragraph 20.

<sup>21</sup> OFT 403, paragraphs 5.1 to 5.3.

segments; LCCs and charters, full service long-haul carriers and their associated feeder traffic, and cargo-only operators.

- D23 For LCCs and charters, the CAA considered that there was limited differentiation in their passenger base which translated into the need for generic facilities. The CAA also considered that LCCs required the airport operator to provide tight turnaround times for their operations. The geographic scope of this market was the service provided to these airlines at Stansted, Luton, Southend and possibly Gatwick.
- D24 For full service long-haul carriers and their associated feeder traffic, the CAA considered that these carriers had a segmented passenger base that required the provision of additional facilities to that required for LCCs and charters for their passengers, i.e. first class and business lounges. In addition, the CAA considered that there was a requirement to allow passengers to interline between feeder flights and long-haul flights to ensure efficient load factors. The geographic scope of this market was the services provided to full service long-haul carriers and their associated feeder traffic at least at Stansted, Gatwick and Heathrow.
- D25 For cargo-only operators, the CAA considered that there was a requirement for dedicated facilities for the handling of cargo and no requirement of facilities for the processing of passengers. The geographic scope of this market was limited to services provided at Stansted.

### **Consultation on recent market developments**

- D26 Following Manchester Airports Group's (MAG) recent acquisition of STAL as well as STAL signing of a number of long term bilateral deals with a number of airlines, the CAA considered that the conditions in the passenger market appeared to have changed in a way that was potentially material and could make a difference to the outcome of the market power test for STAL.
- D27 In October 2013, the CAA therefore released, for consultation, the Stansted Market Power Assessment: consultation on relevant market developments (the additional Consultation).<sup>22</sup>
- D28 While the additional Consultation examined a number of issues the CAA did not consider that the change in ownership and the signing of the bilateral deals required it to reconsider the relevant markets in which STAL operates.

---

<sup>22</sup> This document is available at:  
<http://www.caa.co.uk/application.aspx?catid=33&pagetype=65&appid=11&mode=detail&id=5807>.

D29 Stakeholders' views on the additional Consultation did not suggest that the CAA's market definition should be amended. The views outlined below are therefore limited to those outlined in the minded to Consultation.

## Stakeholders' views

D30 The CAA received five responses to the minded to Consultation:<sup>23</sup>

- easyJet;
- Gatwick Airport Ltd (GAL);
- MAG;<sup>24</sup>
- Ryanair; and
- London Southend Airport Company Ltd (LSACL).

D31 MAG did not agree with the CAA's market definition and criticised the CAA's position on a number of points.<sup>25</sup>

- The product and geographic market definitions were too narrow and inconsistent with the Guidelines, previous regulatory statements and wider competition law practice. MAG also highlighted perceived inconsistencies between the CAA's approach and the analysis conducted by the CC in the BAA airports inquiry. MAG considered that it was not reasonable to depart from the CC's position.
- The CAA had moved from its position of supporting a much wider geographic market definition in its Initial Views.<sup>26</sup>
- The wrong level of the market is assessed and the CAA often conflated the different levels of the market.
- The CAA had misdirected itself in its assessment of the multi-sided nature of the airport and had omitted to take proper account of commercial revenues and its implications for market definition.

---

<sup>23</sup> These submissions are available on the CAA's website:

<http://www.caa.co.uk/default.aspx?catid=1350&pagetype=90&pageid=14395>.

<sup>24</sup> MAG submitted a further response commenting on the airlines' responses to the 'minded to' consultation.

<sup>25</sup> MAG, Civil Aviation Authority Stansted Market Power Assessment; Interim response of MAG to the CAA's 'minded to' document 24 May 2013.

<sup>26</sup> Initial Views refers to the CAA, Stansted – Market Power Assessment: Non-confidential Version The CAA's initial Views, February 2012.



- The CAA had not paid sufficient attention to marginal customers and their willingness to switch in the face of a 5 to 10 per cent price increase.
- D32 GAL challenged the CAA's segmentation of the market between LCCs and full service carriers (FSCs) on the basis that it had failed to recognise the competition and route overlaps between them. It also highlighted inconsistencies between the CAA's analysis and the position set out in the Guidelines, previous decisions and regulatory assessments as well as with the EC.<sup>27</sup>
- D33 Ryanair was supportive of the CAA's overall position. LSACL did not comment substantively on the CAA's findings.
- D34 easyJet, although supportive of the CAA's position, considered that the CAA had overlooked the critical distinction for the product market, namely services provided by STAL to point-to-point carriers and services to networked carriers.<sup>28</sup>
- D35 While the CAA's analysis on stakeholders' views is outlined in the section below, the CAA responds to the criticism that it has been inconsistent in this section.
- D36 Much of the material that the CAA has produced on the airport market was undertaken a significant time ago and under a different legislative regime. In particular, the de-designation assessment of Stansted in 2007 and comments made by the CAA in its initial considerations of the CC's investigation into BAA airports took place prior to the extensive level of work undertaken by the CC and the discussion of the key issues during the course of the appeals that followed. The CAA considers that it would not be rational for it to ignore the CC's findings and approach as part of its assessment of the current market position of STAL.
- D37 With the exception of the geographic market definition where the CAA now considers the market to be Stansted, Luton and Southend. The CAA considers its treatment of the product market and other hubs is consistent with that of the CC. The difference in the geographic market arises as a result of the question under investigation where the CAA has to consider the market position of the individual airport operators.

---

<sup>27</sup> GAL, CAA Stansted Market Power Assessment - Response from Gatwick Airport, reference Q5-050-LGW59, 21 May 2013 and GAL, CAA's Gatwick Market Power Assessment: Response from Gatwick Airport Limited, reference Q5-050-LGW60, 26 July 2013.

<sup>28</sup> easyJet, easyJet's response to the CAA's Minded to Consultation on Market Power on Stansted Airport, May 2013 and easyJet, easyJet response to CAA consultation on Gatwick airport market power, July 2013.



- D38 It is in any event widely accepted that market definition is a flexible tool that may alter depending on the question being asked. For example, the CC's BAA airports investigation considered a particularly wide question on the potential for the development of competition between the three BAA airports and sought to remove structural impediments to the development of potential competition. The CC was not looking into the much narrower question that the CAA must consider under Test A, which is whether an individual airport operator has substantial market power in a market for airport operation services provided at the airport in question. The CAA must also do so in a manner which complies with its duties under section 1 of the CA Act. These direct the CAA to focus on the interests of users of air transport services and to do so, where appropriate, by promoting competition while having regard to a wide range of (potentially) competing factors.
- D39 Likewise, with merger case law, the investigating authority is seeking to determine whether a merger will weaken the current competitive landscape observed within a market.
- D40 Furthermore, market definition is a time-sensitive and context-specific exercise. It is based on an analysis of the structure of the market and competition prevailing at a particular point in time.<sup>29</sup> Hence any assessment may change over time as market circumstances evolve.
- D41 In addition, a prior finding of dominance by the EC or a national competition authority or even a national court is not binding and even the EC has to start a fresh analysis of the condition of competition in the course of making subsequent decisions:
- In the course of any decision applying Article 86 of the Treaty the Commission must define the relevant market again and market a fresh analysis of the conditions of competition which will not necessarily be based on the same considerations as those underlying the previous finding of a dominant position.*<sup>30</sup>
- D42 Therefore, while a significant amount of information can be drawn from the investigation on BAA airports, the CC was considering a different question. Test A, the test that the CAA must consider, is concerned with individual airport operators.
- D43 It also does not follow that the divestment remedy imposed by the CC on BAA is tantamount to there being an immediate and effectively competitive market. In particular, although the potential for competition

---

<sup>29</sup> Bellamy and Child EU law of Competition, paragraph 10.018.

<sup>30</sup> Case T-125/97 Coca-Cola v Commission [2000] ECR ii-1733, paragraph 82.

increased following divestment, this is coming from the position of effectively no competition as the airports were under joint ownership.

D44 The CC also expected competition to develop over time:

*Even under separate ownership, moreover, as a result of capacity constraints, competition in the short term may focus on particular types of traffic, for example in off-peak periods, and therefore be unlikely to be sufficiently effective to substitute for regulation. Separate ownership would also give rise to competition to invest in new capacity; but there would be a period of time before there could be confidence that competition between separately-owned airports was sufficiently effective to substitute for regulation. Heathrow, however, may retain a strong market position as the main UK hub airport, requiring effective regulation for longer.<sup>31</sup>*

D45 Finally, since the publication of the Initial Views the CAA has developed a substantial evidence base on. This evidence and how the CAA has used it was outlined in the minded to Consultation and is also outlined in this document.

### Section 3: CAA analysis

---

D46 In light of the representations from stakeholders on the minded to Consultation, the CAA has re-evaluated its assessment of the evidence and has altered its position on the relevant market definition for STAL. The CAA now considers that there is a single relevant market in which STAL operates. The market is for the provision of airport operation services to passenger airlines, extending not only to those services provided at Stansted but also at Luton and Southend.

D47 This analysis covers only the detail on the CAA's assessment on the market for airport operation services on the passenger side at Stansted. Given the focus of cargo operations at Stansted on the use of freighter aircraft and the limited available bellyhold (due to the significant LCC presence), the CAA has considered airport operation services to cargo-only operators separately.

D48 The CAA received many responses to the Initial Views and the minded to Consultation. This final decision contains summaries of, and answers to, many of the points made.

D49 The CAA's analysis also sets out its response to the key arguments raised during the minded to Consultation and, where appropriate, the

---

<sup>31</sup> CC's 2009 BAA Report, paragraph 6.87.

reasons for not accepting stakeholders' views. The evidence and reasons for the CAA's conclusions are set out in the next section on an issue by issue basis

- D50 This section sets out the CAA's analysis of the evidence on market definition for the services provided by STAL. In particular:
- Section 3.1 examines, in more detail, the analytical concepts considered by the CAA.
  - Section 3.2 outlines the relevant product market definition.
  - Section 3.3 outlines the relevant geographic market definition.
  - Section 3.4 outlines the relevant temporal markets definition.

### Section 3.1: Analytical concepts

- D51 This section outlines a number of the analytical concepts considered when the CAA defined the relevant market:
- The SSNIP test.
  - Interdependence of demand from different user groups.
  - The role of airline and passenger switching in vertical derived demand analysis.
  - Airline competition.

#### The SSNIP test

- D52 As noted in the Guidelines, it is rarely possible to apply the SSNIP test in a precise manner due to evidence and data limitations. One of the key difficulties associated with using this test is identifying the competitive price level for an airport.
- D53 Using a price which is too high as the starting point for a SSNIP analysis risks defining an overly wide market (the Cellophane Fallacy), while using a price which is too low risks defining an overly narrow market (the reverse Cellophane Fallacy).
- D54 To deal with the difficulties in identifying an appropriate price level (that is a price level which controls for the risks of Cellophane and the reverse Cellophane) to be used in the SSNIP test for STAL the CAA considered:
- the regulated price or regulated asset base (RAB) based price;<sup>32</sup>

<sup>32</sup> RAB is the Regulatory Asset Base. A RAB-based price is derived from the income per passenger

- a long-run average incremental costs (LRAIC) based price; and
- a price based on benchmarking comparable airports.

*The regulated price (RAB-based prices)*

D55 In defining the relevant market, the CAA has used the current, regulated price as the basis for its analysis. STAL's pricing behaviour is discussed in appendix H.

D56 Using the regulated price is an appropriate starting point for the SSNIP analysis as it is:

- cost-based (on the basis of an acceptable cost standard) and is designed to prevent a regulated airport from pricing at levels exercising SMP (and potentially making super normal profit). For example, STAL's RAB-based price caps allows for the recovery of efficient operating expenditure and capital expenditure plus a fair return on its RAB. As a result, the use of the regulated price provides the CAA with comfort that they are not the prices that would occur in the extreme cases of monopoly or below cost pricing, which reduces the risk of defining either overly wide or overly narrow markets.
- Are the actual and prevailing prices faced by airlines, groundhandlers and passengers. Its use therefore limits the risks associated with gathering evidence around or hypothesising about unknown price levels. The CAA also considers that it would be difficult for the airlines to respond on how they would react to a 5 per cent SSNIP from a price that they do not observe in practice.
- Have been used in several cases of market definition for regulated industries across Europe. In particular, the EC has taken the view that regulated prices should be taken as the starting point for conducting a SSNIP test. Specifically for telecommunications, the EC has stated:

*In principle, the 'hypothetical monopolist test' is relevant only with regard to products or services, the price of which is freely determined and not subject to regulation. Thus, the working assumption will be that current prevailing prices are set at competitive levels. If, however, a service or product is offered at a regulated, cost-based price, then such price is presumed, in the absence of indications to the contrary, to be set at what would otherwise be a competitive level and should therefore be taken as the starting point for applying the 'hypothetical monopolist test.'*

---

that allows for the recovery of efficient operational expenditure (opex) and capital expenditure (capex) plus a fair return on the assets as measured by the RAB.

D57 Connected with the first bullet point above, the regulated price for STAL is determined through a cost-based approach and the process that the CAA goes through to determine this is rigorous, consultative and lengthy.

*The long-run average incremental costs (LRAIC) based price*

D58 In the minded to Consultation the CAA listed a number of drawbacks with the estimation of LRAIC-based prices including:

- As LRAIC is a long-term forward-looking measure there is a risk of over and under recovery in a particular period.
- A LRAIC approach is data intensive and requires regulatory judgement to define the increment (although this might be less for a replacement cost approach). This can lead to significant uncertainty over future price profiles.
- It has also been argued that it is not an effective proxy for competitive airport prices where investments are very 'lumpy'.
- The accuracy of a LRAIC can be adversely affected by the history of ownership and regulation of the London airports. In particular, it has been argued that the current specification of the airports was set by BAA (as the common owner of Heathrow, Gatwick and Stansted), which means that the estimates of the incremental costs at the airport are higher than the costs of expanding an efficient airport.

D59 Looking to address the various views on the scope and the practical problems of LRAIC modelling the CAA commissioned Europe Economics (EE)<sup>33</sup> to estimate a LRAIC for STAL and identify the advantages and disadvantages of using a LRAIC based approach to inform estimates of the competitive price at Stansted (and to set price caps).

D60 While EE's approach has been criticised (see appendix H), EE examined four<sup>34</sup> increments for STAL and considered that the most appropriate increment to use for LRAIC was complete airport replacement. Using this increment, EE determined that the LRAIC at Stansted was £6.30 per passenger<sup>35</sup> with estimates changing by +/- 10 per cent to 15 per cent with relatively small changes in assumptions.

---

<sup>33</sup> EE, Advice on the application of long run incremental cost estimates for Gatwick and Stansted, Final Report, 20 December 2012.

<sup>34</sup> Five increments were examined if you consider that two scenarios were considered under one of the increments examined.

<sup>35</sup> The other increments EE examined were based on SG1 plans SG2 plans and the airport's current capex plans.

- D61 EE indicated that estimating the LRAIC was one way of assessing price in a normally competitive market. However, it also identified a number of practical disadvantages of using this approach, including:
- Difficulties in determining the appropriate increment to use – as noted above, EE considered that the most credible increment would be the replacement of an airport (rather than, for example, a small amount of incremental capex or a new runway). However, it noted that since Stansted was a relatively new airport, these problems may be less severe.
  - Greater uncertainty (and loss of accuracy) due to the need to make a judgement as to the efficient levels and types of investment required rather than using historic values that were spent.
  - The potential for greater uncertainty of remuneration of investment. For example, a historic cost-based RAB system would offer greater certainty since once an investment cost has been approved for inclusion in the RAB it would be part of the calculation for future price limits.
- D62 EE's analysis also identified that any model that is used to estimate LRAIC would be sensitive to the inputs and the assumptions that underpin it. In particular, EE's sensitivity analysis indicated that changes to the inputs and assumptions could lead to quite significant changes in a LRAIC estimate. More fundamentally, EE questioned the relevance of an estimate of the competitive price obtained through LRAIC given the level of Government involvement in planning of airport capacity, particularly in the south east of England.<sup>36</sup>

### *Benchmarking*

- D63 An alternative way of estimating the level of the competitive price is to consider evidence on pricing at comparable airports. As airports are relatively differentiated, there are, however, some difficulties in identifying reasonably equivalent comparators. In addition, many airport operators are subject to economic regulation and their pricing is likely to be a reflection of the effectiveness of the regulatory regime under which they operate and may therefore bear little resemblance to prices that would be established under competitive conditions.
- D64 To further inform the CAA's understanding on price it commissioned Leigh Fisher (LF)<sup>37</sup> to undertake work on benchmarking airport charges at

---

<sup>36</sup> EE, Advice on the application of long run incremental cost estimates for Gatwick and Stansted.

<sup>37</sup> LF, Updated Final Report, Comparing and Capping Airport Charges at Regulated Airports, for the

Heathrow, Gatwick and Stansted, against suitable comparator airports, which where possible, were operating in a competitive market.

- D65 While LF's approach has been criticised (see appendix H), the CAA considers that the benchmarks used in this analysis are reasonable and can help inform the discussion of the competitive price at Stansted. LF's approach was to identify a set of suitable comparators for each airport based on a set of criteria (such as catchment size and traffic mix) which were important in determining similarities across airports. Suitable criteria and comparators were discussed with airline and airport stakeholders.
- D66 LF's analysis shows (including the revised analysis that was released following the release of the minded to Consultation), that STAL's aeronautical revenue per passenger is approximately £1 above the average of comparable airports and about £1.50 above the subset of airport operators that are subject to lighter regulation<sup>38</sup> LF estimated that the margin of error of the analysis was +/- 10 to 15 per cent (equivalent to £0.60 to £0.90).
- D67 As stated in the minded to Consultation *'overall this analysis appears to indicate that STAL's aeronautical charges are likely to be above the level of comparator airport operators. Given the margin of error it is difficult to be definitive about how much STAL is pricing above the competitive level.'*<sup>39</sup>

### Conclusion

- D68 Based on the analysis outlined above, the CAA considers that conducting its analysis on the basis of the regulated price level is reasonable. In particular, it is:
- Reliable, as it is based on a price that is calculated on an established regulatory methodology and is observed in practice by stakeholders (rather than the theoretical price determined by the benchmarking or a LRAIC-based model).
  - Reasonable and consistent with international practices (including by the EC).
- D69 The use of regulated priced is also robust. If the CAA used a LRAIC or the LF benchmark-based price for undertaking the SSNIP analysis the

---

Civil Aviation Authority, 19 April, 2013.

<sup>38</sup> The analysis also shows that STAL's aeronautical revenue per passenger was below the average at comparable airports over the period 2002 to 2007.

<sup>39</sup> Stansted Market Power Assessment: developing our 'minded to' position, p. 161



CAA would have to have conducted it using a price lower (by £1 to £1.50) than the current regulated price. As a result, there would have been a risk of defining a narrower geographical market definition than it currently has – possibly a market that would exclude Luton and/or Southend from the geographic market. In this narrower market, STAL's market share would be higher. Conversely, the CAA recognises that, given the differing estimates of costs and those which the CAA observes in the deals signed by the airlines, the use of the regulated price may be leading the CAA to conclude in favour of a wider market than it otherwise would have defined. However, even allowing for a margin or error, the use of a wider market does not undermine its assessment of STAL's market position in this case.

### Interdependence of demand from different user groups

- D70 The Guidelines state that airports can be viewed as platforms in a multi-sided market. In particular, the Guidelines state that account should be taken of any interactions and interdependencies between the various activities that the airport operator undertakes.
- D71 The extent to which conventional (one-sided) market definition methods need amending will depend on the strength of the interrelationships between the various activities and whether these form a genuine platform that brings together consumers and other service providers as different sides of the market.<sup>40</sup>
- D72 In deciding whether or not the market definition for STAL should be carried out using conventional methods or as part of a two-sided market, the CAA has adopted a pragmatic approach. That is, the CAA has adopted a conventional approach but has adapted its approach where it considers there are gains to be made in terms of clarity and robustness of analysis.
- D73 A multi-sided approach has not been taken previously by competition authorities with respect to airports, and there is little guidance on how to approach this issue in this sector.<sup>41</sup> However, the CAA considers a multi-sided market consists of a firm whose product acts as a platform through which it can actively bring together differing customer groups to generate revenue. The multi-sided market is formed due to demand interdependencies between the differing sides of the market. Therefore a true multi-sided market is one where the demand interdependencies are

---

<sup>40</sup> The Guidelines, paragraphs 3.18 to 3.26.

<sup>41</sup> Most recently, the CC's 2009 *BAA airports market investigation: A report on the supply of airport services by BAA in the UK*. Previous decisions by the EC: 95/364/EC, 1999/199/EC, 1999/198/EC; 98/513/EC; T-128/98; C-82/01 and 98/190/EC.

reciprocal. The price charged on one side of the market affects the demand on the other side and vice versa; the CAA refers to this phenomenon as network effects.

D74 The key characteristics of a multi-sided market, in the context of airports, has been set out in a paper prepared by independent consultants commissioned by the CAA in 2010 (referred to below as the SY criteria).<sup>42</sup>

- The airport is the platform and its operator can be viewed as having multiple revenue (and associated cost) streams, some of which are highly interrelated.
- Airlines and passengers are the two main groups that use the platform.
- An airport is more attractive to passengers the greater the number of airline services (more routes, greater frequencies, better connections) offered to and from that airport.
- An airport is more attractive to airlines the greater the number of passengers who might use that airport.
- In matching airlines to passengers, the airport operator takes account of the different demand conditions – on the one hand, the airline's demand for access to the airport and its facilities and, on the other, the demand of the passenger for services from the airport.
- If the airport operator is itself the provider of commercial services to passengers (retailing, car parks etc.), or has revenue sharing agreements included in its leases with commercial services providers, then the airport operator has a revenue stream from each of these two groups, and has to consider two sets of prices.

D75 The arguments outlined above fall into three categories:

- The existence of reciprocal demand effects between the different customer groups.
- Marketing activities carried out by the airport operator to attract passengers and airlines separately to the airport.
- The existence of a stream of commercial (non-aeronautical) revenue driven by passenger volumes.

D76 In the minded to Consultation,<sup>43</sup> the CAA did not consider that there were significant reciprocal demand effects present at STAL given:<sup>44</sup>

---

<sup>42</sup> David Starkie and George Yarrow 'Market definition in the airports sector', 1 July 2010, available at: <http://www.caa.co.uk/docs/5/ergdocs/MarketDefAirports.pdf>, p. 13.

- The previous owners of STAL (BAA) had stated that it did not market itself as a brand to passengers as its focus was on advertising to airlines.
- Views expressed by BAA at the time of the CC's review into the joint ownership of BAA airports which suggested that airports have limited levers with which to affect their passenger base.
- The airport operator has a limited direct commercial relationship with passengers.

D77 The CAA recognised<sup>45</sup> that there were complementarities between the airport operator's aeronautical and non-aeronautical revenue streams. As identified by S&Y, by affecting passenger volumes, aeronautical charges may affect the revenues that an airport operator can derive from commercial services. As such, an airport operator may take this into account when setting charges.

D78 However, the CAA was not convinced that commercial pricing affected either passenger demand for air transport services from the airport or airlines' demand of non-aeronautical services.

- There was no indication that complementarities in STAL's revenue streams had been taken into account in its aeronautical pricing decisions. In addition, it noted that while the regulation under which STAL is operated is applied on a single till basis, commercial revenues are forecast as an independent part of the price cap.
- STAL was insulated from changes in its passenger base due to minimum guarantees on income from its concessionaires, except car parking
- Ryanair's one bag rule suppressed demand for non-aeronautical services.

D79 Drawing this evidence together, the CAA considered that STAL did not strongly exhibit in practice the characteristics of a multi-sided platform. It considered it was apparent that the main relationship is vertical in nature, as the airport operator provides a key facilities input in the upstream market to airlines operating in the downstream air transport markets. The CAA did not therefore significantly modify the standard vertical approach to its market analysis.

---

<sup>43</sup> The minded to Consultation, paragraphs 4.9 to 4.10.

<sup>44</sup> In the minded to Consultation the CAA considered airline network effects as relevant to its consideration. It no longer considers that this has a material impact on its analysis of this issue.

<sup>45</sup> The minded to Consultation, paragraph 4.13.

*Stakeholders' views*

- D80 MAG, in its response to the minded to Consultation, suggested that the CAA had dismissed the consideration of the incentive effects that complementarities between aeronautical and non-aeronautical revenues have on the airport operator.<sup>46</sup> In particular, MAG considered that:
- The CAA had fundamentally misunderstood STAL's business as non-aeronautical revenues are central to its business and represented over 44 per cent of revenues in 2012.<sup>47</sup>
  - The CAA's adoption of a vertical approach had lead to the CAA departing from its current policy stance of the use of single till regulation.<sup>48</sup>
  - The CAA has misdirected itself in the application of the S&Y criteria.<sup>49</sup>
  - MAG has submitted additional evidence as to the development of its commercial offering to passengers. The aim of the development is to increase the retail yield per passenger. MAG also stated that this development does not need to be funded through higher airport charges to passenger airlines. This has a significant impact on MAG's incentive to increase passengers, limit spare capacity and should reduce MAG's incentive to increase airport charges.<sup>50</sup>
  - In its negotiations with [§<], it is actively [§<].<sup>51</sup> the CAA notes that STAL has been successful in this respect
- D81 The CAA did not receive representations on this issue from other stakeholders.

---

<sup>46</sup> MAG, Civil Aviation Authority Stansted Market Power Assessment; Interim response of M.A.G to the CAA's 'minded to' document 24 May 2013, paragraph 7.1.

<sup>47</sup> MAG, Civil Aviation Authority Stansted Market Power Assessment; Interim response of M.A.G to the CAA's 'minded to' document 24 May 2013, paragraph 7.2.

<sup>48</sup> MAG, Civil Aviation Authority Stansted Market Power Assessment; Interim response of M.A.G to the CAA's 'minded to' document 24 May 2013, paragraphs 7.3 to 7.5.

<sup>49</sup> MAG, Civil Aviation Authority Stansted Market Power Assessment; Interim response of M.A.G to the CAA's 'minded to' document 24 May 2013, paragraphs 7.6 to 7.7.

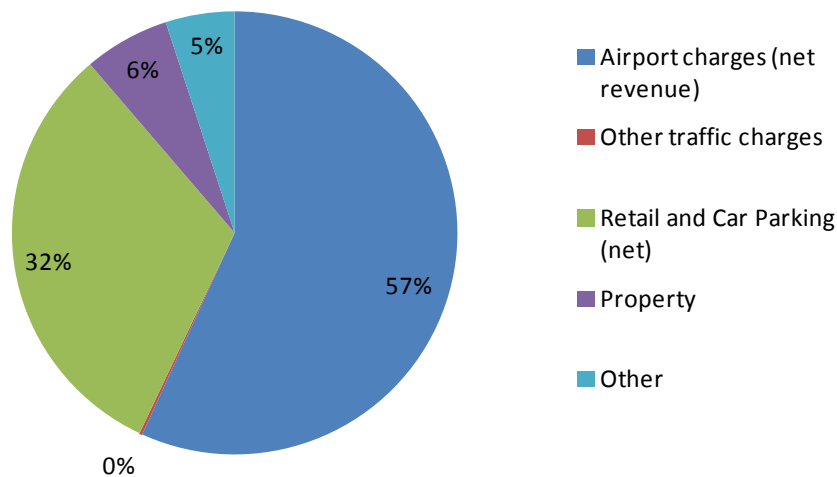
<sup>50</sup> MAG, Civil Aviation Authority Stansted Market Power Assessment; Interim response of M.A.G to the CAA's 'minded to' document 24 May 2013, paragraphs 7.11 to 7.12.

<sup>51</sup> MAG, Civil Aviation Authority Stansted Market Power Assessment; Interim response of M.A.G to the CAA's 'minded to' document 24 May 2013, paragraph 7.13.

### CAA views

D82 The CAA has used the SY criteria to help determine the changes it needs to make to a standard market definition approach. It has resisted simply excluding the standard approach on the basis that airports are evidently a platform that brings together at least three groups – airlines, concessionaries and passengers – without giving consideration to the possible strength of the interrelationships. Figure D.1 (below) highlights the significance of non-aeronautical revenue to the overall revenue of STAL.

**Figure D.1: Breakdown of STAL revenue by area (2012/13)**



Source: CAA analysis of STAL regulatory accounts

D83 The CAA does not consider that it has fundamentally misunderstood the business of STAL. In its analysis, the CAA recognised the importance of STAL's non-aeronautical revenue streams and modified its assessment accordingly. This included adapting the critical loss and price elasticity<sup>52</sup> analysis to account for the potential loss of non-aeronautical revenues from declining passenger numbers.

D84 The evidence also suggests that aeronautical charges affect non-aeronautical revenues. As higher aeronautical charges reduce demand by airlines, and passengers through higher fares, with fewer passengers there will be fewer shoppers and hence lower non-aeronautical revenues. However, the CAA has not seen evidence of the feedback loop or the network effects in the other direction to which MAG's response alludes.<sup>53</sup>

<sup>52</sup> See appendix F and paragraphs D## of this appendix.

<sup>53</sup> MAG, Civil Aviation Authority Stansted Market Power Assessment; Interim response of M.A.G to

- D85 The CAA would have altered its analytical approach where it was clear that there was feedback from the non-aeronautical side of the platform back to the aeronautical side. For example, the CAA has not seen evidence that a rise in non-aeronautical pricing would lead to a decline in passengers (and from that, a decline in aeronautical revenues) and, in turn, a decline in non-aeronautical revenues and so on.
- D86 In light of this lack of reciprocal demand effects, at least to an extent that is material and would justify the extra complexity of the multi-sided approach, the CAA considers that non-aeronautical revenue can merely be viewed and treated as complementary to the aeronautical revenue.
- D87 This position on the multi-sided nature of airports does not undermine the CAA's stance on the single till regulation of airport operators. The CAA has come to this conclusion based on the following reasons:<sup>54</sup>
- Its approach reflects the aeronautical pricing observed at airports actively competing for airlines' business where to gain passenger volume airport operators subsidise aeronautical charges with potential commercial revenues.
  - As a multi-product firm, regulation of a limited range of services may allow an operator with SMP to collect rents elsewhere. A single till limits the scope for such behaviour as all revenues are considered.
  - Single till regulation removes the need for subjective and resource intensive allocation of the costs of services that utilise the same infrastructure.
- D88 MAG's efforts to increase its non-aeronautical revenues will, all else being equal, increase STAL's sensitivity to changes in its passenger numbers. However, efforts to maximise non-aeronautical revenue need not affect the demand for the aeronautical products. This is demonstrated by STAL's terminal transformation programme, which all else being equal will of itself generate additional non-aeronautical revenues per passenger. This will make each passenger more valuable to STAL than was previously the case.
- D89 To ensure the robustness of its consideration on the use of the standard vertical approach to market definition the CAA commissioned Charles River Associates (CRA) to review the CAA's position and the response

---

the CAA's 'minded to' document 24 May 2013, Annex A.

<sup>54</sup> MAG, Civil Aviation Authority Stansted Market Power Assessment; Interim response of M.A.G to the CAA's 'minded to' document 24 May 2013, paragraph 7.6(g) and Annex A, p. 26.

received on this issue as part of the minded to Consultation process. The CRA report sets out<sup>55</sup>:

- There is no single definition of multi-sided market. Under differing definitions practically all markets can be considered to be multi-sided.
- Not all markets that have been identified as multi-sided require an adjustment from the standard approach; the analysis depends on the context of the market.
- Regardless of the structure of the analysis what is important is that it takes into account the possible multi-sided or complementarities present, which CRA concludes that the CAA has done.
- The arguments for single till regulation do not rely on the proposition that airports are two-sided markets.

D90 Based on the above, the CAA therefore considers that it is appropriate for it to analyse the markets in which STAL operates in a conventional vertical derived-demand framework. This view is consistent with the view the CAA outlined in the minded to Consultation

### **The role of airline and passenger switching in vertical derived demand analysis**

D91 Airlines' demand for airport operation services is derived from passengers' demand for air transport services. To assess derived demand, the CAA has considered both the direct and indirect impacts on the demand for airport services. The derived demand process is illustrated as follows.

- Following an increase in airport charges an airline makes the initial response to, broadly, either absorb the cost increase or to pass it onto its passengers and/or to switch some services to another airport.
- Should an airline remove some capacity, there will be a direct effect on the use of the airport, provided that the removal of this capacity does not trigger entry or expansion by another airline.
- Assuming that the airline maintains the same level of capacity at the airport, and passes the price increase onto its passengers, the passengers become indirectly exposed to the airport operator's pricing decision.

---

<sup>55</sup> Charles River Associates, Two-sided market analysis in the context of the CAA's Airport Market Power Assessments, November 2013, see:  
<http://www.caa.co.uk/docs/78/two%20sided%20markets.pdf>.



- To the extent that substitutes to that particular flight is available at other airports, passengers may then decide to switch to flights from other airports in response to the price rise thus affecting the level of derived demand.

- D92 As part of its response to the minded to Consultation, MAG criticised this approach as it considered that the CAA had focused on the wrong level in the supply chain. In particular, MAG considered that the CAA had considered the reactions of passengers rather than the airport operator's airline customers.<sup>56</sup> MAG also considered that downstream passenger markets were not relevant to the CAA's task.<sup>57</sup> The CAA does not agree with this assessment.
- D93 As it is primarily the airline that considers whether or not to provide services from a particular airport, the CAA considers that its market definition analysis should start with the evaluation of airlines' views of the substitutability of other airports for Stansted and, where possible, evidence on airlines' actual switching behaviour. The willingness of passengers to switch airports is a relevant consideration but is considered as a consequence of the airlines' initial decision.
- D94 Airlines' requirements regarding the infrastructure at an airport are also likely to differ according to their business model and the type of services that they offer. In turn, the business model and services may dictate the type of aircraft used, which might require special airport facilities.<sup>58</sup>
- D95 The Guidelines emphasise that the nature and magnitude of airlines' switching costs will depend upon a number of factors and are an important aspect of the overall competition assessment.<sup>59</sup> Thus, an airline's ability to switch to another airport is not just relevant for the product market definition but also for the definition of the relevant geographic market.<sup>60</sup>
- D96 In particular, the geographic market definition will be affected by the ability and willingness of passengers to switch between airports. For example, market definition will be affected by:

---

<sup>56</sup> MAG, Civil Aviation Authority Stansted Market Power Assessment; Interim response of M.A.G to the CAA's 'minded to' document 24 May 2013, paragraph 6.12.

<sup>57</sup> MAG, Civil Aviation Authority Stansted Market Power Assessment; Interim response of M.A.G to the CAA's 'minded to' document 24 May 2013, paragraph 6.13.

<sup>58</sup> The Guidelines, paragraph 3.41.

<sup>59</sup> The Guidelines, paragraph 3.42.

<sup>60</sup> The Guidelines, paragraph 3.65.

- The ability of passengers to respond to a price increase imposed by the airport operator is only derived if they are exposed to the price increase after the airline's initial response.
- The ability and willingness of passengers to switch will depend, in part, on the extent to which they regard services at different airports as reasonably close substitutes and the costs they face in switching demand to the next best alternative.<sup>61</sup>
- The availability of suitable alternative flights to the same destination as well as the willingness of passengers to follow an airline to an alternative airport.

D97 The Guidelines also highlight the importance of passenger switching for geographic market definition:

*... passenger switching is likely to be a significant focus of geographic market definition. However, it may also be important to consider the interdependencies with, or feedback effects from, the airport's other user groups.*

*Whilst geographic market definition might be focused on the potential for passengers to switch between airports, it will also be important to ensure that the ability of airlines to switch away from an airport – potentially to a relatively distant airport – is included within the wider assessment of competitive constraints... Assessing the likelihood that airlines and passengers take these choices, and the impact this would have on the airport in question, is at the core not only of the market definition but also of the assessment of the strength of competitive constraints an airport is facing.<sup>62</sup>*

D98 The CAA therefore considers that air transport markets are relevant to market definition for airport operation services. Where marginal passengers are clearly able to substitute in significant numbers between airports, this will reduce the costs involved in the switching for airlines. Where this is not the case, the costs of switching for airlines will likely be higher due to the additional opportunity cost of no longer serving that particular air transport market.

D99 In common with other authorities carrying out such analyses,<sup>63</sup> the CAA has sought to understand the propensity of marginal passengers'

<sup>61</sup> The Guidelines, paragraph 3.34.

<sup>62</sup> The Guidelines, paragraphs 3.60 and 3.61.

<sup>63</sup> See, for example, the CC's 2009 report into BAA.

likelihood to switch in response to a price rise. It has done this using passenger surveys and catchment area analysis.

D100 However, as part of the analysis of derived demand, the CAA considers that an airline, in making decisions on whether to switch or discontinue a service at an airport in response to a price rise, would have considered:

- The likely possible behaviour of their passengers in the air transport markets.
- Passengers' willingness to use other airports.

D101 It is therefore reasonable to assume that passengers' propensity to switch in response to a price rise by the airport operator has, to some extent, been internalised in the airline's decision-making process.

D102 Consequently, where airlines' decision-making processes are supported with primary evidence, e.g. an analysis of catchment overlaps developed for airport operators' and airlines' internal purposes, the CAA has attached weight to that evidence when delineating the boundaries of the geographic market. It has complemented this evidence with interviews with airlines and airport operators.

D103 However, airlines' propensity to switch may not be fully aligned with that of passengers, as they face different switching costs and constraints. In addition, relying solely on existing airlines' views and evidence may provide too static a view of the market. The CAA has therefore complemented airline and airport operator evidence with findings from its own research and analysis of passenger behaviour.

D104 Analysis in the Initial Views on the cost structure of airlines suggests that, for LCCs, the airport charges make up 10 to 30 per cent of their cost base.<sup>64</sup> The CAA considers that this suggests that a 5 to 10 per cent increase in airport charges, if passed on fully to passengers, may only translate, at most, into a 3 per cent increase in charges to the passenger.<sup>65</sup> Given the scale of the price change that may be faced by passengers it is unlikely that there will be significant marginal switching observed.

D105 In addition, passengers' choice of airports is part of a wider decision on air transport services, whether they are travelling for business or leisure. The impact of airport pricing on passengers is therefore likely to be

---

<sup>64</sup> Initial Views, paragraph 2.70 and Figure 3.

<sup>65</sup> For a long haul FSC, the CAA would expect that an airport operator SSNIP could represent less than a 1 per cent change in the overall ticket price for a passenger.

significantly lessened as it forms one component of a bundle of goods.<sup>66</sup> The CAA's view is, therefore, that marginal passenger responses to an airport operator's SSNIP are likely to be muted.

- D106 Given the derived demand approach, the CAA considers that it is appropriate consider the downstream air transport markets that operate from Stansted, based on the applicable case law.<sup>67</sup>

#### *Air transport markets*

- D107 Merger case law suggests<sup>68</sup> that airline competition takes place on a city-pair basis, which means competition takes place between airlines on routes between two cities and their surrounding areas i.e. London to Milan as a city pair forms a different market from London to Rome or London to New York. Therefore a London Luton to Paris Charles De Gaulle flight may compete with a London City to Paris Orly flight as both flights are serving the London to Paris market. Neither of those flights would compete with a London Heathrow to New York JFK flight. For long-haul services, such as transatlantic routes, indirect routes for which a single ticket is purchased that increase the journey time by no more than 150 minutes may impose a competitive constraint on direct flights.
- D108 This implies that a London airport (or indeed any airport) would be a wholesale input for a range of air transport markets that face varying degrees of competition. For example, on the London to Paris route there is a possibility to fly with 4 different airlines from 4 different airports<sup>69</sup>, plus on the London to Paris route it is possible that rail may provide a suitably close substitute. For London to Lodz (Poland), there is a choice of Ryanair from Stansted.<sup>70</sup>

<sup>66</sup> In this context a list, by no means exhaustive, that may be purchased includes surface access charges, flights, and hotels.

<sup>67</sup> The CAA has not undertaken formal analysis of the retail markets but considers the implications drawn from case law. Furthermore, the CAA does not comment on the market position enjoyed by any airline operating within the downstream air transport markets.

<sup>68</sup> See COMP/M.5440 Lufthansa/Austrian Airlines; COMP/M.5335 Lufthansa/SN Airholding; COMP/M.5364 Iberia/Vueling/Clickair; COMP/M.3280 Air France/KLM; COMP/M.3770 Lufthansa/Swiss; COMP/M.5747 Iberia/British Airways; COMP/M.6447 IAG/BMI.

<sup>69</sup> Review of available direct return flights with one airline departing London 10 January and returning the 14 January 2014 taken from skyscanner.com accessed 6 December 2013. Airlines include Air France, Air Berlin, British Airways and easyJet. Airports include Heathrow, London City, Luton, and Southend.

<sup>70</sup> Review of available direct return flights with one airline departing London 10 January and returning the 14 January 2014 taken from skyscanner.com accessed 6 December 2013.

- D109 Case law<sup>71</sup> also suggests that passengers can be segmented between time-sensitive and non-time-sensitive passengers.
- Time-sensitive passengers tend to travel for business purposes, require significant flexibility with their tickets (such as cost-free cancellation and modification of the time of departure) and tend to pay higher prices for this flexibility.
  - Non-time-sensitive customers travel predominantly for leisure purposes or to visit friends and relatives, book a long time in advance, do not require flexibility with their booking and are generally more price-sensitive.<sup>72</sup>
- D110 In the BA/AA/IB case<sup>73</sup>, the EC expressed that passengers could be segmented by cabin class, with business and first class services (premium passengers) forming a separate product to economy class services (non-premium passengers).
- D111 As for airport substitution, the EC commented that:
- In the BA/AA/IB case, for transatlantic routes, both supply- and demand-side substitution were insufficient to suggest that Heathrow belonged in the same market as the other four London airports (Gatwick, London City, Luton and Stansted).
  - In the Iberia/BA case, for routes between London and Barcelona and Madrid, that for non-time-sensitive passengers Heathrow, Gatwick and London City were considered to be substitutable.
- D112 In addition, for Iberia/BA, the EC stated that all five London airports may be substitutable due to surface access links and cheaper airfares than airports which are less conveniently located. The inclusion of Stansted and Luton was, however, left open as the EC did not consider that this would affect the analysis for the purposes of the case.
- D113 For time-sensitive passengers it is less clear whether Stansted and Luton should be included in any airport substitution analysis. For example:

---

<sup>71</sup> See COMP/M.5440 Lufthansa/Austrian Airlines; COMP/M.5335 Lufthansa/SN Airholding; COMP/M.5364-Iberia/Vueling/Clickair; COMP/M.3280 Air France/KLM; COMP/M.3770 Lufthansa/Swiss; COMP/M.5747 Iberia/British Airways.

<sup>72</sup> COMP/M.5747 Iberia/BA.

<sup>73</sup> COMP/39.596.

- In the IAG/BMI case the EC did not conclude on airport substitutability; it carried out its assessment at three levels: at the airport, at three airports, and at five airports.<sup>74</sup>
- In the Ryanair/Aer Lingus case,<sup>75</sup> the EC considered that the five London airports were substitutable for services between Dublin and London.
- The CC, in its recent consideration of Ryanair/Aer Lingus considered a similar substitutability.<sup>76</sup>

### Airline competition

D114 In a 2008 working paper the CC analysed airline yield data and found some evidence that BAA airports (Heathrow, Gatwick and Stansted) were substitutes for passengers. In that analysis, the CC considered that:

*It is not possible to estimate cross-price elasticities [faced by airports] directly: historical joint-ownership has prevented competition between the airports and so we observe only a few instances of switching behaviour by airlines. This means we must look to passenger willingness to substitute between airports in response to relative airfare changes instead to guide our view on incentives for airlines to switch in response to changes in relative airport charges<sup>77</sup>*

D115 To develop the CAA's view on air transport markets and what this may mean for the airport operation services market, it has reviewed data on easyJet route yield. In particular, the CAA has analysed easyJet route revenue and profitability data<sup>78</sup> to better understand the extent to which there is competition between airlines across the London airports and how passengers substitute between London airports.

D116 The results from this examination suggests that:

---

<sup>74</sup> COMP/M.6447 IAG/BMI.

<sup>75</sup> COMP/M.4439. Ryanair/Aer Lingus III case COMP M.6663 has recently been decided by the EC – case documentation not currently available.

<sup>76</sup> CC, Aer Lingus/Ryanair Provisional Findings Report, 3 June 2013.

<sup>77</sup> CC, Working paper on analysis of airline yield data, available at: [http://www.competitioncommission.org.uk/assets/competitioncommission/docs/pdf/inquiry/ref2007/airports/pdf/working\\_paper\\_airline\\_yield\\_data.pdf](http://www.competitioncommission.org.uk/assets/competitioncommission/docs/pdf/inquiry/ref2007/airports/pdf/working_paper_airline_yield_data.pdf).

<sup>78</sup> For the analysis, the CAA constructed a panel fixed effects model, matching easyJet route revenue to the CAA aviation statistics data. The CAA then regressed easyJet revenue against a number of capacity variables for London airports.

- One extra seat provided at another London airport to the same destination reduces easyJet revenue on a route between Stansted and the destination by about [3%].
- One extra seat provided at Stansted by another airline but to the same destination reduces easyJet revenue on that route by about [3%].
- Each of Heathrow, Gatwick and Luton seem to be constraining route revenue at Stansted, [3%].
- [3%].

D117 While the CAA has not estimated elasticities of demand from that analysis, as it recognised the limitation of doing so, it concludes that:

- There are signs of airline competition for passenger demand at and across London airports.
- Airline competition between routes at the airport seems to be stronger than competition from other London airports.
- [3%].
- Air services from different London airports may place different constraints on easyJet routes but it is difficult to say where from the constraint is bigger.

### Conclusions on air transport markets

D118 Based on the case law outlined and supported by the CAA's analysis above, the CAA notes of the following for its assessment:

- Airlines compete for passengers on a city-pair basis.
- Airports operate as a wholesale input to a number of air transport markets – the airport is either the origin or the destination.
- There is some level of substitutability between all London airports depending on the air transport market in question.
- Non-London airports are not substitutable for London airports at the downstream air transport level therefore by extension would not be at the upstream airport operation services level for passengers.

D119 However, case law on airline competition is based on a 5 to 10 per cent increase from the competitive price in the downstream air transport market. A SSNIP on air transport fares would equate to a 17 to 100 per cent increase in upstream airport operation service



charges.<sup>79</sup> At this level of price increase, substitutability between airports from a passenger perspective could be expected to be greater than that observed when passengers are exposed to a 5 to 10 per cent SSNIP on airport operation services alone.

### Section 3.2: Product market

D120 This section defines the product markets in which STAL provides services. In particular, this section covers:

- Competition with other transport modes.
- The service bundle.
- Retail, property and car parks.
- Market segmentation, paying particular attention to:
  - Inbound and based carriers.
  - Passenger segmentation.
  - Airline business models.

#### Competition with other modes of transport

D121 As discussed in the consideration of air transport markets (above), other transport modes may compete with airlines for some services, particularly for services that non-time-sensitive passengers may require. That said, only 7 per cent<sup>80</sup> of passengers that fly on services from Stansted do so on services that may be substitutable with surface journeys i.e., domestic routes and those European destinations served by high speed rail (Paris and Brussels).

D122 The CC, in its BAA airports market investigation, did not consider that there was sufficient scope for surface substitutability at the London airports.<sup>81</sup>

D123 Based on the above, the CAA does not therefore consider it expeditious to the current investigation to consider this issue further. The markets considered within this document reflect this thinking and are not widened to include surface journey alternatives.

---

<sup>79</sup> This calculation assumes that charges levied by the airport operator account for 10 to 30 per cent of the airlines' cost base.

<sup>80</sup> Source: CAA analysis.

<sup>81</sup> CC Report 2009, paragraph 2.11.

## Service bundle

- D124 STAL provides a number of products and service (which may be interlinked) to airlines, passengers, freight operators and a range of other companies (groundhandlers, retail concessionaires etc) for the use of the infrastructure at Stansted.
- D125 For the market definition, it is therefore important to identify the focal product, or service that is being provided by an airport operator. However, given the nature of an airport, it is more appropriate to analyse the focal product market in terms of a service bundle rather than individual products or services.
- D126 This approach is consistent with the approach adopted by the CC in its consideration of market definition for the BAA airports market reference.<sup>82</sup>
- D127 The CA Act provides a logical starting point for defining the service bundle. In particular, section 3 of the CA Act prohibits an operator of a dominant airport area at a dominant airport from requiring the payment of charges in respect of airport operation services unless it has a licence. An airport area will be dominant if the CAA has made and published a Determination that the market power test in section 6 of the CA Act is met in relation to that area.<sup>83</sup>
- D128 Section 66 of the CA Act states that an airport:
- means an aerodrome within the meaning of the Civil Aviation Act 1982<sup>84</sup> together with other land, buildings and structures used for the purposes of—*
- (a) the landing and taking off of aircraft at the aerodrome,*
- (b) the manoeuvring, parking or servicing of aircraft between landing and take-off at the aerodrome,*

---

<sup>82</sup> Indeed the CC's analysis highlights that where secondary products (i.e. aircraft parking fees and check-in) are considered as primary and secondary products, as the CC did. For clarity, the CAA considers them as a whole.

<sup>83</sup> Section 5(1) of the CA Act. An airport will be dominant if all or part of its core area is a dominant area.

<sup>84</sup> At section 105 of the Civil Aviation Act 1982 aerodrome means any area of land or water designed, equipped, set apart or commonly used for affording facilities for the landing and departure of aircraft and includes any area or space, whether on the ground, on the roof of a building or elsewhere, which is designed, equipped or set apart for affording facilities for the landing and departure of aircraft capable of descending or climbing vertically. In its narrowest interpretation an aerodrome can be considered as the runway.

*(c) the arrival or departure of persons carried or to be carried as passengers by air transport services operating to or from the aerodrome, together with their baggage,*

*(d) the arrival or departure of cargo carried or to be carried by such service(s)*

*(e) the processing of such persons, baggage and cargo between their arrival and departure, and*

*(f) the arrival or departure of persons who work at the airport.<sup>85</sup>*

D129 The definition of airport operation services does not include air transport services, air traffic services (ATS) or services provided in shops and other retail businesses.<sup>86</sup>

D130 This definition also feeds into section 6(1) of the CA Act which sets out the market power test must be applied in relation to an airport area. In addition, under section 5(3) an airport area is defined as '*an area that consists of or forms part of an airport*'.

D131 The market power test will be met in relation to the airport area if Tests A, B and C are met by the relevant operator of the airport area at that time. The relevant operator is the person that has overall responsibility for that area by controlling, to some extent, the type, quality, or price of services provided from that area or the access to and development of that area<sup>87</sup>.

D132 Section 6(3) of the CA Act sets out Test A, i.e. whether the relevant operator has, or is likely to acquire, SMP. In particular, section 6(3), read in conjunction with sections 6(6) and 6(7), requires that an SMP assessment must be made by reference to a market for one or more airport operation services which are provided in the airport area or, where appropriate, the core area.<sup>88</sup>

D133 The core area is defined in section 5(4) of the CA Act as:

*(a) the land, buildings and other structures used for the purposes of the landing, taking off, manoeuvring, parking and servicing of aircraft at the airport,*

<sup>85</sup> The definition of airport specifically excludes hotels (except those situated in a passenger terminal that is part of the airport), bus, tram and railway stations.

<sup>86</sup> Section 68(4).

<sup>87</sup> Section 9(4) of the CA Act.

<sup>88</sup> Section 6(7) provides that, where the airport area includes all or part of the core area, the SMP test will be applied by reference to a market for airport operation services provided in the core area.

*(b) the passenger terminals, and*

*(c) the cargo processing areas.*

- D134 Based on the above, the initial focal product is likely to consist of one or more of the airport operation services supplied in the core area defined.
- D135 However, STAL's primary function is to provide access to the infrastructure of Stansted for the landing, parking and departure of aircraft and the processing of passengers and cargo.
- D136 The CAA therefore considers that the airport operation services provided by STAL at Stansted are likely to consist of at least:
- the use of the runway and taxiways;
  - aerodrome Air Traffic Control (ATC)<sup>89</sup>;
  - aircraft parking;
  - the provision of access and infrastructure needed for the provision of airside and landside groundhandling services.<sup>90</sup>
  - the provision of facilities for check-in;
  - the provision of facilities baggage handling;
  - security screening;
  - the provision of access and facilities for holding passengers between arriving at the airport and departure (holding passenger facilities);

---

<sup>89</sup> Aircraft landing at Stansted will only face charges from the airport operator for the aerodrome element of ATC. The approach service is provided by NATS (en route) Plc as part of the London terminal manoeuvring area (LTMA) and charged directly to airlines operating in this space. At airports outside of the LTMA, the approach service would be included within this bundle of activities. However, the CA Act formally excludes ATS as defined in the Transport Act 2000 from airport operation services. In addition, the ability to land and manoeuvre aircraft at and around an airport is a key service that airport operators are required to provide as part of its services to airlines. In the UK these services are currently contracted by the airport operator with an air navigation service provider in a liberalised market. It is then up to the airport operator how they recover this cost in a similar manner to any other costs incurred, it is not a 'pass through' cost.

<sup>90</sup> Ramp handling services, fuel and oil handling, and aircraft maintenance are groundhandling services as defined in Directive 96/67/EC. Groundhandling services are often provided by the airlines or to the airlines by third parties. However, the groundhandlers pay fees to the airport operator relating to use and access to infrastructure. In these cases the airport charges would still affect the airline through the charges levied on the groundhandlers.

- facilities for the processing of airline staff arriving and departing the airport<sup>91</sup> (airline staff processing facilities); and
  - the transit of passengers to and from the aircraft (in the case of a passenger airline) (passenger transit facilities).
- D137 For ease of reference, the CAA refers to these services as bundle A.
- D138 In addition, for certain airlines, such as those operating as FSCs, the airport operation services are also likely to include.
- access to infrastructure and facilities for the provision of such as lounges and priority security lanes for premium passengers (premium passenger facilities).
  - access to facilities to transfer connecting passengers and their baggage between aircraft without the passenger leaving the airport (integrated transfer facilities).
- D139 For ease of reference, the CAA refers to these services as bundle B.
- D140 The CAA considers that bundles A and B services should be treated as a single product as:
- These services are likely to form the key bundle of services that an airline would require to operate from an airport.
  - An airline would be required to bear the costs of all of these services to provide air transport services.<sup>92</sup>
  - In deciding whether to land at an airport, an airline would take account of the total bundle of charges rather than focusing on any one charge in isolation (even though services may be priced individually by the airport operator to reflect different cost drivers).
- D141 Although an airport operator may not directly supply each individual service identified above, it may have a degree of management control or influence over the services provided, for example, by determining the

---

<sup>91</sup> Given the legislative definitions, staff may never “arrive” at an airport if they do not enter through a passenger terminal, pass the forecourt of such a terminal, or use a qualifying car park. Nevertheless, the CAA considers that staff access costs would be a consideration as part of an airline’s decision to operate from an airport.

<sup>92</sup> Air transport services are defined in the CA Act as a service for the carriage by air of passengers or cargo to or from an airport.

quality and prices of such services through contracting out or licensing access.<sup>93</sup>

### **Retail, property and car parks**

D142 This section briefly outlines the CAA's approach to the retail, property and car park activities that are not included in the service bundle set out above. This includes the services outlined in sections 68(3)(b)-(c) of the CA Act:

*(b) facilities for car parking, and*

*(c) facilities for shops and other retail businesses.*

D143 In relation to the provision of facilities for retail and car park (RCP) and following the discussion outlined above on the multi-sided nature of airports, the CAA would need to be assured that the services in the airport operation services product market and RCP services are interdependent<sup>94</sup> for them to be in the same market.

D144 Although RCP services would not be offered if the airport operator did not provide services to commercial passenger airlines, in principle, an airport could operate without the provision of facilities for retail activities.

D145 In addition, although some passengers may take into account the retail offering and/or prices of products sold at an airport when making a decision on the airline/airport they will use, evidence suggests that this varies across different passenger groups, and expectations vary by airport.<sup>95</sup> As the CAA highlighted in the minded to Consultation, 'all shoppers are fliers, but not all fliers shop'.<sup>96</sup>

D146 In practice, the price for retail activities is unlikely to affect passengers' choice of an airline or airport in a significant way. Furthermore, in considering how to respond to an increase in rent and/or change to other terms of their contracts, concessionaires' decisions are likely to be

<sup>93</sup> Section 9(4) of the CA Act.

<sup>94</sup> In this context, the CAA defined interdependent such that an increase (decrease) in the price to one set of customers impacts on the demand from another set of customers and vice versa. It is not enough for the pricing on just one side of the market to have an impact on the other. Interdependence requires reciprocation.

<sup>95</sup> *Understanding Airport Passenger Experience*, Independent Social Research on behalf of the DfT, March 2009: <http://webarchive.nationalarchives.gov.uk/+http://www.dft.gov.uk/pgr/aviation/airports/reviewregulation/understandingexperience.pdf>; and Consumer Research, Accent for CAA, May 2011: <http://www.caa.co.uk/docs/2107/2131ConsumerResearch06122011.pdf>.

<sup>96</sup> The minded to Consultation, paragraph 4.30.

independent from decisions made by airlines in relation to airport operation services demanded. Likewise, airlines' decision making and profitability is independent of that of RCP concessionaires'.

- D147 The CAA's current view is therefore that in examining the existence and extent of STAL's market power, it is appropriate to define a separate market for the provision of facilities for RCP that is distinct from that of the airport operation services product market. This approach is consistent with the approach adopted by the CC with respect to RCP<sup>97</sup>, as well as previous case law<sup>98</sup>.
- D148 Based on the above, the CAA does not therefore consider it necessary to define this distinct market in more detail.

### Market segmentation

- D149 This section considers the available evidence on whether it is appropriate to segregate the product market due to differences in demand from the airport's customer base.

### Inbound and based operators

- D150 In the minded to Consultation, the CAA considered that it was not appropriate to segment the market between inbound and based carriers as:<sup>99</sup>
- The product demanded by based and inbound airlines appears sufficiently similar. This is in terms of the product bundle and requirements of access to the airport.<sup>100</sup>
  - It appears that the competitive options are similar for those of both operations.<sup>101</sup>
- D151 No representations regarding the CAA's consideration not to segment the market by whether an aircraft was operated as inbound or based services were received.

---

<sup>97</sup> CC 2009 report, paragraph 2.41.

<sup>98</sup> In *Purple Parking v HAL* [2011] EWHC 987 (Ch) at paragraphs 109-131, the High Court distinguished the upstream "Facilities Market" (i.e. the provision of access to Heathrow's facilities) from the downstream "Parking Market" (parking services at Heathrow, including off-airport park and ride parking).

<sup>99</sup> The minded to Consultation, paragraph 4.52.

<sup>100</sup> The minded to Consultation, paragraphs 4.49 and 4.51.

<sup>101</sup> The minded to Consultation, paragraph 4.50.

D152 The CAA therefore concludes that it would be inappropriate to segment the market by whether airlines operate inbound or based services from the airport.

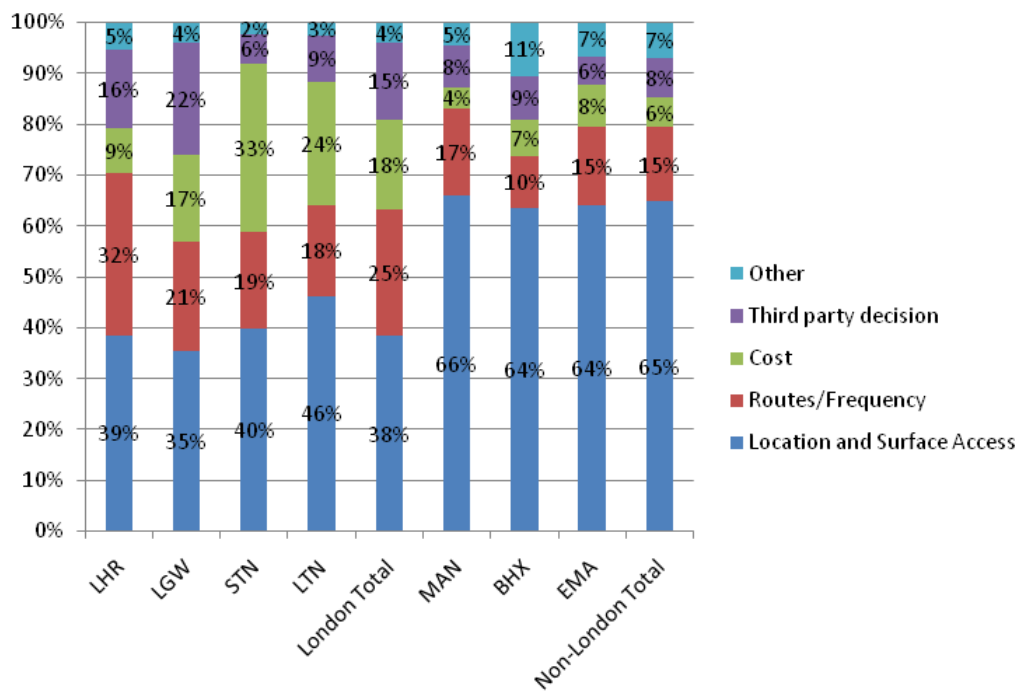
**Passenger segmentation**

D153 There are a number of segmentations of the passenger base that could be considered as candidates for segmenting the product market for airport operation services, including:

- Surface and transfer passengers.
- Business, leisure and visiting friends and relatives (VFR) passengers.

D154 Figure D.2 (below) shows passengers' reasons for their airport choice which could be considered as aspects of the airport product for passengers.

**Figure D.2: Reasons for airport choice**



Source: CAA Passenger Survey Working paper November 2011

D155 Figure D.2 shows that location and surface access is the primary driver and that a third party decision (such as by an employer or other family member), was the second most cited reason of choice. Routes/frequency was the third most cited reason.

D156 The CAA considers that the factors passengers cite as their reasons for airport choice are, in the main, outside of the influence of the airport over



the short to medium term, for example, location and surface access after their construction.

- D157 To some extent, surface access can be altered. However, this can take a considerable time for any modifications to come on stream<sup>102</sup> Although an airport operator may have some influence on cost, through airport charges, these are a small part of the overall fare. Routes/frequency (and to a certain extent third party decision where it is a business account), can only be impacted indirectly by an airport operator's engagement with airlines.
- D158 The CAA considers that it would not be possible for an airport operator to identify with accuracy differing passenger groups, nor to prevent arbitrage by passengers that would reduce the possibility of price discrimination.
- D159 However, in aggregate, the CAA considers that passengers' demand influences the services offered by airlines, which in turn impacts on the airline's demand for airport operation services. Through the purchase of an airfare, passengers also self-select and reveal information about their preferences, on which an airport operator may be able to discriminate through charges on airlines.
- D160 The CAA does not therefore consider it is appropriate to segregate the product market by passenger groups. However, passenger switching is considered in more detail with respect to the geographic market, where passengers' switching between similar services at differing airports is likely to affect the geographic scope of the market.

### Airline business model

- D161 In the minded to Consultation, the CAA concluded that the market could be segmented by airline business model, with separate product markets for LCCs and charter airlines, and for FSC and associated feeder traffic.<sup>103</sup>
- D162 The CAA received a number of responses on this issue from BA, easyJet, GAL and MAG. All these responses suggested that the CAA had:
- Misinterpreted the available evidence and placed too much weight on differentiation in services between the two main carrier types.<sup>104</sup>

---

<sup>102</sup> For example, the development of Crossrail began in 2001 receiving full support from Parliament in 2008. When Crossrail opens in 2018 it is expected to bring four trains an hour to Heathrow. See: <http://www.crossrail.co.uk/>, (accessed 2 April 2013).

<sup>103</sup> The minded to Consultation, paragraph 4.44

<sup>104</sup> MAG, Civil Aviation Authority Stansted Market Power Assessment; Interim response of M.A.G to

- Not given sufficient weight to the competition between the differing types of carrier, especially on short-haul routes.<sup>105</sup>

D163 Having considered the evidence, including that submitted in response to the minded to Consultation, the CAA now considers that it is unlikely that the identification of separate markets, segmented by airline business model is appropriate. In reaching this conclusion the CAA is, however, mindful that:

- There are still significant operational differences between LCCs and FSCs that impact on their substitution opportunities.
- Unlike Gatwick, the traffic at Stansted is highly polarised towards the provision of services to LCCs. This will be a consideration when considering marginal switching that may occur from the airport.

D164 In reaching this view the CAA has considered the following key features of the different airline business models:

- The LCC business model has a number of key features, including:
  - LCCs require quick turnaround times and minimal use of airport facilities.
  - The LCC model is based on all customers using the same basic service without differentiation and the airline maximising the usage of its assets through a high number of rotations.
  - Uniformity in fleet to drive down asset operation costs.
  - There is no ability to interline in an integrated manner.<sup>106</sup>
- The FSC business model also has a number of distinct features, including:

---

the CAA's 'minded to' document 24 May 2013; GAL, CAA's Gatwick Market Power Assessment: Response from Gatwick Airport Limited, reference Q5-050-LGW60, 26 July 2013, easyJet, easyJet response to CAA consultation on Gatwick airport market power, July 2013, BA, BA Response to CAA consultation on Gatwick market power assessment of May 2013, 26 July 2013.

<sup>105</sup> MAG, Civil Aviation Authority Stansted Market Power Assessment; Interim response of M.A.G to the CAA's 'minded to' document 24 May 2013; GAL, CAA's Gatwick Market Power Assessment: Response from Gatwick Airport Limited, reference Q5-050-LGW60, 26 July 2013, easyJet, easyJet response to CAA consultation on Gatwick airport market power, July 2013, BA, BA Response to CAA consultation on Gatwick market power assessment of May 2013, 26 July 2013.

<sup>106</sup> It is possible to self connect with LCCs (as with FSCs) by buying an extra ticket. However, this requires no additional airport infrastructure as the passenger arrives at the airport to go through the entire departure process again. This takes place in the same manner as a passenger arriving at the airport by car or train.

- The provision of differentiated services to a differentiated passenger base (premium and non-premium passengers).
- Requirements for higher specification of airport facility to cater for premium and non-premium passengers separately.
- Integrated transfer for connecting passengers.
- Carrying of bellyhold cargo.
- Greater fleet diversity to cater for both long and short haul services.

D165 Given the above, the CAA considers that for LCCs there is no reliance on additional traffic transferring at the airport or sophisticated transfer baggage systems (a position not shared with their full service counterparts). Given the fleet types employed by the LCCs and the focus on short haul destinations<sup>107</sup>, some may also have lower requirements on airport infrastructure in terms of runway length. The CC made similar observations with regards to LCCs' use of airport infrastructure:

*The requirement of such carriers for airport facilities is also significantly different from that of the more traditional carriers; in particular, a need for rapid and reliable turnaround times (of no more than 25 minutes) to allow three or more rotations of aircraft each day; and no requirement for facilities such as airbridges or facilities for transfer passengers or their baggage.*<sup>108</sup>

D166 BA similarly noted with respect to the segmentation posed by the CAA:

*...is artificial and an unclear and arbitrary basis on which to frame the market power assessment. In fact, the distinction between these airline concepts and what each one might need when it comes to airport services is increasingly blurred.*<sup>109</sup>

D167 BA also noted that traditional FSCs and LCCs fiercely compete to provide services to passengers.<sup>110</sup> To illustrate this, BA listed 26 short-haul and five long-haul routes from Gatwick in which they are in direct competition with LCCs and charters.

<sup>107</sup> Just over half of short-haul services in the UK are provided by LCCs. In 2011, CAA airport statistics show that 54 per cent of passenger flew short-haul with a LCC.

<sup>108</sup> CC, BAA Report (2009), paragraph 3.10.

<sup>109</sup> BA, BA Response to CAA consultation on Gatwick market power assessment of May 2013, 26 July 2013 paragraph 2.1.

<sup>110</sup> BA, BA Response to CAA consultation on Gatwick market power assessment of May 2013, 26 July 2013 paragraph 2.2.

- D168 On convergence of business models, BA has also stated that LCCs are continually seeking to provide services to more corporate customers. For example, BA highlighted evidence on easyJet's moves to provide these services to corporate customers.<sup>111</sup> In particular, it was highlighted that recent investor presentations from easyJet state its approach to targeting corporate passengers by:<sup>112</sup>
- deploying flexible fares;
  - connecting to primary airports; and
  - developing business friendly routes.
- D169 BA also highlighted evidence from the CAA, including:
- Passenger survey data, showing 17 per cent of easyJet's passengers are travelling on business routes.
  - The CAA's considerations in the Moscow scarce capacity decision, which discussed easyJet's ability to service passengers travelling on business.
- D170 In addition, BA outlined developments within its own business model and that of other airlines within the IAG group. For example, it noted that:
- BA's core cost basis is at LCC levels at Gatwick.<sup>113</sup>
  - BA's recent launch of a low priced product targeting LCC passengers, with hand baggage only and no interlining.<sup>114</sup>
  - Growth of feeder traffic at Gatwick is not a strategic priority for BA; its primary focus is point-to-point competition. The Gatwick schedule is not optimised for connection.<sup>115</sup>

---

<sup>111</sup> BA, BA Response to CAA consultation on Gatwick market power assessment of May 2013, 26 July 2013 paragraph 2.4.

<sup>112</sup> BA, BA Response to CAA consultation on Gatwick market power assessment of May 2013, 26 July 2013 paragraphs 2.3 to 2.4.

<sup>113</sup> BA, BA Response to CAA consultation on Gatwick market power assessment of May 2013, 26 July 2013 paragraph 2.5.

<sup>114</sup> BA, BA Response to CAA consultation on Gatwick market power assessment of May 2013, 26 July 2013 paragraph 2.5.

<sup>115</sup> BA, BA Response to CAA consultation on Gatwick market power assessment of May 2013, 26 July 2013 paragraph 2.11.

- Vueling, traditionally operated as a LCC but it is increasingly offering differentiated services such as the 'Vueling Business Pass'. Also BA notes it interlines with Vueling at Barcelona.<sup>116</sup>
- D171 BA further presented evidence relating to the facilities used by airlines.
- LCCs are increasingly using larger aircraft. It noted, for example, easyJet's deployment of A320s Norwegian Air Shuttle's use of B787 on intra-European routes and Thomson Airways' planned deployment of B787s on long haul routes from Gatwick.<sup>117</sup>
  - LCC method of operation focusing on speed of turnaround is likely to require additional and more intensive use of airport infrastructure at the ramp.<sup>118</sup>
- D172 In its response to the minded to Consultation, easyJet considered that the segmentation presented by the CAA was not helpful and that more enduring differences between airline business models is generally whether they offer a point-to-point or a network product. It noted that while there are differences in the airport infrastructure requirements, at Gatwick no such differentiation is present.<sup>119</sup>
- D173 Furthermore, easyJet considered that there are airports that provide services to FSCs without the need for passengers connecting, providing the example of EI AL operating to Luton.<sup>120</sup>
- D174 The CAA is aware that the evidence presented above has been given in respect to operations at Gatwick rather than to operations at Stansted. The CAA has already highlighted the significant LCC presence at Stansted. However, it is also aware that STAL is actively seeking to develop the airport with different airline business models. The CAA considers that where there is on-airport competition between airlines the possible passenger arbitrage is likely to limit the airport operators ability to price discriminate based on airlines' business models.
- D175 Given the evidence outlined above, the CAA considers that there are differences in the demand from airlines purchasing bundle A and those

---

<sup>116</sup> BA, BA Response to CAA consultation on Gatwick market power assessment of May 2013, 26 July 2013 paragraph 2.7.

<sup>117</sup> BA, BA Response to CAA consultation on Gatwick market power assessment of May 2013, 26 July 2013 paragraph 2.10.

<sup>118</sup> BA, BA Response to CAA consultation on Gatwick market power assessment of May 2013, 26 July 2013 paragraph 2.8.

<sup>119</sup> easyJet, easyJet response to CAA consultation on Gatwick airport market power, July 2013.

<sup>120</sup> easyJet, easyJet response to CAA consultation on Gatwick airport market power, July 2013.

purchasing bundles A and B. However, it does not consider this is sufficient to delineate different markets at Stansted.

- D176 The CAA therefore considers that it is unlikely that the product market for airport operation services defined as containing at least the services outlined in bundle A and for some airlines in addition at least those services outlined in bundle B should be segmented by airline business model.

### Supply side substitution

- D177 As well as considering demand side substitution, the CAA needs to consider issues relating to the supply of services by airport operators.

- D178 In response to the minded to Consultation, MAG criticised the CAA's assessment of supply substitutability and that the CAA had excluded airports such as London City. It also suggested that the analysis should not be limited to substitution by other airports but also by Stansted itself.<sup>121</sup>

- D179 For supply side substitution, the capacity available and the services offered by STAL are somewhat irrelevant. With supply side substitution, the question that needs to be asked is whether the other airport operators (providers) that are present can modify their operation sufficiently such that it could provide airport operation services that would be substitutable for those available at Stansted.

- D180 As set out in the Guidelines, supply side substitutability is the ability of an alternative airport operator to enter the market at short notice and provide services in competition with the current provider(s) without incurring substantial sunk costs.<sup>122</sup>

- D181 In addition to (or as an alternative to), new entry, an existing airport operator could also expand or develop its current offering to compete with STAL. If alternative operators can effectively provide additional capacity in the short term (i.e. less than one year), this may discipline STAL's pricing behaviour.

- D182 There are a number of ways in which supply side substitution could occur.

- Conversion of a military airfield to civilian use.

---

<sup>121</sup> MAG, Civil Aviation Authority Stansted Market Power Assessment; Interim response of M.A.G to the CAA's 'minded to' document 24 May 2013 6.20 to 6.22.

<sup>122</sup> The Guidelines, paragraphs 3.56 to 3.58; see also OFT 403, paragraphs 3.12 to 3.18 and EC Market Definition Notice, paragraphs 20 to 23. The CAA refers here to sunk costs specifically as costs incurred in entering the market that are not recoverable on market exit.

- Investment in infrastructure at a current general aviation airport to allow the use of commercial passenger flights.
  - A commercial airport improving its current infrastructure to accommodate larger aircraft.
- D183 However, the amount of investment needed in any of these scenarios (and any other) will depend on a number of factors as there are many constraints on the type and volume of traffic that an airport can handle.
- D184 Investment in a runway extension (or other airport infrastructure), can be a complex and resource intensive exercise. While the precise costs and practicalities of any such development are likely to depend on the location of an airport and the technical nature of the project, some of the challenges associated with such a project may include:
- significant capital and resource cost for the airport operator;
  - local and possible national planning restrictions;<sup>123</sup> and
  - potentially physical restrictions that are site specific.
- D185 It is likely that substantial investment costs involved in supply side substitution would be of a level that would rule it out as a short-term response to direct airport competition. In addition, due to planning restrictions and other constraints, entry or expansion is not likely to occur within a reasonable time period. Furthermore, it would not be rational for the CAA to consider that airlines may alter their fleets as a response to airport charges. This is especially true for LCCs where fleet uniformity is one of their key cost reduction strategies.
- D186 The CAA's analysis also suggests that airports can provide services for a range of aircraft size and provide airport operation services from both bundles A and B. While it is not necessary for an airport operator to be able to provide services to every aircraft type to be able to compete, the CAA does consider it necessary to be able to provide services over a sufficient range of aircraft types.

---

<sup>123</sup> For example, there is currently a Government moratorium on airport expansion at Heathrow, Gatwick and Stansted.



### Conclusion on product market definition

- D187 The CAA does not consider it is appropriate to segregate the product market by reference to based and inbound carriers or passenger groups.
- D188 With respect to airline business model, it is unclear as to whether the market should be segmented. There is a significant body of evidence to suggest there are differing demand conditions resulting from the differing airline business models. However, evidence presented as a result of the consultation on the closeness of competition between the airline business models and the fact that STAL has the facilities to provide services to both suggests that although these differences do exist, there is not a clear line, through which to segment the market. Both MAG and GAL agree on this point as well as easyJet and BA.
- D189 BA has submitted substantial evidence suggesting that at Gatwick its operations are akin in operational terms to those of a LCC. Likewise evidence from both easyJet and BA suggest that they are targeting an increasingly similar client base at Gatwick. It is clear that where there is on-airport competition between airlines that segmentation by business model becomes less clear. This is not the case at Stansted where the traffic is polarised to services offered to LCC. It is however likely that a similar result may occur, as seen at Gatwick, if a FSC carrier were to enter Stansted and offer similar routes to its incumbent LCCs.
- D190 easyJet has also suggested that segmentation by point-to-point and networked operations is an enduring segmentation. Although this maybe the case, in light of the evidence it is unclear how this would affect the market definition analysis at Stansted as the point to point or networked operation is highly specific to an airline and airport context. For example, BA operates a hub operation at Heathrow but not at Gatwick, similarly Emirates operates a spoke operation at Gatwick fulfilling origin and destination (O&D) demand into Dubai where it operates a hub.
- D191 It is also unclear whether a long haul versus short haul segregation would be appropriate, given the difficulties associated with drawing a line between the two services. This is especially the case as long-haul capable aircraft are being used for intra EU, typically short-haul, flying.
- D192 It would also not be rational for an airline to alter its business model at an individual airport in response to the 5 to 10 per cent price rise by an individual airport operator. Intuitively the costs of doing so are likely to be prohibitive. However, it is credible that there could be sufficient marginal passengers at Stansted such that an attempt by an airport operator to impose a SSNIP on a particular business model may be unprofitable given the ability of the passenger to arbitrage.



- D193 It may be possible for a SSNIP to be imposed on short-haul operators as there is unlikely to be sufficient passenger arbitrage (as the air transport services by their nature would not be substitutable). However, it is not clear where a dividing line may sensibly occur, and the CAA does not consider it is appropriate to define markets for airport operation services based on individual routes.
- D194 Based on the above, the CAA does not therefore consider it necessary to provide a definitive segregation of the market, especially given the lack of firm evidence on either side. The CAA concludes that there is likely a singular product market at Stansted that is likely to consist of at least the following services to all airlines:
- the use of the runway and taxiways;
  - aerodrome ATC;
  - aircraft parking;
  - the provision of access and infrastructure needed for the provision of airside and landside groundhandling services;
  - the provision of facilities for check-in;
  - the provision of facilities baggage handling;
  - security screening;
  - holding passenger facilities;
  - airline staff processing facilities; and
  - passenger transit facilities.
- D195 Some airlines may demand the following services at the airport in addition to those listed above:
- premium passenger facilities; and
  - integrated transfer facilities.
- D196 In defining a wider market there are likely to be a number of market segments where groups of airlines face significantly differing competitive conditions. The CAA has considered these differences in its geographical definition and its overall assessment of market power.

## Section 3.3: Geographic market

---

### Minded to consultation

- D197 In the minded to Consultation, the CAA considered there were two geographic markets in which STAL operated – one market for each of the product markets that it had defined:<sup>124</sup>
- LCC and charter market, which extended to Luton, Southend and possibly Gatwick; and
  - FSC and associated feeder traffic market, which was likely to include at least the services provided at Gatwick and Heathrow.

### Stakeholders' views

- D198 In its response to the minded to Consultation, MAG criticised the CAA for:
- Being inconsistent with its previous regulatory statements (in particular the CAA's de-designation proposal) as well as its statements to the CC in the 2009 BAA inquiry.
  - Ignoring the constraint posed by European airports, noting that STAL could not have SMP as it is a small player in a fragmented pan-European market.
  - Defining Gatwick, Heathrow and Stansted as being in separate geographic markets and ignoring constraints from other London airports.
- D199 Other stakeholders did not comment on the scope of the CAA's proposed geographic markets.

### CAA's views and conclusion

- D200 Since the release of the minded to Consultation the CAA has considered the product markets in which STAL operates and has changed its view. The evidence, including that submitted by stakeholders, now suggests that the CAA's analysis should be undertaken based on a unified product market definition (see section 3.2). This has implications for the CAA's consideration of the geographic market.
- D201 This section considers the evidence for the geographic market definition of the service provided by STAL and covers:
- European markets.

---

<sup>124</sup> The minded to Consultation, paragraphs 4.164 to 4.165.

- Airport operators' views.
- Airline evidence.
- Passenger switching.

D202 For the reasons explained above (paragraphs ##), the CAA maintains its position that it is appropriate to look first, at airline switching and subsequently at passenger switching as part of its conventional derived demand analysis. This does not mean that passenger switching has been relegated to being of secondary importance.

D203 Furthermore, the CAA maintains its position with regards to consistency with precedent as set out in paragraphs D##.

### European markets

D204 In the Initial Views, the CAA suggested that airports may operate in a European market.<sup>125</sup> This view was based on submissions on airlines' ability to move aircraft, with limited focus on passengers' ability to switch. The ability of aircraft to switch was in turn based on the flexibility of the LCC business model and the number of European bases that they operate out of. The CAA considered that, at that time, this lowered the switching costs faced by these airlines. The CAA also considered that inbound carriers could easily switch between arrival airports, given limited sunk costs.

D205 However, the CAA's current position on this issue is that airport markets should not be defined as European in scope.

D206 The evidence the CAA has been presented with to date shows generally that airlines flying from airports in the south east of England operate primarily to serve the demand generated by the local catchment area or those that wish to travel to London and the south east of England. As shown in the airline evidence below, airlines do not consider that non-London airports compete with Stansted.

D207 As noted above, the CAA's earlier statements on European markets gave limited consideration to passengers. However, account should be taken of the air transport markets (set out above), where passengers make their decision. Case law indicates competition in air transport markets is based on city-pair routes. The airline evidence and case law also suggest that non-London airports would not be substitutable for London airports, therefore by extension, operating from an airport in Europe cannot serve the local catchment area either.

---

<sup>125</sup> The Guidelines, paragraph 3.67 and Initial Views, paragraph 2.143.

- D208 Passengers and their demand for air transport services is therefore fixed to particular location, such that to serve passenger demand to and from London a London airport must be served. This line of reason appears to be non-contentious and was the view of the CC:
- ...if Ryanair has a customer who wants to fly from the UK to Spain, the customer will not think that an airport in Italy is a close and effective substitute for Stansted from which to fly. It seems to us that airlines care about access to particular locations precisely because the passengers who will choose to fly from a UK airport will not be the same as those who are based close to, for example, an Italian one.<sup>126</sup>*
- D209 Given the fixity of the passenger demand to London, further consideration of the airlines' business models need to be considered. However this is clearly set against a backdrop of airlines exiting retail markets in moving capacity away from present and known passenger demand.
- D210 It has been suggested that airports compete in a pan-European market.<sup>127</sup> The arguments for this remain based on the flexibility of the LCC business model. Set out below is the evidence provided on the issue of a European market and the CAA's rationale as to why it does not consider that this is the case.
- D211 Prior to its acquisition by MAG, STAL<sup>128</sup> had stated that it had been considered as [redacted], whereby [redacted] looked to remove aircraft for use on routes from other bases. STAL notes that for non-neighbouring airports, charges are one of a number of issues that are taken into consideration by airlines and are likely to be considered after market development and the presence of competitor operations offering similar services.<sup>129</sup>
- D212 MAG at Manchester had a similar view to STAL. It considered that it competes with secondary hubs across Europe. However, it stated this was limited to network carrier growth.<sup>130</sup>
- D213 Birmingham Airport Holding Limited (BAHL) told the CAA that it considered that European airports provided a competitive constraint only at the margins. As with aircraft being moved to Stansted, BAHL

---

<sup>126</sup> CC's 2011 report, paragraph 181.

<sup>127</sup> MAG, Civil Aviation Authority Stansted Market Power Assessment; Interim response of M.A.G to the CAA's 'minded to' document 24 May 2013, chapter 4,

<sup>128</sup> Source: STAL [redacted]

<sup>129</sup> Source: STAL [redacted]

<sup>130</sup> Source: MAG [redacted].

considered that an LCC moving aircraft to European airports was tantamount to the LCC using its assets to serve a different market.<sup>131</sup>

- D214 The CAA considers that the representation from these airport operators suggests that there is some perceived competitive constraint from European airports on those operating in the UK.
- D215 The only evidence the CAA has been presented with of actual pan-European switching is at [redacted] in relation to [redacted] services. London [redacted].
- D216 The switching from [redacted] is consistent with the view that [redacted] switches capacity from one market to another. In such circumstances it would not appear to be a competitive constraint within the same market.
- D217 Despite the historic switching, [redacted]<sup>132</sup> has expressly stated that it does not monitor the prices charged at European airports. The CAA has also not seen evidence to suggest that STAL reviews these charges (although it does monitor the prices of airports within the UK). This suggests that STAL is not considering how its price/service offer matches with European airports. The CAA considers it is rational to expect that an airport operator would monitor prices at those airports it considers competitors.
- D218 MAG has highlighted that it considers that the CAA's approach to this issue is wrong; that airline-airport deals are confidential and it would therefore be of little benefit to monitor tariff charges. The CAA does not consider this to be the case and has been able to review the tariff price and growth incentive schemes at a number of European airports without using its statutory powers.<sup>133</sup>
- D219 In its response to the Consultation, MAG emphasised that STAL operates in a fragmented pan-European market.<sup>134</sup> MAG presented an argument suggesting that airlines will, in response to an increase in airport charges, reallocate aircraft within their airline network. This ability to move aircraft from a less profitable route to a more profitable route (as a result of the charging increase) causes airport charge increases to be self

---

<sup>131</sup> Source: BAHL [redacted].

<sup>132</sup> Source: [redacted].

<sup>133</sup> The CAA considered the airport charges and any incentive schemes offered by the top five airports in terms of seats offered in summer 2012 by both easyJet and Ryanair. The CAA was able to view the charges of Berlin Schönefeld, Charleroi, Dublin, Frankfurt-Hahn, Geneva, Milano Malpensa, Paris Charles de Gaulle, Paris Orly, Pisa, and Amsterdam Schiphol. Many of the airports also published growth incentive schemes. Source: Airport websites (accessed 14 August 2013).

<sup>134</sup> MAG, Civil Aviation Authority Stansted Market Power Assessment; Interim response of M.A.G to the CAA's 'minded to' document 24 May 2013, paragraph 4.1.

defeating.<sup>135</sup> That is to say, that from the current routes served where one becomes less profitable the next best alternative route will be served in its place.

D220 To support this view, MAG presented statements from its airlines of their pan-European approach to their businesses.<sup>136</sup> MAG also presented evidence of volume changes in summer season weekly departures for both easyJet and Ryanair from 2006 to 2013. The data shows a general fall in movements from Stansted and a rise in movements at other airports in the airline's networks.

D221 MAG also considered that:

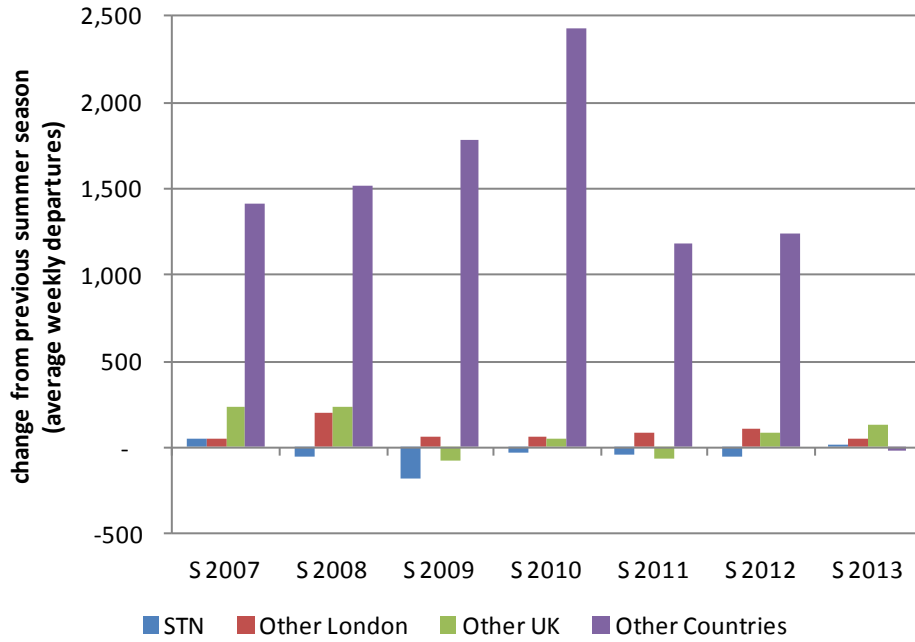
*Switching evidence such as this is the most clear and unequivocal evidence of a competitive constraint being exercised on Stansted from airports across Europe (and, indeed, across the UK). Aircraft have been, and are being, relocated away from Stansted in favour of other European airports. When deciding where to allocate new aircraft, it is clear that the airlines have chosen other European airports in preference to Stansted. These figures clearly demonstrate that Stansted competes in a Europe-wide market.*

---

<sup>135</sup> MAG, Civil Aviation Authority Stansted Market Power Assessment; Interim response of M.A.G to the CAA's 'minded to' document 24 May 2013, Annex A.

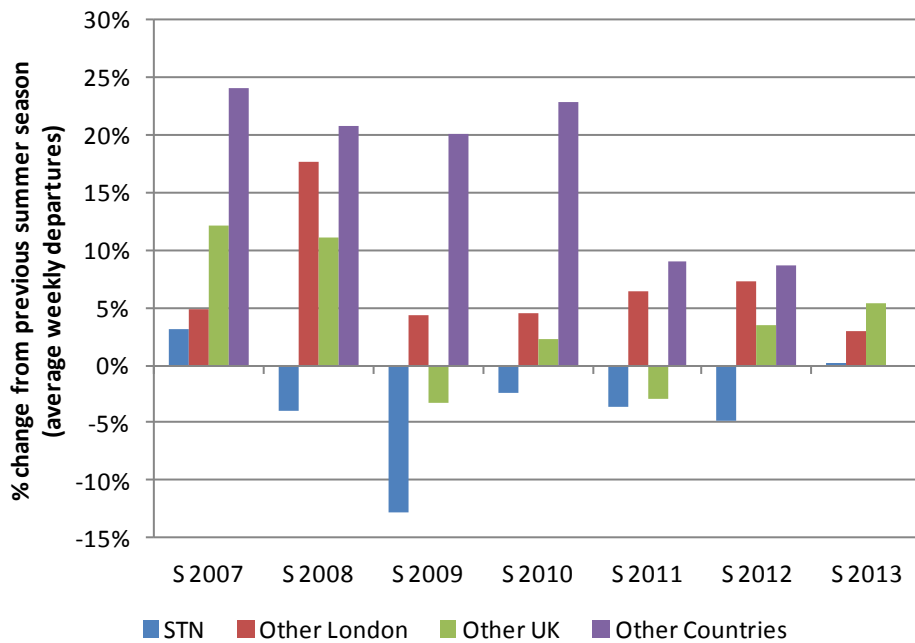
<sup>136</sup> MAG, Civil Aviation Authority Stansted Market Power Assessment; Interim response of M.A.G to the CAA's 'minded to' document 24 May 2013, paragraphs 4.23 to 4.29.

**Figure D.4: Growth in Ryanair and easyJet weekly departures by geographic area**



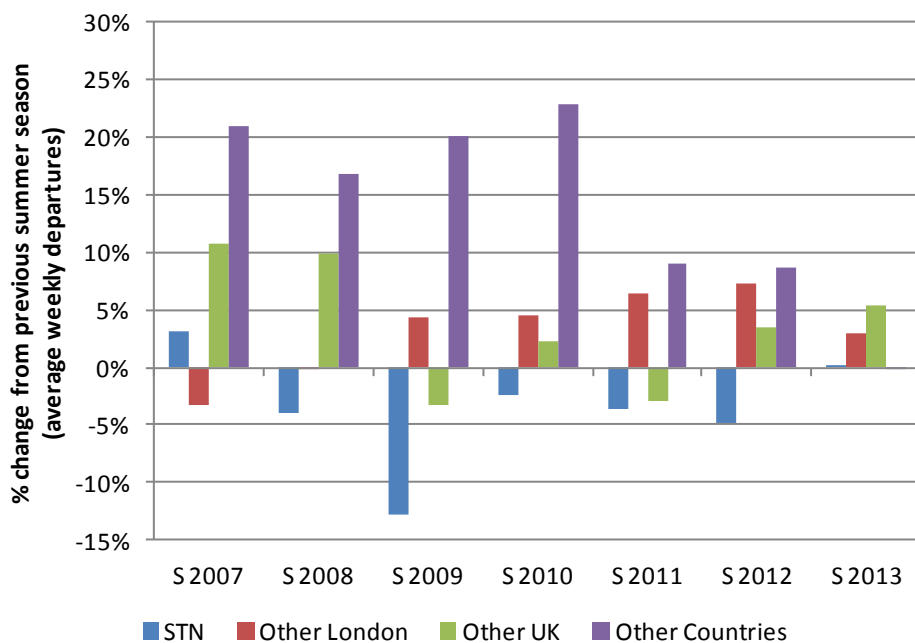
Source: CAA analysis of OAG scheduling data

**Figure D.5: Proportional growth in Ryanair and easyJet weekly departures by Geographic area**



Source: CAA analysis of OAG scheduling data

**Figure D.6: Proportional growth in Ryanair and easyJet weekly departures by Geographic area adjusted for GB Airways aquisition**



Source: CAA analysis of OAG scheduling data



- D222 The CAA has recreated this data in Figures D.4 and D.5. Figure D.6 adjusts the data to take account of easyJet's acquisition of GB Airways, as although new to the easyJet livery, the routes would have already been in operation at Gatwick. As can be seen from the figures above, this significantly reduces the increase in departures from Other London airports from 2007 to 2008.
- D223 These figures also show that for STAL, Ryanair and easyJet have between steadily removing departures from Stansted since summer 2007. It also shows that departures have been added across the UK and more widely in Europe. The sheer volume of increases in departures highlights significant fleet expansion by both airlines.
- D224 However, these figures do not show that STAL faces a strong competitive constraint from European airports. This data highlights the European scope of the LCC networks and their ability to procure and deploy aircraft across that network. In particular, this data:
- Is insufficient to show switching to or from STAL as it does not tackle flows. It does, however, show a decline in services at Stansted as opposed to other airports served by Ryanair and easyJet.
  - Suggests that the falls in departures at Stansted could be accounted for by other behaviour of the airlines to discipline the airport operator such as a reduction in frequencies on routes served, as well as redeployment locally and market exit.<sup>137</sup> During this period STAL did not appear to react to these pressures by altering its pricing policy. It is only in the short time since the change in ownership that STAL has altered its pricing policy.<sup>138</sup>
  - Does not take account of the possible demand side conditions motivating airlines within the air transport markets. The low and negative changes in weekly departures from summer 2008 to summer 2012 could be explained by the performance of the UK economy against countries served by the rest of the LCCs networks.

---

<sup>137</sup> easyJet removal of aircraft from Stansted to service a new base Southend.

<sup>138</sup> This issue is discussed in more detail in appendix H.

- Does not make clear whether the growth seen in Europe could have rationally been supported at STAL neither does it consider the impact that this would have had on the airlines' position against its rivals in new markets. Other London and UK airports saw a rise in departures that was of a similar magnitude to the falls observed at Stansted. However 'Other Countries' airports saw a rise in departures some 20 times greater than the fall in departures seen at Stansted over 2007 to 2013. Almost six times the total departures by those airlines at Stansted in summer 2013.

- D225 MAG's position also assumes that airlines are limited in their ability to procure aircraft and open bases, such that a route would only be opened, and aircraft diverted, if it were more profitable than the current options. Profitable routes would close so that aircraft may service more profitable routes, which may be indicative of a wider airports market. In the absence of airline assets being fixed, it would be expected that all profitable routes would currently be served.
- D226 It does not appear that airlines are, in general, constrained in their choice of airport by either the number of aircraft or bases that they can operate, as MAG has evidenced.<sup>139</sup> Airlines are able to procure aircraft through purchasing from manufacturers,<sup>140</sup> other airlines and/or engaging in leasing agreements.<sup>141</sup> This being the case, the decision to open up new bases or deploy aircraft on particular routes would be driven by individual route or base profitability. Similarly, it is not unreasonable to consider that a route has to be profitable (not more profitable than an existing route); if a route is unprofitable it would close.
- D227 If the scenario outlined above was present, and airlines did close profitable routes, the CAA would expect that the route yields would converge, as airlines would seek to rapidly maximise their portfolio return. However, in reviewing easyJet's route yield<sup>142</sup> it is clear that it maintains routes on a continuum of differing returns, including some with negative

<sup>139</sup> MAG, Civil Aviation Authority Stansted Market Power Assessment; Interim response of M.A.G to the CAA's 'minded to' document 24 May 2013, paragraphs 4.23 to 4.29.

<sup>140</sup> Airbus forecasts that from 2012 to 2031 that it will supply 5,700 aircraft to European airlines. It estimates that 40 per cent of deliveries over this period will be for replacement with the remainder for growth. See: Airbus, Global market forecast; Navigating the future 2012 to 2031, p. 40 to 41, available at: <http://www.airbus.com/company/market/forecast/>, accessed 4 March 2013.

<sup>141</sup> Virgin Atlantic Airways (VAA) launched its Little Red domestic service with wet lease. See: <http://www.virgin-atlantic.com/gb/en/the-virgin-experience/little-red.html>.

<sup>142</sup> easyJet investor presentation, May 2013, 31 January 2012 and Analyst and Investor presentation 15 November 2013.

returns.<sup>143</sup> In its investor presentation easyJet notes the role that low performing routes play:<sup>144</sup>

- Support corporate strategy and provide product range.
- Competitive battles.
- Retail strategic slots or achieve volume deals at high performing airports.
- Complete high performing line of flying.

D228 The above implies that there is likely to be a certain stickiness of routes at airports, as routes that would otherwise appear marginal may be retained for strategic reasons. That is to say, the individually unprofitable routes may be maintained where they are acting to the benefit of the network or other flights i.e. by maintaining high asset utilisation.

D229 The CAA recognises that network yield optimisation of LCCs involves a degree of switching assets between differing markets across Europe and that the ability of airlines to yield-manage across a range of markets is likely to provide some degree of constraint on airport operator pricing. However, when moving capacity from Stansted to a European airport, more so than to a neighbouring UK airport, the airline will be giving up on its competitive position at Stansted and the customers it serves. That is, this is not so much switching as market exit, which is a valid response to a SSNIP.

D230 The CAA does not consider that for the purposes of this Determination the market should be widened to include European airports.

### **Airport operators' views**

D231 This section presents the airport operators' views of the geographic scope of the market in which STAL operates.

D232 MAG has submitted further evidence as to the scope of the geographic area over which STAL faces competition. MAG has not sought to formally define the geographic scope of the market in which they consider STAL operates. MAG has stated that it considers STAL operates in a fragmented pan-European market.<sup>145,146</sup>

<sup>143</sup> The CAA has only observed average yields. Its expectation is that marginal yields are likely to be lower as additional capacity would, all else being equal, be expected to reduce prices.

<sup>144</sup> easyJet investor presentation 31 January 2012, easyJet half year results analyst and investor presentation 9 May 2012

<sup>145</sup> MAG, Civil Aviation Authority Stansted Market Power Assessment; Interim response of M.A.G to

- D233 MAG presented evidence from airline schedules (see Figure D.4 above) which shows that LCCs have decreased weekly departures at Stansted and increased them at other London and other UK airports.
- D234 Evidence from LLAOL suggests that it competes with STAL for airlines. It has also suggested that it competes with BAHL. LLAOL also considered that its catchment area consists of the distance of [redacted] from the airport, roughly [redacted] minutes.<sup>147</sup>
- D235 BAHL considered that MAG at Manchester and East Midlands pose the strongest competitive constraints on its pricing and service offer: considering that both have significant utilisation of their 60 minute catchment (around 90 per cent of passengers). BAHL stated that it currently captures around 40 per cent of its 60 minute catchment and that there is significant overlap within Birmingham, Manchester and East Midlands catchments. BAHL also considered that competition with STAL was only at the margins.<sup>148</sup> In addition, it considered that for long-haul services it competes with HAL. The evidence from BAHL also suggested there is a strong focus on marketing its 60 minute catchment to airlines.<sup>149</sup>
- D236 MAG at Manchester considered that its selling point to airlines was the 22 million people within a 120 minute catchment area.<sup>150</sup>
- D237 MAG at East Midlands considered that a 60 minute catchment was the core of its offering to airlines and that this did not include Stansted. The evidence from East Midlands suggests that competition with Stansted is marginal.<sup>151</sup>
- D238 East Midlands and Manchester airports are part of MAG which now owns STAL. Prospective purchasers of STAL had to be approved by the CC to ensure that there would be no adverse impact on competition from the purchaser.<sup>152</sup> Clearly, given the approved purchase of STAL by MAG, there were no significant concerns over Stansted being added to MAG's portfolio of airports. Given that the CC's investigation had focused on a London airports market, it is rational for the CAA to assume that other MAG airports and Stansted serve different markets.

---

the CAA's 'minded to' document 24 May 2013, paragraph 4.1.

<sup>146</sup> This is consistent with comments made by STAL when under the ownership of BAA. Source: STAL. [redacted]

<sup>147</sup> Source: LLOAL [redacted].

<sup>148</sup> Source: BAHL [redacted].

<sup>149</sup> Source: BAHL [redacted].

<sup>150</sup> Source: MAG at Manchester Airport [redacted].

<sup>151</sup> Source: MAG at East Midlands Airport [redacted].

<sup>152</sup> CC 2009 Report sets out in detail the purchaser requirements at paragraph 10.142.

- D239 LSACL has indicated that its core focus is on its 20 minute catchment area, inbound London passengers and passengers that are equidistant between Stansted and it by rail (i.e. London based outbound passengers).<sup>153</sup>
- D240 GAL's response to the minded to Consultation suggests that it considers that it competes with a number of airport operators within the UK especially those in the South East, namely Heathrow, Luton, Stansted and London City and considers that the market could be broader.<sup>154</sup>
- D241 Taken together, the CAA considers that the responses from the airport operators suggest that they face greater competition from airport operators in close proximity.
- STAL and MAG at Manchester consider European airports as potential airports with which they compete.
  - Both LLAOL and LSACL appear to consider that they face strong competition from STAL.
  - GAL considers that there is a constraint from across the London airports.
  - Other regional airport operators have noted some level of competition with STAL, however this does not appear to particularly significant.

### Airline views

- D242 STAL under the ownership of MAG has managed to secure long-term deals with airlines covering a significant proportion of its current passenger base. Most notably press statements have been released for deals with both Ryanair and easyJet. It is the CAA's consideration that these deals do not alter the evidence already presented by the airlines. The CAA considers the following suggests that it appears that Stansted and Gatwick are being developed as complementary operations rather than in competition with significant commitments from the airlines to grow their operations at both of these airports. This is consistent with the evidence of that Stansted and Gatwick serve separate markets:

---

<sup>153</sup> Source: LSACL [redacted].

<sup>154</sup> Source: GAL, [redacted].

- In June 2013, it was announced that STAL and easyJet had signed a growth deal that could see easyJet's traffic at Stansted double.<sup>155</sup> This deal would see easyJet growing by 3 million passengers at Stansted over the five-year term of the deal. The CAA is also aware of easyJet's recent £20 million purchase of 25 slot pairs from Flybe.<sup>156</sup> The CAA estimates that this would see easyJet grow by between 1 and 2 million passengers at Gatwick.<sup>157</sup>
- Since the announcement of the deals with STAL the CAA has been made aware that a number of airlines common to both airports have also entered negotiations with GAL under the regulatory commitments framework (for a full discussion of these negotiations see Appendix G), These deals are for both the maintenance of and growth from current traffic levels. The CAA considers that this suggests commitment from the airlines to develop operations at both airports.
- On 3 October 2013, GAL announced a significant increase to its scheduled capacity limits for Summer 2014/15<sup>158</sup>. This announcement of the 21 new daily slots<sup>159</sup> - which included 8 morning peak departing slots - constitute around 2.4% of the total runway movements allocated on a peak summer week during Summer 2014.<sup>160</sup> According to the ACC,<sup>161</sup> easyJet, Thomson Airways and Monarch have each acquired one of the 8 peak slots while Norwegian and BA acquired the remaining 2 and 3 slots respectively from the IATA initial coordination conference in November 2013. This again highlights the commitment to both airports from common airlines.

D243 Thomson Airways considered that both Birmingham and Luton are operationally substitutable for Stansted. However, on a commercial basis it considered that Stansted competed with Luton. Additionally, it noted that Stansted competes at the margins with Norwich, although it considered that they serve separate catchment areas. Furthermore, it noted that with regards to London, there is a north/south barrier where

<sup>155</sup> See: [http://www.stanstedairport.com/about-us/media-centre/press-releases/easyjet-sign-long\\_term-deal-to-double-traffic-at-stansted](http://www.stanstedairport.com/about-us/media-centre/press-releases/easyjet-sign-long_term-deal-to-double-traffic-at-stansted) (accessed 18 October 2013).

<sup>156</sup> See <http://www.flybe.com/corporate/media/news/1305/23.htm>

<sup>157</sup> The CAA's discussion on the impact of the easyJet purchase of the Flybe slots is contained within Annex B: Traffic forecasts of CAP 1102.

<sup>158</sup> 'Gatwick Airport Scheduling Declaration for Summer 2014', 3 October 2013.

<sup>159</sup> These were made available through operational improvements on the ground and improved separation control.

<sup>160</sup> Total runway movements allocated in a peak week during summer 2014 is 6,021 movements according to the ACL London Gatwick Summer 2014 initial Coordination Report.

<sup>161</sup> VAA, Email to Charles Ng from Amelia Daair, 26 November 2013

passengers south of the Thames do not typically travel north to Luton or Stansted to fly. Conversely, it noted that Gatwick had a pull even in the north of London.<sup>162</sup>

D244 Wizz, an inbound carrier, noted that it had considered other London airports when deciding to open operations at Luton. Of the London airports, it considered Heathrow was the least accessible due to high costs and the scarcity of suitable slots. By contrast, Gatwick, Luton and Stansted were considered a much better strategic fit for Wizz's business model.

D245 Wizz outlined (see below) the decision-making process it undertakes when considering switching between airports. The key points were:

- The extent of catchment overlap between the airports
- The impact of growing a route at the new airport on the airline's existing services at its current airport and the impact of growing an existing service at that airport, e.g. how many passengers would follow a service moving from one airport to another, and how much of the passenger base would need to be rebuilt if the service was moved.
- The impact at their current airport of switching some services to a new airport. For example, if Wizz switched a route/part of its network to a new airport, another airline may enter at the current airport on the route(s) previously served by Wizz.
- Considering their downstream competition with beginning operations at an airport where the same route(s) were already operated by a competitor with significant capacity results in increased competition on these routes at that airport. This could drive down fare levels and profitability of each airline's operations on the relevant routes.

D246 By undertaking such analysis Wizz determined that that:

- Luton and Stansted catchments overlap and both airports predominantly have LCC and are in competition. Their catchment overlap covers approximately 60 to 70 per cent of Wizz's passenger base.
- Heathrow's catchment overlaps with that of Luton but it is highly capacity constrained and serves a different airline segment (namely long haul).

---

<sup>162</sup> Source: Thomson Airways [3<].



- Gatwick has lower degrees of overlap with the rest of the London airports than do Luton and Stansted, due to its location in the south of London. Its catchment overlaps with approximately 30-40 per cent of Wizz's Luton catchment.

D247 Evidence was also received from [redacted] that suggested that it sees [redacted] evidence also suggests that it sees [redacted]. It is clear from the evidence that [redacted] is concerned with the [redacted] drive-time catchment area of the airports.<sup>163</sup>

D248 In 2012, easyJet opened its operation at Southend. In doing this it switched three based aircraft from Stansted to Southend. In the evidence that has been presented to the CAA, the 60 minute catchment for Southend sits within the 60 minute catchment for Stansted. This shows that there is potentially significant overlap in the customer base for easyJet for these two airports. In this sense, the CAA considers that Southend's catchment could be viewed as a subset of Stansted's catchment.

D249 [redacted]. While, in its minded to Consultation response, easyjet did not consider its move is in itself enough to draw conclusions on whether the geographic market includes Southend<sup>164</sup> [redacted]<sup>165</sup> When questioned on how it could serve the Stansted catchment area without serving Stansted, it considered that it would not be possible. Firstly, it noted that the routes that it currently flies would likely be picked up at the airport by competitor airlines (factors that Wizz also considered important (see above)). [redacted].<sup>166</sup>

D250 The evidence from [redacted] is also consistent with the views put forward by charter airlines. Charter airlines do not appear to consider Stansted as a strong substitute for Gatwick as they consider that their passengers do not view the airports as substitutable.<sup>167</sup> However, where airlines have suggested Gatwick competes, in a broader sense, with the north of London airports this appears to be asymmetric in nature; Gatwick can serve 'north' but the north of London airports do not serve the Gatwick catchment. Ryanair, who supports the market definition outlined in the minded to Consultation, has previously stated that:

*Ignoring capacity constraints in any consideration of airport substitutability only leads to incorrect conclusions. In the case of London airports, LHR, LGW, LTN and LCY are substitutable but are fully utilised (or fully utilised*

<sup>163</sup> Source: [redacted].

<sup>164</sup> easyJet, response to STAL MPA paragraph 9 to 15

<sup>165</sup> Source: [redacted].

<sup>166</sup> Source: [redacted].

<sup>167</sup> Source: Thomson Airways [redacted] and [redacted] [redacted]



*in peak periods in the case of LTN), and where planning and policy constraints prevent the addition of new airport capacity at these airports, airport substitutability cannot be assessed in ignorance of these facts.*

*...The European Commission has ruled that LHR, LGW, LTN and LCY are substitutable but capacity constraints mean that Ryanair cannot move there.<sup>168</sup>*

- D251 Ryanair's statements also suggest that it considers there is to some extent a generic airport product. However, Ryanair also highlights that the opportunities for substitutability between airports are constrained to a high degree by capacity and congestion. For example, it considers that:

*To the extent that there exists a very limited room for growth at the London airports that are suitable for Ryanair's operations, these airports are only partially substitutable for STN. The reason for this limited substitutability is the fact that each of these three airports [Stansted, Luton, and Gatwick] serves a distinct catchment area (with only a limited overlap), with customer bases of different levels of affluence and propensity to travel by air, as well as the fact that each of these three airports has a different appeal for inbound traffic to London.<sup>169</sup>*

- D252 Ryanair also doubts whether passengers originating from Stansted's catchment area to the north of London consider Gatwick as a suitable substitute for Stansted.<sup>170</sup>

- D253 Ryanair press notices show that, in 2013, Ryanair sought to expand at Manchester, Liverpool and East Midlands. When questioned about these proposed network developments, Ryanair indicated that its expansion was driven by the low level of charges at those airports. However, it also noted that those airports served different markets to Stansted. When questioned about the aircraft it would use for this proposed expansion, Ryanair indicated that they would be coming from higher cost airports (they did not confirm which but stated it would not be from Stansted) and from the use of 11 new aircraft.

- D254 The CAA considers that the evidence is clear that a number of airlines consider that there are substitutable airports available for their services at Stansted. For example:

---

<sup>168</sup> Source: Ryanair [redacted].

<sup>169</sup> Source: Ryanair [redacted].

<sup>170</sup> Source: Ryanair [redacted].

- Ryanair and Wizz appear to consider that there is substitutability across all of the London airports. Both these airlines have also argued against the substitutability of Heathrow for Stansted. Indeed, on grounds of current capacity and utilisation, Ryanair considers that substitutability for Stansted is limited.
- easyJet and Thomson suggest that there is limited substitutability of Gatwick for Stansted, this is supported by the commitments to grow at both airports.
- The evidence from easyJet suggests that both Luton and Southend are substitutable for Stansted but not the other London airports.

### **Airline switching**

D255 This section considers the evidence available of airlines switching air transport services to and from Stansted. It initially sets out what recent switching has occurred and then outlines information associated with these moves.

#### *Stansted to Gatwick*

- Mid 2009, Norwegian Air Shuttle moved its entire operation from Stansted to Gatwick.
- February 2011, Air Berlin moved two of its five Stansted routes to Gatwick.
- October 2011, Air Asia X switched from Stansted to Gatwick. The service was cancelled in April 2012.

#### *Gatwick to Stansted*

- April 2013, Air Moldova switched its twice weekly service from London Chişinău from Gatwick to Stansted.<sup>171</sup>

#### *Stansted to Southend*

- April 2012, easyJet switches three aircraft from Stansted to open a new base at Southend.

---

<sup>171</sup> Reported in the press and on STAL's website, the CAA has not been able to discuss the motivations for this move with the airline, see: <http://www.stanstedairport.com/about-us/media-centre/press-releases/new-airline-for-new-stansted-owners> (accessed 29 April 2013).

### *New Stansted services*

- July 2013 to September 2013 Aegean, a FSC, operated a thrice weekly service between Stansted and Athens.<sup>172</sup>
- In 2014 it is reported that Air Blue will be operating a direct service between Stansted and Lahore.<sup>173</sup>

### *Information and analysis of these switches*

D256 Norwegian Air Shuttle indicated that it moved from Stansted to Gatwick due to:

- Gatwick's good connectivity and transport links to London.
- Its improved ability to attract business passengers from Gatwick, compared to Stansted, which is more leisure orientated and associated with LCCs.

D257 Norwegian Air Shuttle also indicated that it did not consider Luton as it is unknown in Scandinavia and London City was not compatible with its aircraft. It also considered that the limited ability to grow due to slot constraints and the excessive costs of entry into Heathrow did not make Heathrow suitable for its operations.<sup>174</sup>

D258 Air Berlin switched traffic in recent years from Stansted to Gatwick. Airport charges were given as a secondary concern in its switching decision; its primary consideration was the level of passenger demand available at the airports, noting that Gatwick and Stansted have different catchment areas. It was also influenced by the fact that Gatwick is a base for its oneworld alliance partners.<sup>175</sup> Air Berlin has since closed some routes offered out of Gatwick.

D259 In October 2011, Air Asia X<sup>176</sup>, which flew limited services between Kuala Lumpur and London, switched its services from Stansted to Gatwick. It noted that it did not initially start operating into Gatwick due to restrictions placed on them by the Malaysian Government. The move was based on the following reasons:

- Gatwick is closer to a greater proportion of the London catchment;

<sup>172</sup> See <http://www.businessstraveller.com/news/aegean-to-launch-stansted-to-athens-route>

<sup>173</sup> See <http://www.ft.com/cms/s/0/2b7ffcaa-34b7-11e3-8148-00144feab7de.html>

<sup>174</sup> Source: Norwegian Air Shuttle [3<].

<sup>175</sup> Source: Air Berlin [3<].

<sup>176</sup> Source: Air Asia X [3<].

- most of Air Asia X's passengers self-connect and Gatwick has more low cost flights to more destinations than Stansted;
- surface access provision to Gatwick is cheaper than to Stansted; and
- Gatwick had a [3<].

D260 Air Asia X also noted that [3<].

D261 The majority of these switches are all moves in the same direction, that is, from Stansted to Gatwick. Only the most recent move by Air Moldova has been from Gatwick to Stansted. Air Moldova is also an FSC operating two weekly services into Stansted on an Embraer 190.<sup>177</sup>

D262 The clearest switching evidence is that of easyJet switching to Southend. In April 2012, easyJet commenced flying from Southend having moved aircraft from Stansted and having exited a growth deal with the airport. The intention of the switch appears to have been to discipline STAL's price. Although the CAA is not aware that this motivated a change in behaviour of the airport operator at the time, easyJet has since been able to secure a long-term deal with MAG as the new owners of STAL.<sup>178</sup> The CAA considers that this switching was competitively motivated and is an indicator that Southend may be in the same market as STAL.<sup>179</sup>

D263 The switching evidence suggests that airlines have been able to switch between Stansted and other London airports i.e. Gatwick and Southend.

D264 The switching to Gatwick appears to be motivated by non-price considerations and more by strategic and commercial considerations such as

- strong international brand;
- surface access in to London;
- greater passenger demand within its catchment;
- greater proportion of business passengers; and
- alliance member airlines.

<sup>177</sup> The Embraer 190 is a relatively small aircraft up circa 100 seats. Furthermore, GAL's stated policy of incentivising the use of larger aircraft on its runway, which was a key issue in the Flybe section 41 complaint against GAL. See <http://www.caa.co.uk/docs/5/S41GatwickFlybeDecision.pdf> .

<sup>178</sup> See [http://www.stanstedairport.com/about-us/media-centre/press-releases/easyjet-sign-long\\_term-deal-to-double-traffic-at-stansted](http://www.stanstedairport.com/about-us/media-centre/press-releases/easyjet-sign-long_term-deal-to-double-traffic-at-stansted) accessed 19 July 2013.

<sup>179</sup> easyJet, in its response to the minded to Consultation indicated that it did not consider its move to Southend was not of itself indicative of the airport being within the same market as STAL. LSACL itself has not contested its inclusion in the same geographic market.

- D265 Statements by the airlines on their motivations for switching from Stansted to Gatwick suggest that STAL could not have won back this airline business this indicates that GAL may provide a differentiated and superior product to that of STAL at Stansted. The CAA considers that the switching observed to Gatwick tends to show Gatwick as a superior product to that offered by STAL at Stansted. This suggests that GAL poses a level of constraint on STAL however clearly this one directional.
- D266 The recent switch from Gatwick to Stansted has been by an FSC which shows STAL is beginning to be active in this segment. However, GAL has a stated policy of disincentivising the use of aircraft such as that employed by Air Moldova on its Stansted route. The view on the relative attractiveness of the product offered at Stansted and Gatwick is likely to be subject to change in the coming years with STAL under MAG's ownership.

### Passenger switching

- D267 To supplement the evidence gained from the airport operators and airlines the CAA has considered the implications of its passenger survey and catchment analysis.<sup>180</sup>
- D268 The survey on which the working papers are developed takes place as a random sample of passengers within the international departure lounge of the airport. As a result, the survey captures passengers for whom Stansted and the surrounding area is their point of origin or was their original destination.

### Evidence on passenger preferences

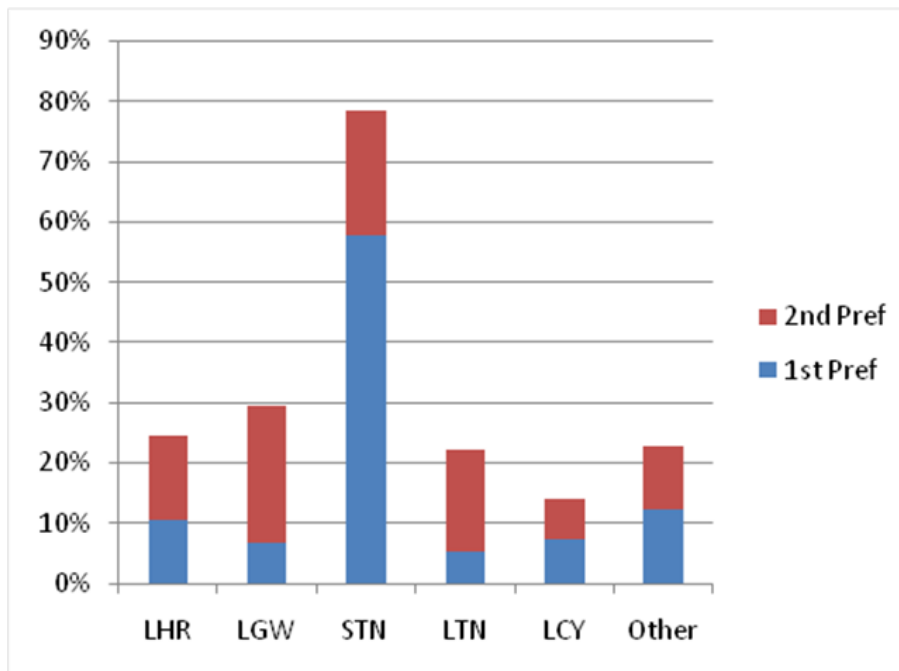
- D269 The travel times that passengers are willing to make to catch a flight are likely to be different and dependent on a number of factors, such as purpose of travel, their frequency of travel and the particular flight which they are taking.
- D270 Analysis of the 2011 CAA passenger survey supports this view; this shows that the location of and access to an airport are the primary reason for choosing a departure airport, although this was the reason given by only 36 per cent of passengers for a London airport, compared to 62 per cent for a non-London airport.<sup>181</sup> The CAA considers that this suggests

<sup>180</sup> Unless otherwise stated this section draws on the evidence presented within the working paper, Passengers' airport preferences: results from the CAA passenger survey and catchment area analysis, published in 2011. The data behind these working papers takes into account both domestic and foreign travellers.

<sup>181</sup> For the 2011 data set non-London airports consist of Manchester, Birmingham, and East Midlands.

that passengers for London airports are less concerned with location. This could be driven by the fact that a high proportion of passengers at these airports come from the central London districts (as illustrated in Figure D.7 below), where there are a number of surface access options available to all of the London airports. The evidence also shows that this varies by service.

**Figure D.7: First and second preference airports for Stansted short haul passengers**



Source: CAA, Passengers' airport preferences: Results from the CAA Passenger Survey, November 2011

D271 In addition, the CAA's working paper on passengers' airport preferences<sup>182</sup> suggests that for the majority of passengers flying short-haul from Stansted, Stansted is their airport of choice. Heathrow, Gatwick, London City, and Luton were all named as a preferred airport but each with less than 10 per cent of responses. Gatwick appears to be a strong second preference to Stansted but it is similar in magnitude to passengers using Stansted as their second preference airport.

D272 Based on the above evidence, the CAA considers that although the majority of passengers are flying from Stansted as their airport of choice, a number of passengers may substitute Stansted for a different London airport if an equivalent flight was available.

<sup>182</sup> Passengers' airport preferences, CAA working paper 2011.

### Evidence from review of catchment areas

- D273 Catchment analysis can provide useful evidence regarding an airport's passenger base. It is a way of estimating the geographic area from which a large proportion of an airport's outbound passengers originate. The size of catchment areas and overlaps between catchment areas<sup>183</sup> of neighbouring airports could provide useful evidence of the potential competition between these airports. It is therefore a useful tool in aiding the understanding of possible geographic markets. It does not however provide price sensitivities of the passenger base as it only considers the location of passengers and the travel times that they may face and may therefore overestimate the competitive constraint arising from passengers' ability to switch.
- D274 In 2011, the CAA conducted catchment analysis for the four largest London airports Heathrow, Gatwick, Stansted and Luton.
- D275 MAG has expressed considerable reservations over the CAA's use of catchment analysis within its market power assessments. In particular, MAG was concerned over the inherently historical nature of the catchment analysis and that the patterns it reflects are those associated with the incentives of BAA under the previous joint ownership.<sup>184</sup>

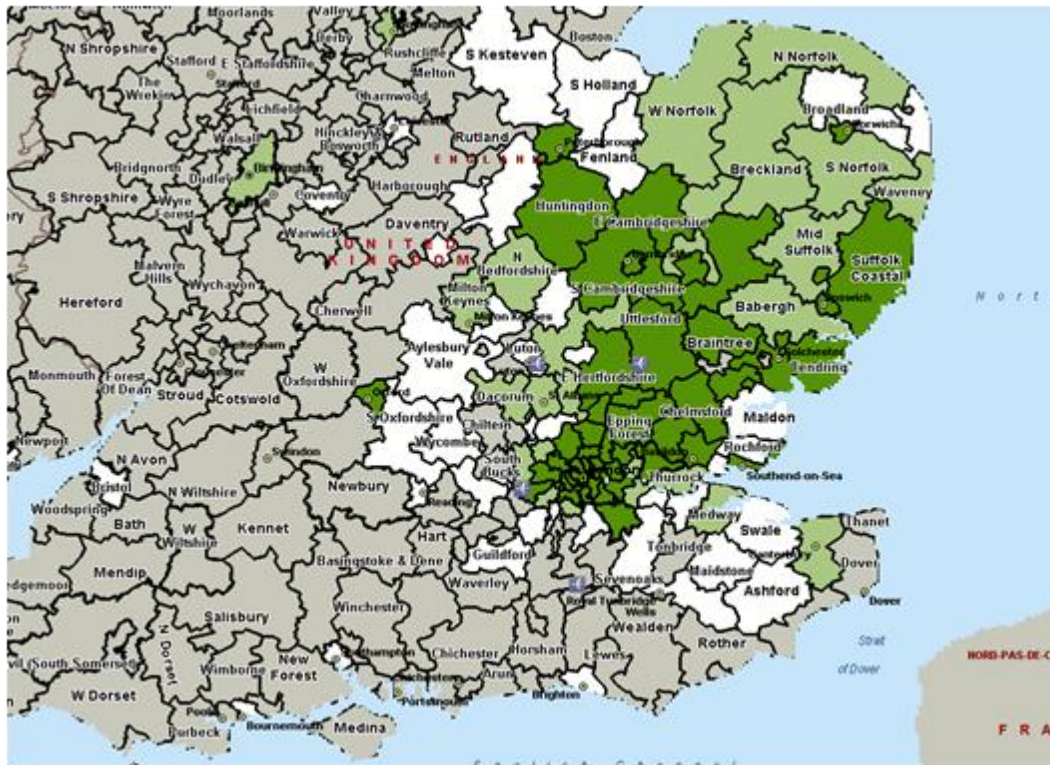
---

<sup>183</sup> The overlaps presented from catchment areas are to some degree impacted by the travel time selected, as travel time increases so will overlap. To limit the effect of this, the CAA has considered a number of possible travel times and historic passenger behaviour.

<sup>184</sup> MAG, Civil Aviation Authority Stansted Market Power Assessment; Interim response of M.A.G to the CAA's 'minded to' document 24 May 2013, paragraph 5.83.



**Figure D.8: Catchment overlaps based on where 80 per cent of passengers originate**



Source: CAA

analysis of the CAA Passenger Survey (2010)

Blue: 1 airport; Light blue: 2 airports; Light red: 3 airports; Red: 4 airports

**Figure D.9: Stansted historical catchment area**

Overlaps	No of Districts	Proportion of Stansted Passengers (%)
STN/	18	11
LHR/STN/	1	0
LGW/STN/	4	3
STN/LTN/	6	5
LHR/LGW/STN/	7	6
LHR/STN/LTN/	7	7
LHR/LGW/STN/LTN/	28	47
Total Catchment	71	79
Out of Catchment		21
Total		100

Source: CAA analysis of the CAA Passenger Survey (2010)



- D276 Figure D.9 focuses on the overlaps of the other London airports with Stansted. It shows that 11 per cent of Stansted passengers have historically come from districts 'unique' to Stansted; the key finding being that there is significant overlap in the historic passenger usage from the central London area whereas outside of this Stansted faces significantly less overlap in its catchment. In 2010, 53 per cent of passengers using airline services at Stansted came from areas where the three other London airports drew passengers from.
- D277 As part of the analysis of historic catchment, the CAA also considered travel times by reference to both long and short-haul passengers. The evidence shows that 80 per cent of passengers taking a short-haul flight travel up to 90 minutes, whereas for long-haul they travel up to 120 minutes.
- D278 Comparing short haul routes at Stansted where the routes are available at the other three large London airports, Stansted passengers are likely to travel further for a flight where it is only available at Stansted around 75 minutes. This drops to a little under 60 minutes where routes are available at all of the London airports.
- D279 As with the differences in travel time by haul consideration was given to travel time for travel purpose. The results of this analysis show that business travellers and VFR travellers travel a shorter distance to the airport than those that are travelling for leisure. Similarly foreign visitors travel shorter distance to the airport than domestic travellers.
- D280 The CAA's catchment analysis considered non-London airports in a limited light showing comparators of 60 and 120 minute isochrones. At 60 minutes Stansted only sees overlap with the Luton catchment whereas at 120 minutes there is some additional overlap with Birmingham, East Midlands and Bristol. The inclusion of these airports and other London airports, such as London City and Southend, within the formal catchment analysis would undoubtedly show additional overlap.<sup>185</sup>
- D281 As to MAG's concern over the historic nature of catchment analysis, the CAA is aware of the limitations of catchment analysis and has considered these limitations when coming to its conclusions.

---

<sup>185</sup> MAG commented (MAG, Civil Aviation Authority Stansted Market Power Assessment; Interim response of M.A.G to the CAA's 'minded to' document 24 May 2013 paragraph 5.79) that the analysis conducted by the CAA was limited given the lack of inclusion of other airports, namely London City and Southend.

## Summary of passengers' ability and propensity to switch

- D282 Both the evidence on passenger preference and catchment area analysis highlight the potential for passengers to access a range of airports. However, this does only highlight the potential switching opportunities it does not take into account the reactions of passengers to relative changes in airport charges.

### Price elasticity of demand (PED)<sup>186</sup>

- D283 PED is a measure of the responsiveness of the amount of demand for a product in relation to a change in price. Typically, a PED of 1<sup>187</sup> would suggest the demand changes on a one-for-one basis with price. A PED greater than 1 suggests that demand changes by a greater proportion to a price change. Where a PED is less than 1, demand changes by a lesser proportion than the change in price.
- D284 The CAA has reviewed a number of pieces of evidence with regards to own-price PED at Stansted. PED analysis goes straight to the heart of the market definition issue by focusing on the marginal reactions of passengers and/or airlines.
- D285 Given the number of revenue streams at Stansted each of which is affected by its passenger numbers a PED which is at or just above 1 would likely result in a price increase being unprofitable. This is due to the additional losses of these revenues as passengers leave the airport. The CAA's evidence suggests that for an airport operator to be able to profitably raise prices it would need to face a PED of less than approximately 0.7.<sup>188</sup>
- D286 The CAA's review of the evidence on this for Stansted suggests that Stansted faces a passenger base<sup>189</sup> with an elasticity of demand of 0.2 to 0.6. This suggests that, given the substitution possibilities available to Stansted's customer base, STAL would be able to sustain profitably a SSNIP. This strongly suggests that a geographic definition should be no wider than Stansted airport.

---

<sup>186</sup> A more detailed discussion of CAA's approach and the results of its PED analysis see Annex F.

<sup>187</sup> For most goods and services elasticities are negative numbers. By convention they are cited as absolute numbers.

<sup>188</sup> The CAA's critical loss analysis implies that a PED of 0.6 to 0.8 would be required for a 5 to 10 per cent increase in aeronautical charges to be profitable.

<sup>189</sup> These studies focus mostly on passenger demand rather than the strategic actions of airlines. It has generally been conducted on the assumed basis that airlines follow passengers. It can therefore be considered that these are reflective of an unconstrained passenger PED.

## Supply side substitution

- D287 This section considers the ability of other airport operators to supply the services required for the operation of the aircraft fleets currently at Stansted. MAG considers that STAL competes with airport operators on a pan-European basis.
- D288 The presence of Ryanair and easyJet at a number of bases across Europe suggests that there are airports with the basic facilities required to make them supply side substitutes. However, the CAA's demand side analysis suggests that it should be focusing the supply side substitutability of airports within the London area.<sup>190</sup> The CAA has therefore taken this as a guide and does not explore the supply side possibilities of European or wider UK airports. Its analysis below focuses on the ability to act as a supply side substitute for Stansted by the London airports.
- D289 As outlined in the discussion on supply side substitution in the product market (above), competition for airport operation services will only take place on the currently available infrastructure. Planned infrastructure development and those in the process of construction are only going to be of relevance to competition if they are to be operational over the medium term. The majority of airport developments will impact on the long-term competitive potential.
- D290 With respect to supply side substitution on the geographical market, the CAA needs to consider the ability of airport operators to supply services to airlines in response to SSNIP, and in turn the ability of airlines to substitute to that new supply. As discussed at D17 to provide a constraint on the behaviour of other market players alternative airports are required to be an 'effective' substitute. Available capacity at an airport is a key factor in whether the airport can be used as an effective substitute.
- D291 VAA, has highlighted a number of supply side issues that it considers limit substitutability in terms of operating long-haul services from regional airports including that of runway length:
- Many regional airports do not have runways that can accommodate long-haul aircraft. ...which means that, we could not operate services using our current fleet without altering the passenger payload and/or the cargo carrying capabilities.*
- Many regional airports do not have the terminal capacity or suitable facilities to operate regular long-haul services. For example, due to the high passenger density, check-in desks and immigration services need to*

---

<sup>190</sup> See D223, D257 and D256

*be designed for the high volume of passengers which need to be processed in a condensed space of time. We operate our aircraft in a high density configuration of up to 451 seats. To compete effectively as a full-service airline, we require airport facilities to accommodate particular service standards including separate designated, differential queue standards and the use of business class lounges, as well as facilities for transfer passengers. Many regional airports have insufficient airside facilities to handle wide-body aircraft used for long haul routes. For example, we prefer to use contact stands with direct airbridge access on to the aircraft.*<sup>191</sup>

D292 With runways of over 3,000 meters in length Gatwick and Heathrow are able to offer services to all currently available commercial passenger aircraft. Equally these airports have terminal facilities to handle such aircraft. However, nearby airports, such as Luton and London City, are restricted in the type of operations they can support due to runway length.

D293 London City Airport Limited's website also highlights the limited range of aircraft over which it can offer services to airlines:

*All aircraft using the Airport must be of an approved type. To qualify for approval an aircraft must meet specific noise criteria and be capable of making an approach at 5.5 degrees or steeper (this compares with 3 degrees at most other airports). Helicopters and other vertical take-off and landing (VTOL) aircraft, and single-engined aircraft, are prohibited. Flying for club or leisure purposes is not permitted. Type approval is given by the Airport's Operations and Control Department:*

*Main scheduled aircraft currently approved for LCY: Avro RJ's; EMB 135/170/190; DH-8 Q100,200,300,400; F50/70; ATR42/72; S2000; D328*<sup>192</sup>

D294 Given the fleets in operation at Stansted, it appears that from a supply side perspective, London City would not be able to provide airport operation services to a sufficient range of aircraft sizes to provide an effective constraint on pricing at other London airports, including Stansted. The fleets in operation at London City carry less than 100 passengers, whereas those employed by airlines at Stansted have capacity in excess of 100 seats.<sup>193</sup> The difference in operating fleets is

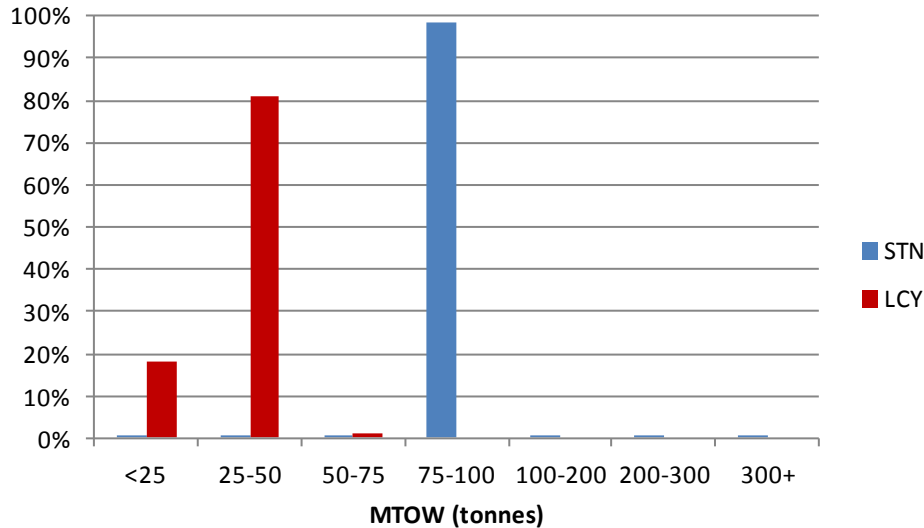
<sup>191</sup> Source: VAA [3&].

<sup>192</sup> London City Airport Limited, Permitted aircraft, available at: <http://www.londoncityairport.com/AboutAndCorporate/page/AirlinePartnersFacilities> (accessed 11 July 2013).

<sup>193</sup> easyJet's A319 the smaller of its aircraft have capacity for 156 seats, Ryanair's Boeing 737-800s have capacity for 189 passengers. See: [www.seatguru.com](http://www.seatguru.com) accessed 11 July 2013.

illustrated in Figure D.10 which considers passenger numbers by maximum takeoff weight (MTOW) of the aircraft.

**Figure D.10: Proportion of passengers by MTOW of aircraft flown in 2012**



Source: CAA analysis

D295 Figure D.3 shows that 98 per cent of passengers using Stansted fly on aircraft that are significantly larger than those on which passengers fly from London City. This coupled with the difference in the passenger base (shown in Appendix F figure F.6 where London City has the highest proportion of business traveller and STAL the lowest from a London airport) indicates that operations from London City are not a credible substitute for operations from Stansted.

D296 With respect to Luton:<sup>194</sup>

- It is likely to have sufficient capacity for inbound aircraft to substitute to Luton in the morning peak period.
- There is insufficient capacity at Luton for the substitution of based aircraft from Stansted due to binding stand capacity constraints.
- Luton is near terminal capacity at peak times.
- The runway at Luton is 2,160 meters in length some 880 meters shorter than Stansted which impacts on the aircraft sizes that it can service. For example, LLAOL told the CAA that:

<sup>194</sup> CAA, STAL Minded to consultation, Annex 4, paragraphs 3.29.

*The [Luton] runway of approximately 2km in length largely precludes long-haul traffic from operating.<sup>195</sup> The model is based on high frequency; short sector (mostly 2 hours and a couple of 5/6hours).*

- D297 This suggests Luton is nearing capacity, which may limit its ability to credibly constrain other airports. Its main capacity issue arises from servicing additional based aircraft. Inbound aircraft could still use the availability at the morning peak, which is the key period for Stansted's current airline mix. The runway at Luton clearly does not limit its ability to act as a constraint on STAL as currently it services a near identical fleet mix.<sup>196</sup> The CAA considers that Luton should be able to provide a sufficiently credible alternative supplier for airport operation services to those at Stansted.
- D298 With respect to Gatwick, it has comparable facilities to those at Stansted. However, there appears to be:<sup>197</sup>
- Very little capacity available during the early morning period to accommodate additional based aircraft; though capacity exists for arrivals. The overall allocation for runway movements in the summer season mornings is high.<sup>198</sup> As stated earlier new morning slots have been released for summer 2014 these have however already been filled.
  - Some capacity outside of the morning period in the summer, especially from 19:00 onwards, and over the winter where runway allocation is consistently below capacity.<sup>199</sup>
  - No capacity issues with regards to the terminal or aircraft stands.
- D299 Given that there appears to be indications of some excess demand at certain time for access to Gatwick slot availability and slot prices may form a barrier to entry at Gatwick. This is especially the case as the CAA is not aware of a secondary market for slots being present at Stansted, where there is effectively free entry. However the CAA does not consider

<sup>195</sup> Source: LLAOL. LLAOL has since stated that with recent improvements to aircraft technology, new aircraft such as the B787, which have shorter take off distances, could potentially facilitate long-haul aircraft.

<sup>196</sup> ACL start of season report for winter 13 for both airports show that in excess of 97 and 90 per cent of departures at Luton and Stansted respectively are made on B737 or A320 family aircraft. ACL, Luton Airport LTN Winter 2013 (W13) Start of season report and ACL, Stansted Airport STN Winter 2013 (W13) Start of season report

<sup>197</sup> CAA, STAL Minded to consultation, Annex 4, paragraphs 3.50 to 3.51.

<sup>198</sup> ACL, Gatwick Airport LGW Summer 2013 (s13) Start of season report, pg 12

<sup>199</sup> ACL, Gatwick Airport LGW Summer 2013 (s13) Start of season report, pg 12 and ACL, Gatwick Airport LGW Winter 2013/14 (W13) Start of season report, pg 12

slot prices to be significant at this time although may increase as capacity tightens in the coming years. The CAA is aware of the recent sale of slots at Gatwick by Flybe generated £20 million for 25 slot pairs (or around £0.8 million per slot pair).<sup>200</sup> However, this must be put into perspective as ACL, the slot co-ordinator, has told the CAA there is only a small amount of trading at Gatwick for modest sums. ACL also noted the lack of liquidity in the Gatwick slot market, with slots being returned to the slot pool rather than sold on.<sup>201</sup> Neither has access to Gatwick been reported as an issue to the CAA by airlines.

- D300 Given the lack of spare capacity in the morning peak at Gatwick, the ability of LCCs to switch from Stansted to Gatwick is likely to be limited for inbound and severely limited for the addition of based aircraft in this period. There is capacity outside of the morning in the summer season. However to maximise aircraft utilisation LCC generally require a series of slots pairs throughout the day that are contingent on them having access to morning slots. Therefore excess capacity at this time is less likely pose a credible switching opportunity as morning slots. The spare capacity during the off-peak periods is, however, likely to allow GAL to provide services to some inbound operators, especially those flying long haul to destinations such as south east Asia. STAL does not currently provide airport operation services to airlines offering long-haul routes.
- D301 Overall, given the current airline mix at Stansted being predominantly LCC, the CAA considers that Gatwick is unlikely to provide a sufficiently credible switching option under current known capacity constraints as these airlines require a high asset utilisation and access to morning departure slots though which to achieve this.
- D302 So far as Heathrow is concerned, there is little overlap in practice. As noted earlier, Stansted is a predominantly a LCC airport serving a passenger base that is generally flying short haul.<sup>202</sup> It has only just to make its first tentative foray into the FSC market. Given Heathrow's predominance for FSC airlines and capacity constraints, it is unlikely that Heathrow would be an effective alternative for STAL's airlines in the medium term.
- D303 Heathrow is operating at 98 per cent of its declared landing slot capacity and has been effectively full for a number of years. There are also significant barriers of entry present at Heathrow in terms of the acquisition

---

<sup>200</sup> See: <http://www.flybe.com/corporate/media/news/1305/23.htm>.

<sup>201</sup> Source: ACL.[3<].

<sup>202</sup> The routes from Stansted are generally considered to be flying short haul to holiday destinations intra-Europe, around the Mediterranean and to North Africa.



of landing slots. It has been possible for airlines at Heathrow to grow their passenger bases through the deployment of larger aircraft, notably the A380. However the deployment of larger aircraft is to some degree limited to aircraft such as the A380 that fly to long haul destinations. These developments are unlikely to provide sufficient additional capacity at Heathrow to such an extent that it may form a credible alternative.

- D304 The development of airlines at Heathrow is almost based on a one in one out basis. Estimates have been calculated for Heathrow slot prices of between £1 million and £25 million per slot pair over the 2001 to 2010 period, with morning slots being more expensive than those in the afternoon and evening.<sup>203</sup> More recently, BAA was quoted as saying that the average slot value at Heathrow was £7 million per year, with morning slots at around £15 million a pair.<sup>204</sup> It has also been reported that in 2012, Delta purchased two slot pairs at an average of £15.4 million a pair<sup>205</sup> and in 2013 Etihad purchased three slot pairs at a similar price.<sup>206</sup> The CAA considers that the price of the Heathrow slots is likely to far exceed the costs incurred by airlines operating at Stansted as a result of a 5 to 10 per cent price rise by STAL.
- D305 Given the capacity constraints and excess demand at the airport, access to Heathrow and the ability for it to act as a substitute is likely to be limited. The CAA also has considerable reservations over the ability of the airport to exert a constraint on neighbouring airports given the supply issues. This is especially the case for LCCs, which (due to their business model) require quick turnaround times and access to the airport at regular intervals during the day to maximise their rotations.
- D306 With the switching observed by easyJet,<sup>207</sup> it is clear that Southend is a credible supply side substitute for some of the airlines operating from Stansted. However, there are some limitations. LSACL notes that it can only take narrow body aircraft up to the size of a B757; this includes most of the A320 and B737 families.<sup>208</sup> In addition, Ryanair has stated that it

<sup>203</sup> Source: Icfi.[3<].

<sup>204</sup> Reported in Euro and converted to GBP at a rate of 1.24 2nd July 2012 estimated from xe.com values reported by route-news.com. See: <http://www.routes-news.com/airlines/item/887-heathrow-airport-slot-trading> (accessed February 2013).

<sup>205</sup> See: <http://buyingbusinesstravel.com/news/2320624-delta-reveals-cost-more-heathrow-flights> (accessed 23 October 2013).

<sup>206</sup> See: <http://www.businesstraveller.com/news/etihad-buys-jet-airways-heathrow-slots> (accessed 23 October 2013).

<sup>207</sup> Paragraph D248 above.

<sup>208</sup> LSACL URL: <http://www.southendairport.com/airport-facilities/operational-information/aviation-services/aircraft-noise-restriction-amp-maximum-size/> (accessed 14 August 2013).



cannot operate its current fleet from Southend<sup>209</sup> and that easyJet appears to be operating only the smaller A319s from the airport (not its larger A320).<sup>210</sup> With respect to passengers, Southend is aiming to grow to 2 million by 2020 which is around 10 per cent of STAL current passenger base.

- D307 Based on the evidence outlined above, the CAA considers that Gatwick, Heathrow, Luton and Southend all have the requisite facilities to service aircraft operating from Stansted. However, capacity constraints and other barriers to entry pose limits on both Gatwick and Heathrow posing credible switching opportunities for the airlines operating from Stansted.

### Conclusion on geographic markets

- D308 The evidence on the geographic market for STAL has focused on the switching opportunities for LCCs and charters, as these are the airlines that dominate at Stansted. While recognising STAL's recent venture into providing services to FSCs, in the short time since MAG's acquisition of STAL, the CAA has not been able to consider the geographic demand side substitute for this particular segment of airlines operating from Stansted in any detail.

#### *Inferences from airport evidence*

- D309 The evidence from airport operators suggests that competition is greatest between neighbouring airports. However, a number of airport operators have suggested that they may compete to some extent with more distant airports. MAG, for example, considers that STAL competes in a market that may be European in scope.
- D310 Having reviewed the evidence on whether there is a European market the CAA considers that there is insufficient evidence to support this contention. To conclude that airports compete on a European level, given the fixity of passenger demand, the CAA would need to consider that the supply of aircraft was fixed such that airlines would close profitable routes and that the costs associated with exit and route development were minimal. For the purposes of this Determination, the CAA does not consider a European wide airport market, but focuses on domestic substitutes.

<sup>209</sup> Ryanair reconfirmed this in their response to the Consultation.

<sup>210</sup> Extracting data from OAG. It was reported that easyJet opened its services at Southend with three A319s (see <http://www.anna.aero/2011/07/27/easyjets-southend-network-clarified/> (accessed 22 August 2013)). It was also reported that the fourth based aircraft is an A319 (see: <http://www.anna.aero/2013/06/19/london-southend-welcomes-easyjets-fourth-based-aircraft/> (accessed 22 Aug 2013)).

*Inferences from airline evidence*

- D311 Evidence from the airlines, however, suggests a much smaller airport set as possible substitutes from which they could operate. This is likely to stem from their competition with rivals which takes place on a city pair basis. A number of airlines have also stated that they consider that there is a north/south divide within the London airports, such that passengers to the south do not travel north. This runs against the general idea of competition in the downstream air transport service market being on a city pair basis. However, in case law, the substitutability of airports and, in particular, Stansted and Luton against Heathrow, Gatwick and London City airports has not been clearly defined.
- D312 It also appears that easyJet operates Gatwick separately from its operations at Stansted, Luton and Southend. This again supports a north/south divide. Wizz has also suggested that Gatwick is not a good substitute for Luton and by extension Stansted, although it does consider there is 30 to 40 per cent overlap in the catchment. Ryanair, which is STAL's largest customer, sees that there is potential substitutability across the London airports, however there are practical constraints posed by entry barriers, capacity constraints and congestion.
- D313 This is supported by the development of long-term deals between STAL and its airlines which coincide with negotiations and other clear commitments to growth at Gatwick, Suggesting that the airports are being developed as complementary operations.
- D314 While there is some evidence of limited switching from Stansted to Gatwick, such switching does not appear to have disciplined the previous owners of STAL into altering its pricing policy. That may have been a feature of the previous owners' commercial strategy. That said, the switching by easyJet to Southend is likely to have motivated some changes in STAL's approach to pricing under the new MAG ownership. However, that response does not, in the short interval since MAG's acquisition of STAL, throw light on its likely reaction to switching to Gatwick or on Gatwick's effectiveness as a substitute.
- D315 Airlines' submissions indicate that:
- Luton and Southend are substitutable for Stansted;
  - Gatwick appears more complementary than substitute to operations at Stansted; and
  - Airlines do not appear to consider that Heathrow is a substitute for Stansted.

*Inferences from passenger evidence*

- D316 Evidence on passengers' decision-making also suggests that passengers, especially those in central London, may have a great deal of choice between airports available to them. However, this does not capture passengers' sensitivities to price or airline preference, which may limit the scope of airports available to them in practical terms.
- D317 To consider directly the reactions of marginal passengers and airlines, the CAA therefore reviewed evidence on PED to consider the possible boundaries of the geographic scope of the market. While the CAA recognises the limitations of this analysis, the PED analysis that it reviewed suggests that STAL could profitably apply a SSNIP of 5 to 10 per cent, suggesting that Stansted may be a market within its own right.
- D318 With respect to the supply side substitutability, the evidence also suggests that Luton and Southend are substitutable for Stansted. In particular, the evidence suggests that these airports:
- Can provide services to a sufficient range of aircraft, most notably the A320 and B737 type aircraft which is in common use by Stansted's current airlines.
  - Have the capacity through which a switch could be credible.
- D319 Heathrow, Gatwick and London City are unlikely to pose significant supply side constraints:
- The fleets currently operating from Stansted cannot be operated from London City due to runway limitations and landing restrictions. Further its passenger base is significantly different from STAL's.
  - Gatwick, despite having the necessary facilities, lacks capacity in the key morning period where access is required for LCC operations and this position is unlikely to change going forward.
  - Heathrow has all of the facilities required to service every available commercial airliner, however, it is effectively full and it therefore does not provide a credible switching option for airlines at Stansted.

*Overall Conclusion.*

- D320 In conclusion, there is strong evidence to suggest that STAL operates in a market no wider than Stansted. However, the CAA recognises that there are limitations to the PED analysis that the CAA has reviewed. Other evidence suggests that substitution opportunities from Stansted exist in the face of a SSNIP. These are likely to include Luton and Southend,

where the airports are sufficiently close and have a high catchment overlap (especially Southend) and similar there is evidence that several airlines have deployed their operations between such airports.

- D321 With respect to Gatwick, the CAA has seen switching to the airport from Stansted. This is, however, difficult to interpret as this has only occurred a limited number of times and appears to have been in response to non-price considerations. The CAA also notes that the evidence suggests that Gatwick may pose a constraint as a superior or preferred product. The moves do not appear to have affected STAL's pricing behaviour under its previous ownership. There have been no switches from Stansted to Gatwick in the short time since MAG took over the operation of Stansted, although there has been one transfer by a FSC airline, Air Moldova, from Gatwick to Stansted.
- D322 In conclusion, the geographic scope of the Stansted product market is likely to include the relevant airport operation services provided at Stansted, Luton and Southend.

### Section 3.4: Temporal markets

- D323 In the minded to Consultation, the CAA indicated that it was not appropriate to segment the market by time of day or season.<sup>211</sup> This was considered appropriate as:
- LCCs require access to Stansted at a number of periods during a day to gain sufficient rotations of their aircraft. The CAA recognised that limited access to peak slots may limit the development of an airline at the airport. The CAA also considered that it was reasonable to consider that limited access to slots during the day would prove problematic to LCC business model as they would be unable to achieve the necessary number of rotations to support their business model.<sup>212</sup>
  - The CAA did not consider that demand changes due to season impact on the inherent competitive structure of the market between the seasons, such that its analysis would benefit from segmenting the market in this way.
  - The CAA had not seen evidence to suggest that passengers become more price sensitive in either season.<sup>213</sup>

---

<sup>211</sup> The minded to Consultation, paragraphs 4.125 to 4.131.

<sup>212</sup> The minded to Consultation, paragraphs 4.126 to 4.129.

<sup>213</sup> The minded to Consultation, paragraph 4.130.

- D324 The CAA received no further representation regarding its consideration not to segment the market by time of day or season and therefore concludes that it would be inappropriate to segment the market by time of day or season.

## Section 4: Conclusion on market definition

---

- D325 Based on the evidence outlined above, the CAA considers that there is a single market for the provision of airport operation services to passenger airlines at Stansted; this market extends to the services provided to airlines at Stansted, Luton and Southend, by their respective operators. The particular services provided at Stansted consists of at least the following airport operation services:

- the use of the runway and taxiways;
- ATC;
- aircraft parking;
- the provision of access and infrastructure needed for the provision of other airside and landside groundhandling services;
- the provision of facilities for check-in;
- baggage handling;
- security screening;
- holding passenger facilities;
- airline staff processing facilities
- passenger transit facilities
- premium passenger facilities; and
- integrated transfer facilities.

- D326 In coming to this view, the CAA considers:

- There is likely to be sufficient competition between airline business models competing at the airport such that passenger arbitrage would likely defeat attempts by the airport operator to discriminate between any particular airline business model.
- The demand side analysis suggests that Gatwick, Luton and Southend are potentially substitutable for Stansted but that other London airports and non-London airports do not appear substitutable.

- With regards to Gatwick, switching opportunities for airlines to move from Stansted to Gatwick appear limited as a result of Gatwick's lack of availability of peak slots at the airport. To the extent that any switching has taken place, the constraint appears to be asymmetric. The CAA considers that Gatwick is perceived as a superior product to the services offered at Stansted and the other north London airports and airlines that have switched have tended to do so for non-price related reasons in order to gain wider commercial and strategic advantages. Recent developments in deals and negotiation at the airports suggest that airlines are developing Stansted and Gatwick as complementary operations.
- The supply side analysis indicates that both Luton and Southend would present credible substitutes to Stansted given their available capacity. The facilities at London City are inadequate.
- The capacity constraints and entry barriers at Heathrow are such that it does not pose a credible or effective switching opportunity.