

# Transport Committee

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16 January 2018

Dear Brian and Peter

The Transport Select Committee is currently completing its inquiry into the Airports National Policy Statement (NPS). Chapter 3 of the Airports NPS outlines the Government's case for choosing the Heathrow Northwest Runway (NWR) scheme over the other scheme options, namely an extended Northern Runway and a second runway at Gatwick Airport. The NWR scheme was chosen predominantly on its relative strategic and economic cases. Because of this, the Committee has spent considerable time understanding these cases for the NWR scheme and is seeking further clarity on the points below.

## **Strategic case**

The headline strategic benefit of the NWR scheme is that it will maintain the UK's hub capacity and more so than Gatwick which, according to the NPS, would threaten the UK's global aviation hub status (para 3.19). The benefits of hub airports have long been espoused to increase connectivity and capacity for air travel as they enable route viability that would not otherwise be the case without transfer traffic. We have heard conflicting views about whether hub airports are the way forward to expand connectivity, particularly considering ongoing technological and commercial changes in the aviation sector. Are hub airports still the best way to maintain connectivity or is the market heading more toward a point-to-point dominant market?

The NPS also states that "expansion at Heathrow Airport would increase the availability of services, and increase competition between airlines. This would lower fares that passengers can expect to face relative to no expansion..." (para 3.26). What capacity is there for increased airline competition at Heathrow, particularly induced by new entrant airlines, in the context of slot allocation regulations and possible landing charge rises?

Should the potential benefits of airline competition at Heathrow be considered against greater airport competition under the scenario of an expanded Gatwick Airport?

The NPS places a great deal of emphasis on the broader range and greater frequency of long haul flights that an expanded Heathrow Airport would offer. This was based, in a large part, on the need to accommodate the growth of business travel, though it only accounts for the minority of traffic at Heathrow (26 per cent of passengers in 2016). Evidence submitted appears to suggest that business travel growth has been relatively constant in recent years. In the context of changes in communication technologies, what expectations are there for business travel demand going forward? How is the London airport system placed to cater for future business travel needs in the context of constrained capacity at Heathrow?

### **Passenger forecasts**

The international connectivity benefits of an expanded Heathrow are derived from the updated aviation forecasts produced by the Department for Transport (DfT) in October 2017. The modelling seems to assume that Gatwick, even with a second runway, will continue operating as a point-to-point airport, with limited long-haul connectivity. Because of this, Gatwick Airport – which had 11 daily long-haul routes in 2016 – is forecast to see a decline in daily long-haul routes to 7 in 2030 with a second runway. This appears to be inconsistent with recent growth in long-haul connectivity at Gatwick in recent years. Is this sort of long-haul connectivity growth consistent with what might be otherwise expected at an expanded Gatwick, particularly if Heathrow were to remain capacity constrained?

The Department's model assumes a constant elasticity of demand at all price levels which reduces the responsiveness of air traffic to real fare changes. Do these assumptions potentially understate the changes that might take place within the London system under different expansion scenarios? Are such assumptions capable of adjustment within the DfT's modelling? The DfT also seems to have assumed that any changes in airports charges at an expanded Heathrow airport would be absorbed by the airlines, rather than being passed through to passengers. Is this a realistic assumption to be making? What effect might a real change in airfares, because of higher landing charges, have on passenger demand at an expanded Heathrow Airport?

The demand growth profile for an expanded Heathrow has also changed to that forecast by the Airports Commission. The DfT have now forecast capacity at the airport to fill-up within the space of two-years from 2026. Putting aside the debate around the plausibility of the opening date, this seems to be a highly optimistic assumption made by the DfT. It was refuted by several witnesses who appeared in front of the Committee. This outcome also appears to counter Heathrow's own commercial expectations in which they anticipate phased growth. The updated forecasts have also led to some highly unusual growth profiles for other airports which seem detached from real-world expectations. This seems to occur because of the suppressed demand at Heathrow assumed in the modelling which sees demand flow quickly away from other airports upon capacity being released. Is there enough evidence of that scale of suppressed demand for Heathrow? How does the DfT model allocate traffic between the airports more generally?

The DfT has conducted sensitivity analysis with a phased growth profile, albeit over a 10-year period. Should phased growth be part of the DfT's central appraisal case? Given the additional effect of discounting, what might the implications be on the net present value benefits by compressing capacity growth within a two-year period, rather than phasing it over a longer-period?

The passenger benefits in the economic case are estimated to include passenger benefits accrued to UK residents, non-UK residents and international-to-international transfer passengers. Is it best-practice to include benefits accrued to non-UK residents and transfer passengers in this sort of appraisal?

### **Wider economic benefits**

One of the other headline statements in the NPS is that Heathrow Airport would result in greater wider economic benefits than an expanded Gatwick. Outside those appraised in the economic case per WebTAG guidance, PwC attempted to quantify the wider economic benefits and as rightly acknowledged in your May 2015 note to the Airports Commission, there are considerable methodological issues in providing reliable wider economic impact estimates. In principle, though, how might the wider economic benefits of an expanded Heathrow be substantially greater than Gatwick if the relative connectivity benefits are broadly the same?

The NPS also states that an expanded Heathrow Airport would result in up to 114,000 additional jobs in the local area by 2030. How is jobs growth usually accounted for in economic appraisals? Is this jobs growth not simply a shift in jobs from elsewhere within the economy? Is it possible to estimate net growth in jobs in these types of appraisals?

### **Carbon costs**

The DfT's updated appraisal now only uses one carbon scenario to forecast demand, compared with the Airports Commission which forecast passenger demand under carbon capped and carbon traded scenarios. Previously, a carbon capped scenario would have resulted in a higher carbon price being applied, resulting in lower demand. The DfT have assumed that more of the carbon reductions can be met through supply side abatement policies without having to use a higher carbon price to reduce demand. Is it a realistic approach to be using a single carbon scenario to forecast demand?

The final point concerns how carbon costs are monetised as part of economic appraisals. The monetised costs of carbon were estimated at £19.2 billion by the Airports Commission, including £18.5 billion for air travel. In the economic case the carbon costs from air travel are excluded from the appraisal. It has become apparent that the exact allocation of these costs in the economic appraisal is dependent upon effective carbon trading being in place. The DfT has assumed a fully-effective international carbon trading scheme to be operating after 2030 and hence the carbon costs from air travel are excluded in the economic case. Is this a reasonable approach to be taking? How should carbon costs of air travel be allocated in an appraisal under a scenario of an absent or ineffective international emissions trading scheme?

I recognise there is a considerable amount of information in here to respond to. Any clarity you can provide is greatly appreciated as part of our scrutiny.  
You are welcome to reply jointly or individually, as you see fit.

Yours sincerely

A handwritten signature in blue ink that reads "Lilian". Below the signature is a single horizontal blue line.

**Lilian Greenwood MP**  
**Chair of the Transport Committee**