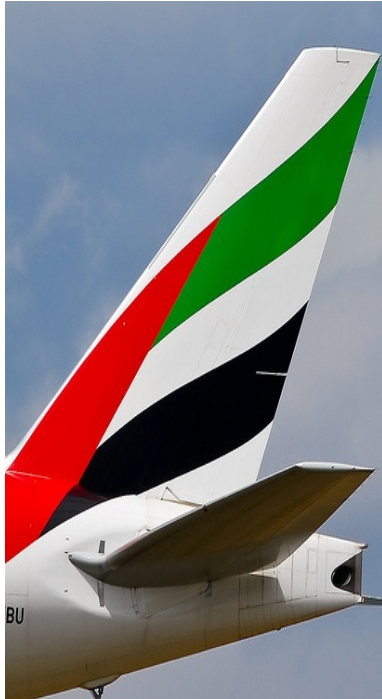




Middle Eastern Carriers - An Aviation Strategy Perspective

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Middle Eastern Carriers – An Aviation Strategy perspective

1.1.1 Introduction

This paper has been prepared to provide guidance to the Airport Regions Conference (ARC) members on the current and future role and impact of the Middle East hub carriers; specifically focussing on Emirates of Dubai, Etihad of Abu Dhabi and Qatar Airways of Qatar.

In particular, ARC has asked for commentary on these airlines' potential impact on:

- Structural change in the airline business
- The impact on the major European hub airports
- The impact and opportunity on smaller European airports (up to 20 million passengers per annum)

In order to provide a valid commentary, the paper:

- Introduces each of the carriers in terms of size, network, traffic composition, business focus and strategic outlook
- Provides some background on the policy and strategic context including ownership, staffing and related issues
- Comments on the Strengths, Weaknesses, Opportunities and Threats facing those companies.

1.1.2 Background

Since the end of the Second World War there has been an inexorable growth of air transport. That growth has been driven by a combination of changes in technology, including the advent of the Jet Age, the advent of globalisation (itself fuelled by air transport networks), consumerism, market power and significant changes in the regulatory environment of international air transport. This is particularly so in the field of economic regulation of services, frequency, capacity, fares and products through changes to the International network of government Air Service Agreements (also known as Bilateral Air Service Agreements). Most of these are modelled on the agreements made in Chicago in 1944 to establish the Freedoms of the Air under the jurisdiction of the International Civil Aviation Organisation (ICAO).

Almost above any other factor, it is the establishment of the right to fly under ICAO bilateral principles that Middle East carriers have exploited. Despite the relatively small indigenous populations and markets that they represent; particularly in contrast with the substantial

populations and markets that they seek to link and serve in Europe, Asia and North America, these carriers have focused their efforts focussing on service and developing their transfer hub strategies.

The reliance on equality of treatment through bilateral process to feed traffic via hubs is fundamental to the business models; these carriers are not the first to recognise and exploit this apparent “loop hole” in the process. The phenomenon was first exploited by carriers such as Singapore Airlines at Singapore and KLM at Amsterdam. Long haul air services to/from the Middle East were initially developed by the need for aircraft en-route from Europe to the Far East and Australia to have to stop for fuel due to aircraft performance and payload /range restrictions.

There have been a number of historic hubs / transit points that had developed as a consequence of aircraft range capabilities and these included airports such as Gander, Anchorage, Singapore, Shannon and Prestwick. All bar Singapore have become aviation backwaters for long haul services with their previous positions sacrificed due to changes in aircraft performance and market expectations. Will this happen again in the future? The only prospect is the significant deployment of the new long range twins which will offer non stop direct services on ‘thinner’ routes.

It is also important to recognise that air transport is not a totally free market. Whilst safety oversight and performance remains paramount and covered by international regulation, economic regulation by governments as to who can fly where, when and with what capacity is still prevalent internationally despite de-regulation in Europe and the USA.

It should also be recognised that all three Middle East hubs associated with the three largest ‘Middle East big three carriers’ (MEB3) studied – Dubai, Abu Dhabi and Doha have grown from small local sea based trading ports with few air services over the last 50 years into major international ports, airports and trading centres.

All are totally focussed and have a unified Gulf State Government, Airline and airport strategic thinking, vision and direction offering a single minded vision and determination. Much of the funding of the airlines and associated airport infrastructure is via the State and the true cost of capital and associated interest rates remain unknown. In the case of development in Abu Dhabi and Qatar, it is understood that a lot of development has been funded by oil / gas receipts and possibly Sovereign Wealth funds.

None of the airlines or their vitally associated airports suffer from planning constraints. All the hub airports operate on a 24/7 basis with no night movement restrictions or related constraints. Indeed, often the busiest time of the day for the Gulf airports is in the early hours of the morning with peak transfer operations feeding traffic between Europe/Americas/Africa and Asia/Australasia. To replicate that and compete on a level playing field is just not possible in Europe due to geography, time zones, history, urbanisation, the democratic process and related operational restrictions and constraints.

The playing field for Europe, for its airlines and airports in competing with the Gulf carriers is far from even.

1.1.3 Historical context

Since the Second World War, each decade has highlighted new aviation phenomena. In the 1960s and 70s it was the role and development of the charter carriers and the impact of the Inclusive Tour charter, particularly in Europe, driven by growing markets, increased disposable income and affluence and ever improving aircraft technology and operating economics.

The 70s and 80s also saw the development of the wide bodied jets with improved economics and payload range performance which extended the scope of market opportunity to new long haul destinations.

The 1980s was the era of rapid expansion driven by economic development but also a trend to de-regulation and liberalisation, started in the USA in 1979 and gradually adopted by Europe from the mid 1980s.

That in turn spawned the development of the Low Cost Carriers such as Southwest in the USA and Ryanair and easyJet in Europe and increasingly worldwide with carriers such as Air Asia, Tiger etc.

The new millennium has seen the accelerated emergence of the MEB3 as major players in international air transport. This has been driven by the rapid development of international air transport on the back of the global economy for both business and leisure travel, together with the expansion at their home cities and economies. It has seen the singular focussed vision of a combination of State, airline and airport to develop aviation as a way of enhancing their nation's status on the world stage and diversifying their longer term reliance on oil and gas receipts (particularly for Qatar and Abu Dhabi). The Gulf Carriers of Etihad, Qatar Airways and most notably Emirates have developed at a pace that has surpassed even the predictions of the most optimistic aviation observers.

This expansion has not come without arousing controversy amongst some of their more established competitors and in some cases the Governments of the states concerned. This is usually about issues of competition, particularly in relation to the rules, financial and policy requirements under which the Middle East carriers operate as compared with those in Europe.

Emirates has had a series of disputes, particularly with the German and Canadian governments over what the airline perceives as "restrictive bilateral agreements." Albeit those bi-lateral agreements are meant to be about a balance and equality of opportunity for both parties and the balance of opportunity might be said to be in favour of Emirates!

Emirates has also been an outspoken critic of airline 'alliances', with its president Tim Clark likening Star Alliance in particular to 'Gang Warfare'. On the other hand the Gulf carriers are often accused of receiving hidden subsidies with preferential rates on fees and charges at their home bases by their competitors, although this has never been confirmed and they hotly deny such underwriting.

James Hogan of Etihad has also recently stated that “Although we compete fiercely in the marketplace, it is important we present as a unified stance to those outside, who would like to see the global aviation landscape look more like it did in the early eighties when no one in Europe lost any sleep over the threat of competition posed by the Middle East carriers. European, American and Asian carriers were the kings of the sky, free to roam as they pleased. Well that is not the case any more.”

Regardless of controversy, their on-going impact on the aviation landscape of Europe and the world is, and will remain, significant for Europe’s airlines and airports, particularly in the short to medium term. Albeit that the primary competition and impact will be on traffic and routes to the Middle East, Asia, the Far East and parts of Africa. In addition, some traffic from North America previously connecting over European hub airports en route to points in the Middle East and the Indian sub continent is now routing on the direct / connecting services via the MEB3 carriers with the consequent loss of traffic, revenue and opportunity for EU airlines and airports.

European airlines are faced with new stronger competitors operating modern fleets with high product standards and competitive prices in their home and connecting markets. In contrast many of the larger European airports have and will increasingly face, the requirement to invest in facilities to accommodate the three airlines rapidly growing fleets including over 100 Airbus A380s, representing some 40% of the current total orders of the A380.

To that end this briefing paper seeks to provide an overview of the Middle Eastern carriers, their impact and possible changes and implications to EC airports and air transport in the future.

1.1.4 Summary and Conclusions

- 1) The three Gulf Carriers subject of this brief study – Emirates, Etihad and Qatar Airways are a growing force in international civil aviation.
- 2) Their individual size already matches or exceeds major EC airlines such as British Airways and Lufthansa.
- 3) All have massive future fleet orders with the carriers accounting for more than 20% of the orders for the A380.
- 4) The single minded purpose of the Governments', airlines and airports working in unison of the three states provides a focus, funding and direction that Europe would find it impossible / difficult to match.
- 5) The geographic position of the Gulf hubs and current aircraft payload range performance / economics does give the carriers a significant advantage.
- 6) Any disbenefit of having to connect is offset by pricing policy and discounting of air fares to compensate.
- 7) The airlines fleets are amongst the most modern in the world. Their products, prices and service standards set industry benchmarks
- 8) The fiscal, economic and planning constraints that apply to the operation and development of air transport in Europe do not exist for the three Gulf carriers.
- 9) All the home base airports of the three airlines operate on an unrestricted 365 day 24/7 regime.
- 10) All the airlines rely on the long established internationally accepted concept of Bilaterals to achieve their business goals. This despite the fact that the largest home market (Abu Dhabi) is a little over 5 million population.
- 11) The availability of financial support to the airlines, particularly those making losses would not be permitted under EC State Aid Rules.
- 12) There is growing resistance to acceding to the demands of the carriers for increased market access. Parts of Europe have given way; China and India appear to be holding out.
- 13) Justifying the future fleet orders depends upon the three carriers being able to:
 - a. Gain additional bilateral authority
 - b. Obtain slots at the most congested European hubs

- 14) Although the three carriers do provide extensive networks of service linking European hub and secondary airports, many more than their European competitors via the Middle East hubs to Asia, the Far East and Africa, disproportionate traffic and focus is still on the primary EC hub airports such as London Heathrow.
- 15) Future European airport hub capacity shortages and changes to slot allocation rules may see the Gulf carriers using the new rules to acquire slots to the detriment of European regional air services.
- 16) The operation of short haul hubs, such as in the USA is under threat from the Low Cost Carriers. The established position of the Gulf carriers and initial lack of suitable long range aircraft in sufficient numbers will mean that any potential threat to the position of the Gulf hubs will be in the medium not short term.
- 17) Previous hubs have been driven by aircraft performance requirements. This is not currently the case with the three Gulf carriers.
- 18) The three carriers can only offer service and routing opportunities to European markets to and from the Middle East, Asia, the Far East / Australasia and Africa. They do not address the EC – North American market.
- 19) There is no direct evidence of poor working practices, pay and conditions amongst such carriers. All have to meet international safety and operating standards and pay the going rate for their professional staff. There may be some savings on issues such as national insurance and pensions at the margin for some staff.
- 20) The Arab Spring revolution has not spread to the three states. The political situation there is allegedly different, despite the apparent lack of democratic process! Any change to that situation could have a significant impact on the future operation and development of the three carriers.
- 21) The future availability and development of new long range, highly economic twin jets such as the B787 and A350, will bring about new service and routing opportunities that will allow direct service to points in the globe. Just as aircraft technological improvements made places like Shannon, Gander and Anchorage redundant, then in time the role of purely transfer hubs, with limited home / Origin / Destination markets may be usurped. However such is the established position and power of the three Gulf carriers that this would take sometime to bite.

2. Airline Profiles

2.1.1 Emirates

Emirates	Information
Established	1985
Home Airport	Dubai, United Arab Emirates
Passenger Fleet Size (Orders)	153 (184)
Destinations served Worldwide	102
Destinations served in Europe	28
Passengers Carried (2010)	31,420,000
Freight Tonne kilometres (millions)	8,151.43
Employees	30,258

Source: ATI and OAG

Emirates was founded in 1985 when, along with a number of other Middle East Gulf states, Dubai decided to pull out of their previous joint venture operation and support for Bahrain based Gulf Air.

Establishing Emirates was seen as a crucial part of the Emir's broader vision of establishing Dubai as a trading and leisure focus for the Middle East that could rival the best the world could offer. It was also recognition that unlike other Gulf States, Dubai did not have the natural resources in terms of oil and natural gas of its near neighbours so needed to diversify and develop its economy in other ways.

This meant developing a Middle East hub airport and airline operation that offered 365 day a year, 24 hour a day hub connectivity, with no operational or night movement restrictions from a worldwide network of air services capitalising on the unique geographic position of the region in relation to world air transport markets and aircraft payload range performance.

The development of Emirates and Dubai International airport were seen as key parts of that overarching strategy which brought together a broad strategic vision with policy and associated funding for the airline and airport backed from the highest level in the State and Government. No questions were asked, no planning constraints imposed, just the achievement of the single purpose goal with the policy backing and funding in place.

With a population of Dubai of some 2 million directly and an estimate of 3 million for the total metropolitan area, Emirates has inevitably had to focus on attracting connecting traffic from the major European, Asian and Far East markets to achieve its goal. This disparity, which is also true for Etihad and Qatar Airways, is one of the keys to the success but also the potential relative imbalance and advantage enjoyed by the Gulf carriers.

Purely by dint of bilateral / air service agreement convention, a state of 2 – 3 million people gains access to markets of many millions, and in the case of China and India, billions. Whether China and India will be as generous on the bilateral front as the three carriers require, and their future fleet orders demand, remains to be seen.

For the future, and unless the world is going to adopt total de-regulation of air service provision (as has happened with shipping), then it may be that the like of the European nations will look for greater transparency and reciprocity. Giving access to the 60 million UK market or 90 million German markets might be seen to command a greater balance than currently offered by Dubai (or Qatar or Abu Dhabi).

The airline now carries over 30 million passengers a year and in the last financial year achieved a 10% operating margin on revenues of \$14,807 million: an achievement that most European carriers can only dream of.

With a modern fleet of over 150 aircraft (compared with some 250 operated by British Airways) and almost 20% of the A380 order book, Emirates has grown to be a force to be reckoned with. One that can take on the best and longest established airlines and win, despite the fact that the largest percentage of its traffic has to connect. Its route network and close association with the Dubai Airport hub and high quality facilities with the emphasis on making ease of connection, it has managed to make a virtue of the connecting requirement. Its pricing policy also reflects a discount for the one stop requirement.

In terms of its employment practices, rates of pay, terms and conditions, there is limited hard publicly available evidence. The majority of Emirates employees are expatriates. In the technical and operational areas, the rates of pay, terms and conditions are dictated by the market place and international comparison. So a pilot joining Emirates will enjoy a competitive salary, support for housing and some associated bonuses, together with the fact that with over 100 aircraft on order, the opportunities for promotion and command on some of the world's youngest and most modern fleet are significantly increased.

The situation on pensions, sickness pay and related benefits is also unknown, but in the key areas to support the main operational and flight operations functions, they will be competitive. It is in the other more general support functions ground handling, aircraft cleaning & catering, back office, IT where the terms and conditions may not match such international standards. But that is potentially true for the whole of the Gulf region in any area of employment and not just confined to Dubai and possibly Emirates. But it does mean that for European Airlines and Airports trying to compete, they are at a competitive cost disadvantage as they are bearing all the national insurance and associated tax and related employment costs which the Gulf carriers probably do not have to. That could be as much as 25 to 30% when the actual cost of employment is also allowed for.*

It serves some 28 destinations in Europe. See map and Appendix (A)

*(It is understood that a similar approach is made with regard to employment terms and conditions by both Etihad and Qatar Airways).

2.1.2 Etihad

Etihad	Information
Established	2003
Home Airport	Abu Dhabi, United Arab Emirates
Passenger Fleet Size (Orders)	61 (91)
Destinations served Worldwide	81
Destinations served in Europe	15
Passengers Carried (2010)	7,010,000
Freight Tonne kilometres (millions)	2,212.75
Employees	7,855

Source: ATI and OAG

The airline was founded in 2003. In some respects it might be seen as the Emirate of Abu Dhabi seeing the outstanding success of Emirates at Dubai, wishing not to be left behind, and with the same vision, drive, initiative and single purpose it could replicate and exceed that achievement, whilst also helping to diversify the economy from its reliance on oil and gas production.

The home market of Abu Dhabi / UAE has a population of some 5.1million whilst the population of Abu Dhabi is merely 666,000. As with Emirates, Etihad is totally reliant on securing the bilateral rights to enable it to capture the connecting markets over its integral and co owned Abu Dhabi International Airport hub.

Unlike Emirates, Etihad remains unprofitable with its continued existence reliant on the backing of the state. Also like Emirates, Etihad is effectively owned and controlled via the same Government department that owns and operates the airport and sets the overall policy and strategic context and provides the ultimate funding.

But as a carrier with a fleet of over 60 aircraft and almost 100 in prospect, transporting over 7 million passengers a year with some 8,000 staff, Etihad is already a relatively large operator and one with significant ambition and financial backing to enable it to develop and influence markets.

Etihad serves some 15 destinations in Europe. See map and Appendix (A).

2.1.3 Qatar Airways

Qatar Airways	Information
Established	1993
Home Airport	Doha, Qatar
Passenger Fleet Size (Orders)	102 (179)
Destinations served Worldwide	109
Destinations served in Europe	26
Passengers Carried 2010	12,900,000
Freight (million) tonne kilometres	3.290.00
Employees	13,136

Source: ATI and OAG

Of the three Gulf carriers, the one with the most aggressive and objective focus is Qatar. More than any other factor, this is attributable to the airline's CEO Akbar Al Baker who is also the Prime Minister of the Country and responsible for seeing through policy and securing financial backing.

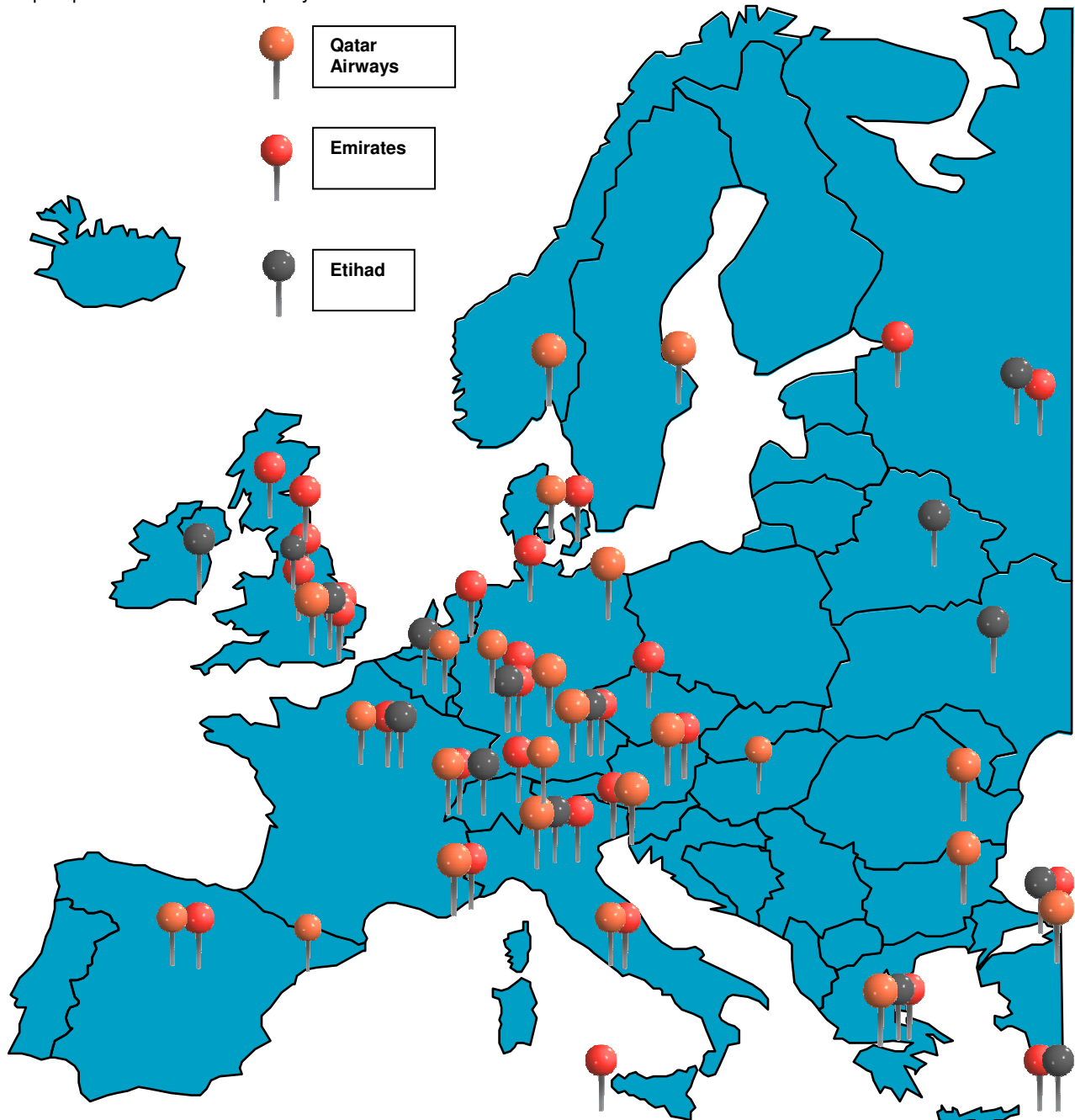
As with both Emirates and Etihad, Qatar Airways also enjoys the same ownership and backing as the airport. As with the other two airlines there is a commitment to ensure that the traffic growth of the airline is more than matched by the capacity available at Doha International Airport and indeed from a brand new airport under construction. Qatar also benefits from being the only carrier from the country, meaning that it does not have to compete with a neighbour for traffic rights in bilateral terms as Emirates and Etihad do within the UAE market.

Also, like the other two carriers, Qatar Airways serves a relatively small home market, in this case a population of under 1 million. As with the other airlines, Qatar Airways's strategy is to capture connecting traffic over the Doha hub, albeit that the fleet strategy and its deployment is somewhat different (see below).

The airline has grown since its foundation in 1993, to a fleet of over 100 aircraft carrying some 13 million passengers and employing 13,000 staff.

It serves some 26 destinations in Europe. See map and Appendix (A)

Map of points served in Europe by Middle Eastern Carriers



Source: Mott MacDonald analysis of OAG schedules

See also appendix (A).

Between them, the three MEB3 carriers serve all the major cities in Europe and many European secondary cities. Emirates has the largest network with service to 29 points in Europe, whilst Etihad serves 14 and Qatar 24.

An interesting divergence in strategy is that whilst both Emirates smallest aircraft is in the 250 to 300 seat category, Etihad and Qatar have been deploying their 150-seat A320 family narrow-body aircraft to new destinations in Eastern Europe, allowing them to better develop such

secondary markets with aircraft that are better suited to the market size, related schedule and frequency requirements. (See below).

2.1.4 The importance of the hub to the Gulf Carrier development Strategy

The Business model for each of the 3 carriers is based on the same premise. With very small, local origin and destination markets, the carriers must each develop networks to link large markets requiring links to a multiplicity of origins and destinations via their respective hubs. The strategy relies totally on the size and composition of the other end markets.

Development of the Middle East hubs has been helped by technology and the evolution of the Long Range twins such as the Boeing 777 and Airbus A330 giving the right combination of aircraft size and ability to serve the markets.

The concept of the use of the hub is not new. For years the power of the hubs in the USA such as Atlanta, Dallas/Fort Worth, Chicago etc was what powered the fortunes of the US legacy carriers. They relied on the fact that hubs generate traffic and opportunities making new routes and frequencies possible in a way that point to point based operating models cannot. But at the price of extended journey times and having to connect. None of the MEB3 airlines appear concerned about the development in parallel of three competing hubs within a few hundred kilometres of one another. Time will tell if they are correct.

This point is best illustrated by a simple table taken from one of the key academic texts on the economics of Air Transport – Flying Off Course by Professor Rigas Doganis.

Impact of hubbing on the number of city pairs served

Number of spokes from the hub	Number of points connected via the hub $n(n-1)/2$	Number of points linked to the hub by direct flights (n)	Total city pairs served $n(n+1)/2$
2	1	2	3
6	15	6	21
10	45	10	55
50	1,225	50	1,275
75	2,775	75	2,850
100	4,950	100	5,050

Source: Rigas Doganis – Flying off Course Third Edition

This table shows clearly that each new spoke in a hub adds disproportionately (almost exponentially) to the service and network options available. So a network of 100 points served creates over 5000 potential city pair linkages. Each new point on an established network adds further traffic and revenue earning capability. It is one of the key reasons why the major legacy airlines and indeed airports (e.g. London Heathrow, Paris, Frankfurt, Amsterdam and the MB3 hub airports) are keen to develop hub concepts. Airlines attract vital additional and incremental revenue whilst airports get significant additional traffic which, but for the enhanced air links would otherwise have not visited the airport. The availability of hub feed traffic can represent the difference between viable and non viable operations.

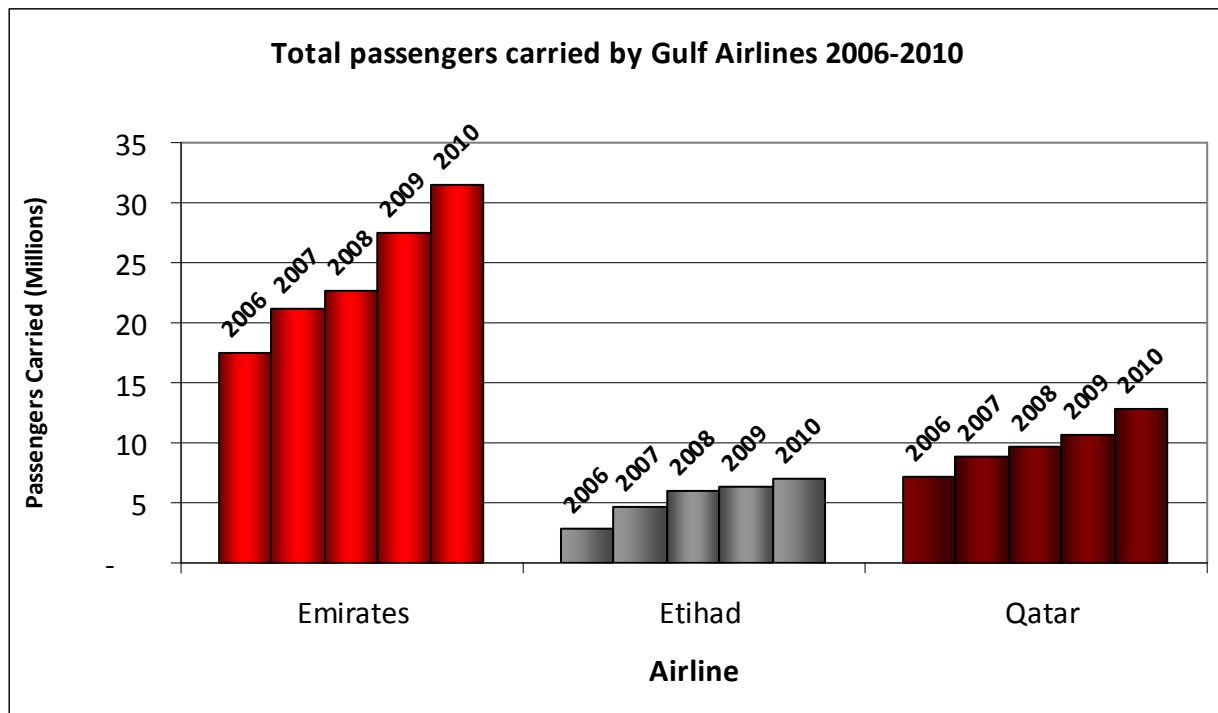
In the case of the Gulf carriers and their small home markets, it is virtually the sole rationale for their existence.

It should be recognised that the US hub model has subsequently been adversely impacted by a combination of de-regulation and the growth of the simplified models of the Low Cost Carriers such as Southwest and Jet Blue who focussed solely on providing cheap (through high density seating and high aircraft utilisation) simple no frills point to point service. But that has been largely a short haul operating phenomena and until the extensive availability of the new ultra long range highly efficient twin jets such as the A350 and B787, will be unlikely to impact the Gulf carrier operations in the short term. Indeed such aircraft types could be added to the fleets of the MEB3 carriers to open up even more markets from their respective hubs to secondary and tertiary cities, which may help some EC regional points in the short term.

2.1.5 Traffic Development

All the airlines have enjoyed rapid growth over the last 5 years, only experiencing some slight slowing in traffic in 2011 during the recent Arab Spring and the impact of recession in key markets in Europe and the USA. Overall traffic at the three airlines can be seen to have at least doubled as shown in the graph below

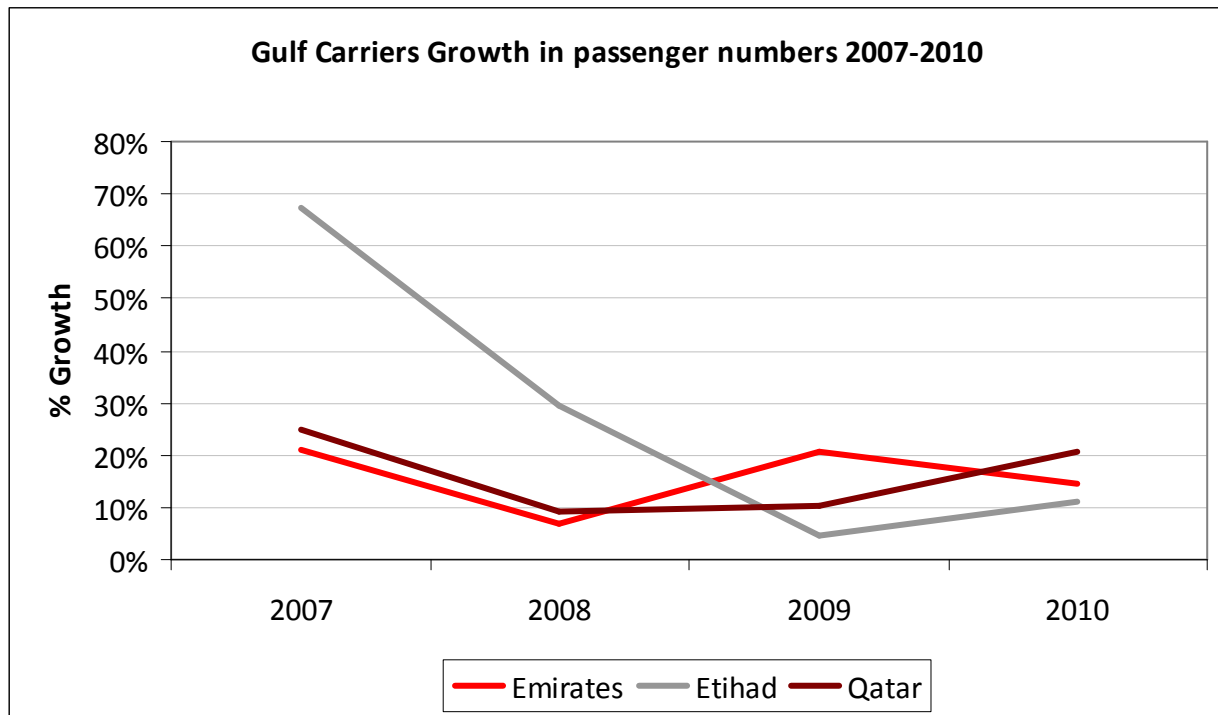
Total Passengers carried by Gulf Airlines 2006-2010



Source: Mott MacDonald analysis of ATI data

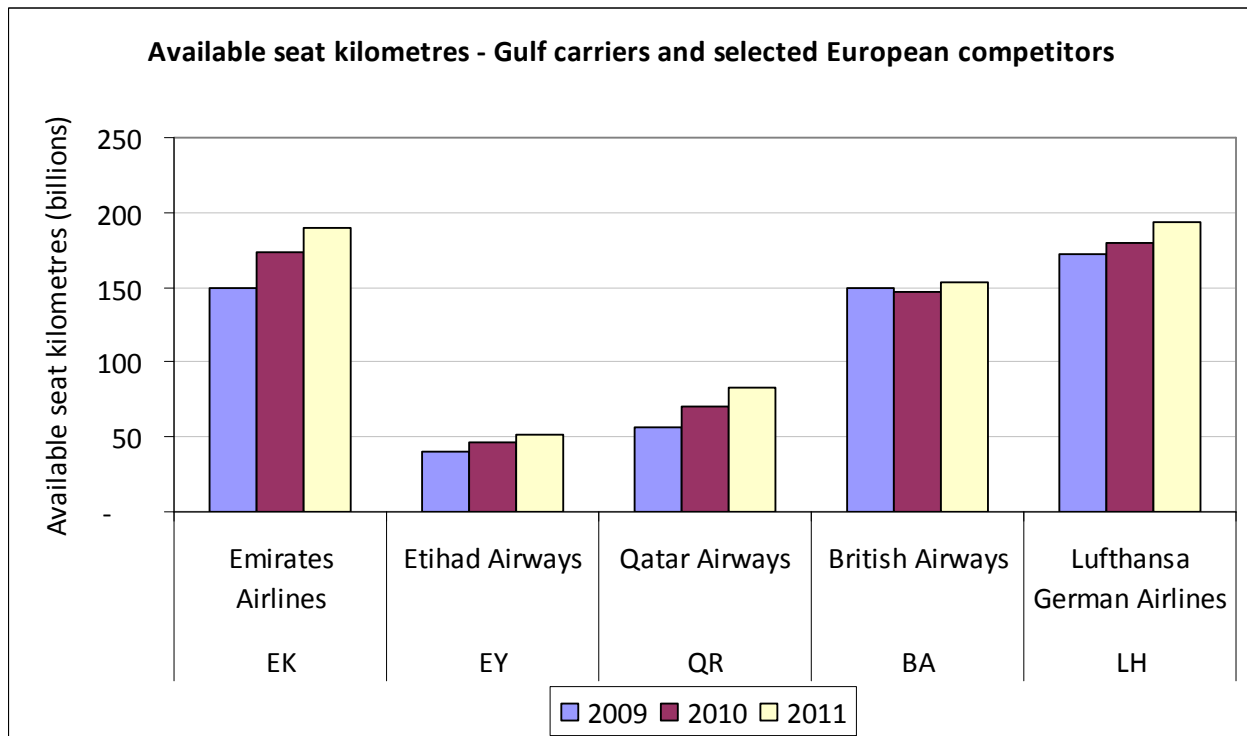
The following graph shows the annual growth rates for each of the three carriers which ranges between 10 and 20%. Although such growth rates would appear to defy prevailing market conditions in the rest of the world, they can be seen to more than justify the highly aggressive fleet procurement and route development strategies of all three carriers. The key issue will be, can it be sustained?

Gulf carriers percentage growth in passenger numbers 2007-2010



Source: Mott MacDonald analysis of ATI data

Gulf Carriers development of Available seat kilometre(ASKs)



Source: Mott MacDonald analysis of OAG data

Emirates carried 31.4 million passengers in 2010, which would place it as a similar size to British Airways which carried 30.6 million passengers during 2010. Qatar Airways carried 12.9 million passengers in 2010 which is comparable to SWISS who carried 14.2 million. The youngest and smallest of the airlines, Etihad carried 7.1 million passengers in 2010, which would place it as twice the size of bmi British Midland.

In terms of Available Seat Kilometres (ASKs) Emirates is now the 4th largest carrier in the world behind the American giants of United, Delta and American Airlines. The Gulf carriers are also expanding their available seat capacity at a rate far exceeding that of their European peers. For instance Emirates increased ASKs by an AAGR of 12.7% between 2009 and 2011, Etihad by 12.9% and Qatar Airways 21.2%, British Airways increased ASKs by 1.2% and Lufthansa 6.4%. While it would be expected that the more established European carriers with a larger short haul network would increase capacity at slower rate, the sheer difference is considerable.

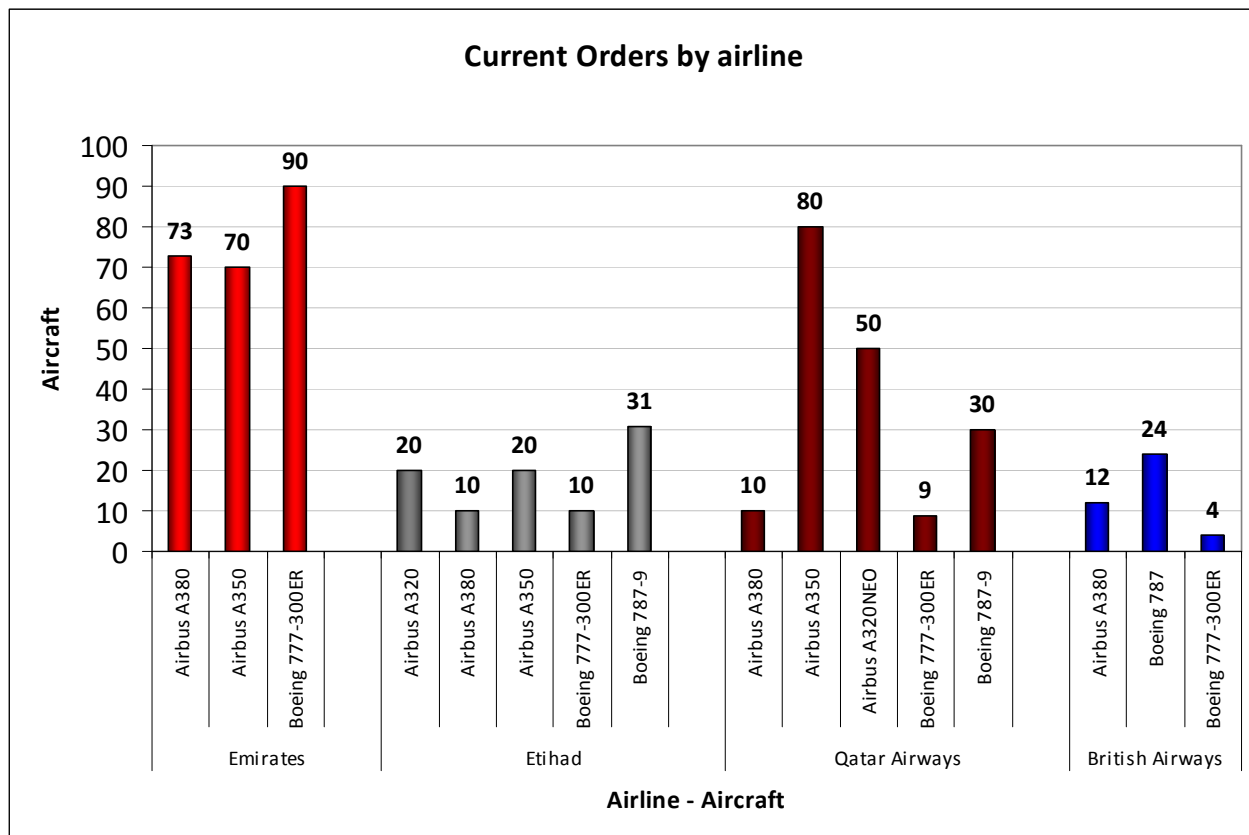
All three airlines also maintained positive traffic growth during the recession of 2008 and 2009

2.1.6 Fleet Development

One of the most significant aspects of the MEB3 Gulf carriers development is the extent of their ambitious growth plans. At the recent (November 2011) Dubai Airshow, Emirates placed an \$18bn order for 50 Boeing 777-300ER aircraft, each typically seating 300-400 passengers. Qatar Airways also placed a \$6.4bn order with European manufacturer Airbus for 55 of its new ultra efficient short range jet the A320NEO and for an additional 5 Airbus A380s. Etihad also has a substantial order book for 91 mainly long range wide-bodied aircraft.

The chart below shows aircraft orders for the three Gulf Carriers as well as orders for British Airways to provide a comparison. At the time of writing, Emirates has orders for 233 aircraft, Etihad for 91 aircraft and Qatar Airways 179. By comparison, British Airways currently has orders for 40 aircraft.

Current Orders by airline



Source: RATI and Airline websites

2.1.7 What does this mean for Europe?

The significant aircraft orders are good news for Airbus who has 345 orders from the Gulf carriers or 68% of the 503 aircraft on order. These orders will help to safeguard jobs at the various Airbus plants across Europe. Even the Boeing orders will be beneficial to a large number of component suppliers in Europe.

In addition the impact on many European airports will be major. The larger hubs in Europe will have to accommodate increasing numbers of Airbus A380 aircraft as capacity constraints get ever tighter at the most congested airports and the carriers seek to maximise the number of passengers carried per movement. But that in turn may mean a loss of some of the regional feed services from peripheral parts of the EC. This could be exacerbated if the EC change the current Slot Allocation rules and allow increased slot trading.

There is little doubt that given their strong financial backing, corporate focus, success and overall business strategy the Gulf carriers would be in the market to acquire any slots, particularly at the most congested hub airports both now and in the future.

An analysis of the top ten points served by Emirates, Etihad and Qatar airways confirms that despite their extensive European networks, it is still the primary European hub airports that dominate in terms of service and frequency.

For Emirates London Heathrow dominates its seat production with some 772,000 seats. The next largest is Bangkok at 575,000. The largest EC regional airport service is Manchester with some 375,000 seats. For them gaining another pair of slots at Heathrow would potentially represent significant value in terms of network traffic and overall revenue. With Heathrow down to only 6 UK regional points served, the potential threat is significant. What Heathrow experiences today, then other EC airports whose capacity is already at a premium, particularly within the next 10 years (based on EUROCONTROL forecasts), will also face, with potential consequences to the EC regions and connectivity.

The approach for Etihad and Qatar Airways can, in some cases be different to that of Emirates as its operation of 150 seat A320s means that it can access more smaller markets in Europe more economically, therefore potentially provide a wider range of opportunity to such EC regional points for connecting service via Doha to the Middle East, Asia, and the Far East.

What the MEB3 carriers do not offer to Europe and could not unless they brought a minority share in a European carrier is improved service or access, particularly for the secondary EC airports to North America. Neither the geography nor current bilateral requirements would allow that. But any further relaxation of bilateral rules, allowing additional 5th freedom operations, could change that. In such an instance the Gulf carriers have the wherewithal, motivation and fleets to exploit such an opportunity, but EU political will and legacy carrier lobbying may work against that due to the balance of opportunity arguments.

2.1.8 The Gulf Carriers European network

The OAG airline timetable data shows that a total of 15 European airports were served either individually or collectively by the three Gulf airlines in 2003. The vast majority of these were either major capital cities such as London, Paris, Rome and Brussels or significant business centres such as Frankfurt (Germany's capital in aviation terms) and Dusseldorf. Emirates in particular have also sought to serve markets where significant Asian immigrant communities are found such as Birmingham and Manchester. The relatively low prices and wide choice of flights have proved popular to travellers to these countries, avoiding the need for a transit at either London Heathrow or another hub in Europe (and any potential additional visa requirements).

A recent trend has seen Qatar Airways make use of smaller narrow body aircraft such as the Airbus A320 to open routes to cities in Central and Eastern Europe. This is of particular benefit to consumers in these regions who now have access to the carriers global networks, but can also bring economic benefits to the regions themselves. For instance – cities such as Bucharest and Sofia are now 1 stop from destinations such as Melbourne, Tokyo and Beijing via a hub that avoids significant backtracking to one of the major European centres.



The flexibility afforded by these smaller aircraft allows a more diverse range of markets to be served. For instance, it is unlikely that Bucharest would be able to provide enough origin or destination passengers to provide a daily flight with more than 250 seats, but a 136 – 150 seat Airbus A320 is a more suitable aircraft for this market at required frequencies.

2.1.9 The advent of the Boeing 787 and Airbus A350

The next generation of medium and long haul aircraft are expected to provide substantial improvements in operating costs plus significant improvements in payload range capability. For example Boeing claims that the Boeing 787 will burn 20% less fuel than its predecessor, the Boeing 767. Airbus claims that its slightly larger A350 series will have 25% lower operating costs than its existing rivals, whilst opening up new direct long haul operating capability.

Both the B787 and A350 will offer viable payloads (i.e. passenger loads) on sectors of 8,500 nautical miles. That means that parts of Australia can be accessed direct from points in Europe without the need for technical or traffic stops or making connections. As such, viable direct operations to a range of non-stop points in the Far East and potentially Australasia, from a range of points in Europe. For example the greater range and increased cargo capacity afforded by a Boeing 787 could theoretically make a whole host of new routes viable. The predecessor to the 787 – the '767' offers a typical range of 7,500km with a maximum load of passengers and baggage (Frankfurt to Dhaka, Bangladesh). The 787 would carry the same load from London to Perth!

If such developments were to take place then the need for traffic to and from Europe to connect over the Gulf airline hubs would potentially reduce. The only real counter to such development would be the established networks and service opportunities that the Gulf carriers offer and pricing incentives to keep the traffic connecting.



2.1.10 Fares and pricing policy

One of the main weapons used by the Gulf carriers to attract traffic onto their services, other than providing direct service to an increased number of secondary cities in Europe, is use of the price mechanism.

Using a sample of fares for both economy and business class travel for typical routings from London to Hong Kong and Singapore results in the following outcome:

2.1.11 Fares Comparison – London to Hong Kong and Singapore case study

Fares Comparison – London to Hong Kong

Analysis of Airfares					
	Date	Direct	Carrier	1 Stop via M. East	Carrier
London to Hong Kong	Jan 14-21	£748	Cathay Pacific	£796	Qatar Airways
Economy	Jan 16-20	£828	Cathay Pacific	£692	Emirates
London to Hong Kong	Jan 14-21	£2,823	Virgin Atlantic	£2,212	Emirates
Business	Jan 16-20	£4,666	Qantas	£2,177	Emirates
London to Singapore	Jan 14-21	£962	British Airways/Qantas	£648	Emirates
Economy	Jan 16-20	£789	British Airways/Qantas	£613	Emirates
London to Singapore	Jan 14-21	£3,175	British Airways	£2,233	Emirates
Business	Jan 16-20	£4,347	British Airways	£2,198	Emirates

Source: IATA Trip software. Retrieved 25/11/11

Of the four economy itineraries queried, the Gulf carrier was the cheapest option by between 20% and 49% on 3 occasions. In terms of Business Class fares the Gulf carriers proved cheaper for all itineraries by very substantial margins.

2.1.12 State subsidy and support

If the airlines were EU carriers then State subsidy / support would be an issue. A number of EC airlines have failed e.g. Sabena or had massive reorganisation such as Olympic and Alitalia and others due to the stringencies of EC State Aid Rules. These rules do not apply internationally and are not covered under ICAO but it does potentially give such airlines in support of aid a potentially unfair competitive advantage.

It is understood that Etihad has yet to make a profit and is still supported by the Government of Abu Dhabi. It is suggested that all three airlines have had or continue to receive State support or guarantee loans for aircraft etc. This will enable them to achieve financial terms that are potentially superior to those available to many EC based major carriers with whom they compete.

2.1.13 Environment

Although routing via a hub can bring significant economic and financial benefits to airlines and airports, from an environmental perspective, routing via the Middle East means more take offs and landings per passenger than if that passenger were to travel direct.

2.1.14 Political climate

So far the impact of the Arab Spring and associated political turmoil has had a very limited impact on the three carriers.

Some have admitted some lost traffic and revenue, but at the margin only.

However, the events of early 2011 and the overthrow of totalitarian regimes in Egypt and Libya plus the riots in Bahrain must have caused some stock-taking by both the airlines and the Governments of the three states.

Although we understand that the potential political tensions are not as prevalent, any further spread of unrest could have implications to the three carriers, most particularly on the willingness of passengers to transit such areas at times of uncertainty.

2.2 SWOT Analysis of the MEB3 carriers

STRENGTHS

Concerted backing and direction for the airline and airports of the three Airlines from their respective Governments.

Availability of financial backing.

High standard of service and established reputations

Geographic position in relation to the major world markets

Lack of organised labour

Identification of hitherto underserved markets

Modern fleets and committed forward order books

Unconstrained home bases with commitment for future expansion and development and ability to leverage hub model at limited cost but with maximum benefit

WEAKNESSES

Small home markets

Heavy reliance on ex-patriot labour

Inability to serve some major markets: Europe to North America and South America

Growing competition for same markets from hubs only a few hundred kilometres apart

OPPORTUNITIES

Deregulation of world air transport market (as has happened with sea transport)

Changes to the airline ownership and control rules in Europe and the USA allowing one or more of the carriers to buy a US or European affiliate.

Continued constraint on the development of airport infrastructure particularly runways in Europe at the major hub airports.

Not being bound by local APD or ETS regimes or requirements.

Association with major oil producing states

THREATS

Any extension of the Arab Spring rebellion into the Gulf Region

Instability in Iran or Saudi Arabia

Development of new direct air services between points in Europe and Asia by the new B787 / A350 aircraft, by passing the Middle East.

3. Appendix (A) – MB3 carrier – European points served.

Emirates (29)

London Heathrow,
London Gatwick,
Birmingham,
Glasgow,
Manchester,
Newcastle
Dublin
Paris CDG,
Nice Copenhagen
Amsterdam
Madrid
Frankfurt,
Munich,
Dusseldorf,
Hamburg
Geneva,
Zurich
Vienna
Prague
Rome,
Milan,
Venice
Malta
Larnaca
Athens
Istanbul
Moscow,
St Petersburg

Etihad (14)

London Heathrow, Manchester
Dublin
Paris CDG
Brussels
Dusseldorf, Frankfurt, Munich
Prague
Geneva
Milan
Athens
Larnaca
Minsk
Moscow

Qatar Airways (24)

London Heathrow, Manchester
Paris, Nice
Barcelona, Madrid
Milan, Rome, Venice
Frankfurt, Munich, Stuttgart, Berlin
Vienna
Copenhagen
Stockholm
Oslo
Vienna
Budapest
Sofia
Bucharest
Athens
Istanbul
Moscow