

## **DECISION ON THE REGULATORY STATUS OF MANCHESTER AIRPORT**

This document sets out the Secretary of State for Transport's (Secretary of State/ Department for Transport — DfT) decision about whether Manchester airport should continue to be designated under Section 40 of the Airports Act 1986. In reaching her decision, the Secretary of State has carefully considered the advice she has received from the Civil Aviation Authority (CAA) as well as responses from interested parties that were provided to her through the consultation process. This has been considered in the context of the designation and de-designation criteria published in May 2007. On the basis of the evidence, she has decided that Manchester airport should be de-designated because the first criterion is not met. As Manchester airport does not meet the first criterion, it is not necessary for the Secretary of State to formally consider the second and third criteria.

The Secretary of State's decision will be implemented by means of a statutory instrument that will revoke the existing designation.<sup>1</sup> The intended effect of revocation is that the existing price and accounts conditions imposed under section 40 of the Airports Act 1986, together with the public interest conditions imposed under section 46, will lapse at the end of the current control period in March 2009; and the CAA will not be required to set a further price cap for Manchester airport for the period commencing in April 2009. This change in regulation will be accompanied by an Impact Assessment (IA) when the statutory instrument is laid in Parliament.

The CAA has stated that following de-designation of Manchester airport it proposes to consult on re-applying under Section 41(1) of the Airports Act 1986 the accounts conditions that currently apply to Manchester airport by virtue of it being a designated airport.

This decision document has the following sections:

- A description of the current regulatory framework.
- A summary of how the criteria for considering the designation and de-designation of airports were developed.
- A description of the request for advice from the CAA on whether the criteria are met for Manchester airport.

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<sup>1</sup> The statutory instrument will revoke the designation of Manchester International Airport contained in the Economic Regulation of Airports (Designation) Order 1986 (S.I. 1986/1502).

- A summary of the conclusions of the CAA’s advice as to whether Manchester airport meets the criteria.
- A summary of the responses to the consultation process about whether Manchester airport should remain designated or not and our process for considering the responses.
- Analysis of the key issues that arose through the consultation process.
- The Secretary of State’s decision.
- An explanation of the next steps and timetable.
- Annex 1 provides a more detailed summary of the responses received by the DfT in relation to Manchester airport’s regulatory status.

### **Current regulatory framework and recent developments**

Currently, Heathrow, Gatwick, Stansted and Manchester airports are designated by the Secretary of State under Section 40(10) of the Airports Act 1986. Such designation places an obligation on the CAA to impose the following conditions on these airports:

- (i) price controls that limit the maximum revenue that they can recover from airport charges over a five year period;
- (ii) an accounts condition that obliges the airport to publish certain accounting information; and
- (iii) any public interest conditions required to remedy certain types of conduct identified by the Competition Commission.

The CAA makes its price cap decisions after taking account of advice from the Competition Commission. Prior to putting in place a price cap, there is a mandatory reference to the Competition Commission. The Competition Commission has recently reported on the proposed price caps for Heathrow and Gatwick airports<sup>2</sup>, and the CAA has issued its proposed price caps for these airports.<sup>3</sup>

The Competition Commission is also separately considering wider issues associated with the UK airport market through its evaluation of whether the airport services offered by

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<sup>2</sup> “Competition Commission report: BAA Ltd – A report on the economic regulation of the London airports companies (Heathrow Airport Ltd and Gatwick Airport Ltd)”, Competition Commission, September 2007.

<sup>3</sup> “Heathrow and Gatwick Airports, CAA price control proposals”, CAA, November 2007.

BAA at UK airports, including Heathrow, Gatwick and Stansted airports, prevent, restrict or distort competition in the UK. This inquiry was referred to the Competition Commission by the Office of Fair Trading in March 2007 and a decision will be made by March 2009.

### **The criteria for assessing designation and de-designation**

Following advice from the CAA, the Office of Fair Trading (OFT) and the Transport Select Committee, and in keeping with the principles of better regulation, the DfT reviewed the criteria for assessing whether airports should be designated or de-designated. The then Secretary of State consulted on new criteria and following consideration of responses to the consultation, the new criteria were confirmed by the then Secretary of State on 31 May 2007.<sup>4</sup>

The final criteria adopted by the Secretary of State are set out below:

*'Designation of an airport is appropriate if, in the view of the Secretary of State:*

- 1. the airport, either alone or together with any other airport(s) in common ownership or control, has or is likely to acquire, substantial market power; and*
- 2. domestic and EC competition law may not be sufficient to address the risk that, absent regulation, the airport would increase and sustain prices profitably above the competitive level or restrict output or quality below the competitive level; and*
- 3. designation under Section 40 of the Airports Act 1986 would, taking account of the magnitude of the risk identified in (2) and its detrimental effects were it to materialise, deliver additional benefits (i.e. over and above competition law) which exceed the costs and potential adverse effects of such designation (i.e. the incremental benefits are positive).*

*De-designation is appropriate if, in the view of the Secretary of State, any of these factors would cease to apply were the airport to be de-designated.*

*In reaching any decision to designate or de-designate, the Secretary of State will take into account all other relevant matters, including international obligations.'*

The decision document stated the Secretary of State's intention to consult on whether there should be a change in the designated status of Manchester and/or Stansted airports. This consultation process included written submissions from interested parties, a stakeholder meeting in September 2007 as well as correspondence with certain respondents to follow up on particular issues.

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<sup>4</sup> The decision document was subsequently amended, on 27 June 2007, to rectify two minor typographical errors.

## **Request for advice from the CAA**

Having confirmed the criteria to be used, Gillian Merron MP, the then Parliamentary Under Secretary of State at the DfT asked the CAA, under Section 16 of the Civil Aviation Act 1982, for its advice about how these criteria applied to Manchester and Stansted airports, and therefore, whether the CAA considered that – against these criteria – the status of either or both airports should change. She stressed the importance of the CAA seeking to provide as much evidence as possible to support its views, and taking account of comments received in respect of its previous consultations on market analysis for Manchester and Stansted airports.

## **CAA's advice on whether Manchester Airport meets the criteria**

We briefly summarise below the conclusions of the advice provided by the CAA, which is available in full from their website<sup>5</sup>. It covered Manchester and Stansted airports. However, those sections relating to Manchester airport specifically, can be found by reading the summary, chapters 1 to 7, and annexes A and B.

### *Summary of the CAA's conclusions*

The CAA advised the Secretary of State that Manchester airport does not meet any of the three criteria. Accordingly, the CAA advised the Secretary of State that Manchester airport should be de-designated. The CAA considered a number of sensitivities in respect of the future ownership of Manchester airport, the regulatory framework and the development of the airline market, and concluded that its recommendations would not be affected by any such event that is now foreseeable or likely.

In relation to each of the criteria, the CAA concluded that:

- *Criterion one* – Manchester airport does not currently hold a position of substantial market power and the degree of market power held by the airport is unlikely to increase over the foreseeable future and, in fact, is more likely to be eroded.
- *Criterion two* – Competition law is sufficient to address any risk that, absent regulation, Manchester airport would increase and sustain prices profitably above the competitive level or restrict output or quality below the competitive level.

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<sup>5</sup> CAA 2007, De-designation of Manchester and Stansted airports for price control regulation: the CAA's advice to the Secretary of State, [http://www.caa.co.uk/docs/5/ergdocs/de-designation\\_advice.pdf](http://www.caa.co.uk/docs/5/ergdocs/de-designation_advice.pdf) (accessed 10 November 2007).

- *Criterion three* – Designation would not deliver additional benefits (i.e. over and above competition law) that exceed the costs and potential adverse effects of such designation (i.e. the incremental benefits are negative).

The CAA considered that the evidence in respect of the first criterion alone is sufficiently compelling to justify a decision to de-designate Manchester airport.

### **Responses and the process to consider responses**

The DfT received feedback from 19 stakeholders about the regulatory status of Manchester airport. These comprised 5 MPs, 2 MEPs, 2 airports, 3 local councils, 1 individual, 3 airline representative bodies, 2 airlines and 1 freight industry body. We have summarized below the key views of respondents and the issues raised. A summary of responses is provided as an annex together with a full list of respondents.

The following respondents support de-designating Manchester airport - Macclesfield Borough Council (MBC), the Freight Transport Association (FTA), Association of Greater Manchester Authorities (AGMA), Manchester Airport Group (MAG), Manchester City Council (MCC), David Starkie and Arlene McCarthy MEP, Gary Titley MEP, Paul Goggins MP, Ian Stewart MP, Andrew Stunell MP, Phil Woolas MP and David Borrow MP.

The following respondents oppose de-designating Manchester airport - Liverpool John Lennon Airport (Liverpool Airport), the International Air Transport Association (IATA), the Board of Airline Representatives in the UK (BARUK), Virgin Atlantic (VA), British Airways (BA) and British Air Transport Association (BATA). It should be noted that BA principally argued that de-designation was inappropriate for Stansted airport and acknowledged that its arguments held less strongly for Manchester airport. BA's comments are summarised in greater detail in the decision letter regarding Stansted airport.

The Secretary of State has carefully reviewed the CAA's advice, responses to the consultation and then considered whether the responses provide any reasons to materially question the CAA's advice. The Secretary of State has also engaged professional advice to inform her considerations. The Secretary of State welcomed the CAA's advice as a substantial piece of evidence based analysis on whether Manchester airport meets her criteria. When considering the responses of interested parties, she put most weight on those views that were supported by evidence and analysis.

Only a few respondents presented material that called into question the CAA's advice. The DfT contacted VA and BARUK to clarify issues raised in their responses and to seek further information to support their views. Following receipt of this information, the

Secretary of State has carefully considered the comments of all respondents, and whether any of the issues raised by respondents were such that it would not be appropriate to follow the advice of the CAA as to whether the criteria for designation/ de-designation for Manchester airport are met. For completeness, the Secretary of State has also considered whether any of the more generic comments about the CAA's advice for Stansted airport would lead her to have any reason to believe that it would not be appropriate to follow the advice of the CAA for Manchester airport.

We describe in detail the responses and our analysis in relation to the first criterion below. Evaluation against this criterion was sufficient to determine that Manchester airport ought to be de-designated. Consequently, we do not discuss the responses relating to the second and third criteria, as it was not necessary for the Secretary of State to reach a formal view on whether these criteria were met for Manchester airport.

### **Analysis of the First Criterion**

#### *Respondents' views*

MBC, David Starkie, AGMA, MAG, MCC and the FTA agreed with the CAA that Manchester airport did not meet the first criterion. In contrast, VA, IATA, Liverpool Airport and BATA disagreed. Some respondents that disagreed felt that the CAA had focused too much on passengers' behaviour instead of airlines behaviour in its analysis of market definition. A case was made for the CAA to consider in more detail whether runway restrictions in relation to aircraft size and limitations in the terminal facilities at other local airports give Manchester airport substantial market power for long haul flights. It was also suggested that negative experiences of de-regulating airports abroad have implications for what might happen at Manchester airport were it to be no longer price regulated. However, these suggestions were not supported by clear evidence that demonstrated alternative conclusions were more appropriate than those reached by the CAA.

In contrast, MAG provided a detailed response with evidence that supported the CAA's advice. Given the length of MAG's submission, we felt it worthwhile to repeat elements of it here. MAG suggested a number of factors that it believed limited its market power, including the changing market for air travel, the outbound nature of traffic at Manchester airport, the prevalence of charter airlines at Manchester airport, that no carrier is based at Manchester Airport and alternative available capacity at nearby airports. MAG drew attention to the increasing gap between the price cap and actual revenues at Manchester Airport since the mid-1990s as evidence of competitive forces disciplining its ability to charge high prices. Further, it described how Low Cost Carrier (LCC) traffic to a number of European destinations, including Madrid, Paris and Geneva, has transferred from Manchester Airport to Liverpool Airport. MAG argued this transfer demonstrates that

local airports are able to compete well in the LCC market, which is a key source of growth for airline traffic. MAG stated that Manchester Airport keeps its prices low for growth opportunities through winning business from new entrants. Its experience is that the prices of airport services are part of everyday discussions between the airlines and the airport and the threat of switching acts as an effective discipline upon prices. MAG believed that the costs incurred by airlines in switching airports are not prohibitive. MAG also listed the customer service awards Manchester Airport has received to demonstrate that it competes on quality as well as price.

### *Analysis*

To establish the market definition the CAA analysed the behaviour of airlines and of passengers. The CAA faced some limits in its ability to analyse the behaviour of the airlines by the lack of information and data given to it by the airlines, and so placed some reliance on observed patterns of their behaviour. Airlines did not provide evidence to suggest that the inferences drawn by the CAA were not appropriate. In general, a robust market definition for this type of analysis will consider both the behaviour of airlines and passengers. The primary relationship is the provision of airport services to airlines by the airport while the demand from airlines for airport services is derived from the demand for air travel from passengers. Meanwhile, passengers have some more direct relationships with the airport by virtue of their use of commercial services at the airport. Further, the CAA considered its conclusions to be robust for a relatively wide (North of England) and narrower market definitions (more focused on the North West of England). Additional support for the CAA's advice is given by the proximity of Liverpool airport as a competitor with substantial spare capacity.

The DfT followed up with VA to find out more about why it considers that Manchester airport has substantial market power in relation to its long haul operations. The information that VA provided indicates the runway and terminal facilities offered at Manchester airport fit its model of operation better than those offered at Liverpool and Birmingham airports (the nearest alternatives), which cannot support its long haul, scheduled operations. However, any impact on VA is not sufficient to conclude overall that Manchester airport has substantial market power for long-haul activities. (This paragraph is a brief summary of VA's views, and further information is not provided because of the confidential nature of some of the information provided by VA.)

The CAA highlighted that other carriers do operate long-haul flights out of Liverpool and Birmingham airports using different types of aircraft. Other long-haul operators with larger volumes of passengers at Manchester airport did not use the consultation process as an opportunity to voice similar concerns about how the lack of airport infrastructure locally means they are restricted to using Manchester airport. For example, BA made

different points with regard to whether de-designation was appropriate and principally in relation to Stansted airport.

Information provided by the CAA and MAG indicated that if a sub-market for long haul services were to be defined, it is likely that its geographic element would be wider than the North-West or even North of England. It might include Heathrow airport and even continental airports that passengers interconnect with for long haul services. The CAA emphasised that passengers on long-haul flights do seem to be more willing to travel further to their departure point than other types of passengers, which might make London airports more of a substitute for them. MAG highlighted the high speed rail link between London and Manchester that allows the South East of England airports to compete better with Manchester Airport as a departure point. Further, this long haul market segment does seem quite volatile, with a relatively high turnover compared to other segments at Manchester airport. If such a wide definition were developed, it is very unlikely that Manchester airport would be considered to have any substantial market power for long haul services.

BARUK highlighted the Canadian experience of de-regulation leading to increased airport charges, for example, the highest in the world at Toronto-Pearson airport. The DfT asked BARUK for further information about this point but the material they sent failed to make an explicit link between what has happened in Canada and the implications for Manchester airport.

DfT has considered whether the other airports that MAG own could affect the conclusion made about whether the first criterion is met. None of the respondents to the consultation suggested that the common ownership of other airports by MAG was a material consideration for assessing whether it had substantial market power. We agree with the CAA that the common ownership of other UK airports to Manchester airport in MAG does not alter our view about the lack of substantial market power. Factors that have influenced our opinion include the other airports in the MAG are not close substitutes for Manchester airport, they are generally smaller airports (albeit in some cases with growth potential) and subject to their own competitive pressures from other UK airports.

In summary, the key points that appear to support Manchester airport not meeting the first criterion are:

- Local airports provide a meaningful substitute to Manchester airport, such as Liverpool airport;
- There is spare capacity at Manchester and competing airports now and for the foreseeable future, even allowing for expected demand growth;

- The market share of Manchester airport is declining, while the overall market for air travel is growing;
- There is high service quality at Manchester airport;
- Airlines and the airport operator at Manchester are effectively and constructively engaged with one another to produce better outcomes at the airport; and
- Pricing and quality of service decisions by the airport appear to have been determined more by competitive forces than the price cap in recent years.

### *Conclusion*

Therefore, the Secretary of State has concluded that Manchester airport does not meet the first criterion. She does not believe that there is enough evidence to overturn or materially question the CAA's conclusion that Manchester airport faces competitive constraints across all the major market segments within which airlines operate. The failure to meet this criterion alone is enough to conclude that Manchester airport should be de-designated.

### **The Second and Third Criteria**

Due to the conclusion reached on criterion one, it has not been necessary for the Secretary of State to reach any conclusion on whether criteria two or three are met in relation to Manchester Airport. The views put forward by respondents to the consultation are summarised in Annex 1.

### **Decision**

The Secretary of State has decided that Manchester airport should be de-designated because the first criterion is not met. It has not been necessary for the Secretary of State to consider whether the second and third criteria are met for Manchester airport, as an airport should be de-designated if any one of the criteria is not met.

In making her decision about the status of Manchester airport under Section 40 of the Airports Act 1986, the Secretary of State took account of the principles for better regulation set out by the Better Regulation Executive, which is part of the Department for Business, Enterprise and Regulatory Reform. More information about these principles and the work of the Better Regulation Executive is available at [www.cabinetoffice.gov.uk/REGULATION](http://www.cabinetoffice.gov.uk/REGULATION). Her decision was also made with regard to the Government's overall policy for the aviation sector as set out in its December 2003

White Paper entitled, “The Future of Air Transport”, which is available on the DfT’s website at [www.dft.gov.uk](http://www.dft.gov.uk).

### **Next steps**

The Secretary of State’s decision will be implemented by means of a statutory instrument that will revoke the existing designation.<sup>6</sup> When the proposed revocation becomes effective, the existing conditions imposed by the CAA pursuant to sections 40 and 46 of the Airports Act 1986 will lapse; and the CAA will not be required to set a further price cap for Manchester airport once the current cap expires in March 2009. The existing public interest conditions imposed by the CAA to remedy certain courses of conduct identified by the Competition Commission will also lapse. This change in regulation will be accompanied by an Impact Assessment (IA).

The CAA has stated that following de-designation of Manchester airport it proposes to consult on re-applying under Section 41(1) of the Airports Act 1986 the accounts conditions that currently apply to Manchester airport by virtue of it being a designated airport.

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<sup>6</sup> The statutory instrument will revoke the designation of Manchester International Airport contained in the Economic Regulation of Airports (Designation) Order 1986 (S.I. 1986/1502).

## **ANNEX 1 – SUMMARY OF RESPONSES TO THE DfT CONSULTATION ON THE REGULATORY STATUS OF MANCHESTER AIRPORT**

This Annex summarises, as appropriate, specific arguments made by respondents to DfT's consultation on the regulatory status of Manchester airport. It does not seek to replicate these arguments exactly as made or reflect all of the arguments by respondents that were considered by the Secretary of State in reaching her decision. As explained above, the decision is based on careful review and consideration of all evidence submitted, including evidence that is not referred to or summarised in this Annex.

Some of the comments that the respondents have made apply to more than one question. Where this is the case, we have noted the response under the most relevant question, instead of repeating it under each one.

### **Respondents' views**

- *Question 1* – Do respondents agree with the CAA's proposed approach to assessing whether airports have substantial market power? If not, which elements of the CAA's approach do respondents disagree with and what alternative analytical approaches do respondents believe should be adopted?

MBC and MAG agreed. IATA, BARUK and Virgin Atlantic (VA) disagreed.

IATA and VA believed that the CAA's approach was flawed because it focused too much on the relationship between the airport and passengers instead of examining further the relationship between the airlines and the airport. In a similar vein, BARUK suggested that the CAA's analysis focused too much on outbound charter passengers instead of inbound passenger airlines. Further, VA and BARUK felt that the CAA should consider in more detail the capacity constraints faced at Manchester airport for long-haul operators in relation to aircraft size and runway restrictions.

- *Question 2* – Do respondents agree with the CAA's conclusions about the general factors relevant to the assessment of substantial market power at airports?

MBC and MAG agreed.

- *Question 3* – Do interested parties agree with the CAA's analysis that the competition law framework is capable of tackling effectively the risk of excessive pricing and/ or under-investment by an airport with substantial market power in terms of its application and enforcement?

MBC, MAG and FTA agreed.

IATA, VA and BATA disagreed.

- *Question 4* – If interested parties are concerned that the competition law framework may not be an adequate mechanism to protect customers from potential anti-competitive behaviour, please set out, with supporting evidence, the specific factors about the airports sector that support this view.

AGMA and MAG agreed. AGMA highlighted how competition law applied to other companies with market power instead of price regulation, its applicability to airports and the potentially significant financial penalties. MAG emphasised that it did not believe that recourse to competition law would be necessary because competitive forces would act as a discipline upon Manchester Airport.

IATA, VA and BARUK disagreed. IATA were concerned that the delay associated with using competition law to discipline firms made competition law an ineffective substitute to price regulation - designation is 'forward looking' while legal remedies under competition law are 'backward looking'. IATA also believed that the CAA's economic regulation of Manchester Airport delivered continuous improvement in cost-effectiveness and service quality. VA described competition law as being a lengthy, cumbersome and expensive process relative to price regulation and could not suitably protect users relative to price regulation. BARUK cited the increase in airport charges that had occurred in Canada after airports were de-designated, with Toronto-Pearson airport having the highest landing fees in the world.

- *Question 5* – Do respondents agree with the CAA's proposed approach to assessing the costs and benefits of regulation, including that the analysis is necessarily a mix of quantitative and qualitative factors? If interested parties consider that it is possible to quantify more of the costs and benefits than the CAA has done, please explain why and where possible provide evidence to allow such quantification.

MBC and MAG agreed. MAG believed that the most significant costs related to management time spent engaging with the regulator instead of other areas of the business, which is unquantifiable.

- *Question 6* – Do interested parties agree that the CAA has correctly identified the three potential incremental benefits associated with *ex ante* regulation, over and above general competition law? If not, please explain.

MAG agreed. No other respondents made comments in relation to this specific question.

- *Question 7* – Do interested parties agree that the CAA has correctly identified the four potential costs of *ex ante* regulation? If not, please explain.

MAG agreed. No other respondents made comments in relation to this specific question.

- *Question 8* – Do interested parties agree with the CAA’s assessment of the relevant market for its analysis of the market power of Manchester airport (paragraph 5.138 of the CAA’s advice)?

MBC and MAG agreed. In particular, MAG supported the CAA’s catchment area analysis and felt the relevant geographic market was the North of England. MAG believed that passengers are increasingly willing to travel longer distances by road to reach their departure airport because they are increasingly price sensitive, as demonstrated by their greater use of the internet to purchase flights and Low Cost Carriers (LCC) for travel.

- *Question 9* – Do interested parties agree with the CAA’s conclusion that Manchester airport does not currently have substantial market power? Where interested parties disagree with all or some of the CAA’s analysis or believe that issues have not been covered in the CAA’s analysis, please explain and provide evidence.

MBC, David Starkie, AGMA, MAG and the FTA agreed.

David Starkie believed that Manchester Airport pricing below the cap set by the CAA reflected the competitive pressures that it faced. AGMA also gave competitive pressures as the reason for Manchester Airport pricing 5 per cent below the cap. David Starkie cited the measures taken by Manchester Airport to attract and retain airlines - it has spent approximately £5 million on discounts, rebates and marketing support over the past two price control periods, with substantial increase estimated for the current control period.

The FTA believed that Manchester Airport faced substantial competition from freight flown into airports in the south of England that is then transported north by road.

AGMA emphasised Manchester airport’s falling passenger share over time for the North of England and the increasing market shares of other local airports.

The MAG suggested a number of factors that it believed limited its market power, including the changing market for air travel, the outbound nature of traffic at Manchester airport, that no carrier is based at Manchester Airport and there is alternative capacity at nearby airports. MAG drew attention to the increasing gap between the price cap and

actual revenues at Manchester Airport since the mid-1990s as evidence of competitive forces disciplining its ability to charge high prices.

MAG also felt that relative market sizes at Manchester Airport limits its market power. Its key customer group is charter airlines, which MAG argued is less sensitive to the choice of departure airport, through the link to package holidays, and has greater buyer power, through recent mergers in the industry. Further, it described how LCC traffic to a number of European destinations, including Madrid, Paris and Geneva, has transferred from Manchester Airport to Liverpool Airport. MAG argued this transfer demonstrates that local airports are able to compete well in the LCC market, which is a key source of growth for airline traffic. Indeed, it suggested that smaller airports are favoured by LCCs because of their spare capacity and lower fixed costs. MAG cited other evidence given by the CAA that showed the overlap in routes between Manchester and other local airports.

In relation to long-haul, MAG emphasised the relatively small size at Manchester Airport as well as the possibility of these carriers choosing to fly their aircraft on completely different routes. MAG also highlighted the high speed rail link between London and Manchester that allows the South East of England airports to compete better with Manchester Airport as a departure point.

MAG also believed that the costs incurred by airlines in switching airports are not prohibitive. Its experience is that the prices of airport services are part of everyday discussions between the airlines and airport and the threat of switching acts as an effective discipline upon prices. Further, it stated that Manchester Airport keeps its prices low for growth opportunities through winning business from new entrants. MAG also listed the customer service rewards Manchester Airport has received to demonstrate that it competes on quality as well as price.

IATA, BARUK, VA and Liverpool Airport disagreed.

Liverpool Airport and VA believed that Manchester Airport's high share of passengers in the North West of England demonstrates that it still has a dominant position. BARUK and VA suggested that Manchester Airport had market power in the long-haul passenger market because infrastructure requirements of this type of service are only met by Manchester airport in the North of England. VA highlighted that the weight restrictions that are in place for other local airports mean that it is only able to land Boeing 747s at Manchester airport.

- *Question 10* – The CAA's analysis of the potential market power of Manchester airport comprises a number of different elements. While recognising that a

decision about the regulatory status of the airport is an overall decision, the DfT would welcome views on the CAA's analysis of:

- *a* – Initial results from its passenger surveys (paragraph 5.61 to 5.75 of the CAA's advice).
- *b* – Switching costs faced by airlines at Manchester airport (paragraph 5.82 to 5.94 of the CAA's advice), and in particular, any additional information that airlines can provide about their switching costs.
- *c* – The potential different market segments for airline and passenger demand at Manchester airport.

MAG agreed. No other respondents made comments in relation to this specific question.

- *Question 11* – Do interested parties agree with the CAA's conclusion that Manchester airport is not likely to acquire substantial market power in the foreseeable future due to the increase in competitive constraints facing the airport and available capacity at competing airports? If interested parties disagree with all or some of the CAA's analysis or believe that issues have not been covered in the CAA's advice please explain and provide evidence.

MBC, AGMA, AGMA and FTA agreed.

AGMA believed that the competition faced by Manchester airport is likely to increase over time. MAG was of the same opinion because of the ongoing expansion of LCCs.

- *Question 12* – On the day that the CAA submitted its advice to the Secretary of State, Luton airport announced that it no longer intended to pursue the development of a full length replacement runway.<sup>7</sup> Do interested parties consider that this development should alter the conclusions reached by the CAA regarding Manchester airport's market power, and if so, why?

MBC and MAG believed that this change at Luton airport did not affect the conclusions reached by the CAA. MAG cited the lack of evidence in the CAA's advice of an origin overlap between Manchester and Luton airports. Further, MAG suggested that the decision by Luton airport not to expand its runway may have limited impact because Luton airport's focus is on the LCC market, which has little need of this additional infrastructure.

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<sup>7</sup> Press release from Luton Airport of 6 July 2007, titled "London Luton Airport Development Proposals".

- *Question 13* – Do interested parties agree with the CAA’s conclusion that Manchester airport does not meet criterion 1?

MBC, David Starkie, AGMA, MAG, MCC and the FTA agreed.

VA, IATA, Liverpool Airport and BATA disagreed.

- *Question 14* – Do interested parties agree with the CAA that there are no particular constraints on the information available to users at Manchester airport which might inform any allegation of excessive pricing?

MBC and MAG agreed. MAG drew attention to the information that the CAA requires all regulated airports to put into the public domain, not just price-regulated airports, which is in addition to that required by general accounting and auditing procedures.

- *Question 15* – Do respondents agree with the CAA that the concentration of airline users is sufficiently high, combined with the magnitude of airport charges and the commercial importance of these to airlines, to indicate that the ten largest operators would, individually or in combination, have the means and motivation to pursue legal actions against any allegations of excessive pricing?

MBC and MAG agreed. MAG felt that this would be possible at a minimum.

BATA disagreed. It queried whether a company or group of companies have used competition law as a remedy for excessive pricing.

- *Question 16* – Do respondents agree with the CAA’s conclusion that Manchester airport does not meet criterion 2?

MBC, MAG, MCC and AGMA agreed.

VA and BATA disagreed.

- *Question 17* – Do respondents agree with the CAA that there appear to be very limited incremental benefits associated with designation, over and above the benefits that might flow from competition and the application of competition law?

MBC, AGMA, MAG, David Starkie and FTA agreed.

VA disagreed. It felt that the CAA’s analysis underplayed the benefits that price regulation offers. In particular, VA believed that price regulation has fostered positive outcomes through the sharing of information on capital investment programmes and

service quality and offered protection to users to ensure the timely delivery of capital investment through mechanisms such as capital triggers.

- *Question 18* – Do interested parties agree with the CAA that the potential costs and risks of regulation are significant, particularly in terms of the potential for price controls to be set too low, and for regulation therefore to distort investment, including at rival airports operating in the same market as Manchester airport?

AGMA, MBC, David Starkie and FTA agreed. FTA believed that de-designation may assist Manchester Airport with investing in its facilities more appropriately. AGMA thought that this hindrance is likely to become more important over time as Manchester airport faces more competition from rival local airports. AGMA believed that designation limits operational and capital expenditure. Similarly, MAG highlighted the danger of price controls being set too low and the potentially negative impact on customer service levels.

AGMA described the incremental costs to Manchester Airport of complying with price regulation, including the direct costs of diverting resources away from improving services and operations as well as the opportunity cost of management time. MAG noted that price regulation can create a competitive disadvantage for those airports that are price regulated compared to those that are not. David Starkie suggested that de-designation may reduce the tendency for excessive price discrimination.

- *Question 19* – We would welcome any additional information or evidence that respondents can provide to consider the potential incremental costs and benefits of designation compared to de-designation.

AGMA suggested that the incremental costs to Manchester Airport of complying with price regulation are approximately £1 million per year. This broadly matched the figure presented by MAG, which was £5.42 million for the last airport review. In contrast, VA suggested the number was £1.9 million.

- *Question 20* – Do respondents agree with the CAA's conclusion that Manchester airport does not meet criterion 3?

MBC, MAG, MCC and AGMA agreed.

VA disagreed.

*Other issues raised by respondents*

We describe below some other issues raised by respondents that do not reply to any of the specific questions that we asked.

Competition Commission ownership inquiry - BATA believed it was premature to consider de-designating airports ahead of the Competition Commission's decision.

EU airport charges directive - BARUK questioned the wisdom of considering de-designating Manchester airport when the EU airport charges directive may mean that it has to be price designated again. Liverpool Airport questioned the impact of this potential directive upon market competition.

Transparency of prices - MBC asked that a specific condition be made as part of de-designation that requires airlines to ensure airport charges continue to be transparent.

Charges too low - Liverpool Airport and FTA expressed concerns that without price designation Manchester Airport might set prices too low.