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Deregulation of Ground Handling on six European Airports

1. Ground handling – what is it good for?

Ground handling is the barely noticed service between flights and very important for the airlines´ performance ant therefore competitiveness. It consists of different services with different market structures. Cargo and Passenger handling being completely open to competition, whereas ramp and baggages services have mostly limited competition. The central infrastructure (including bridges, baggage conveyor belts, waste- and water-facilities, fuelling facilities etc.) on the other hand is provided by one supplier.

Providers of ground handling services can be airlines, airports or independent third party providers. Airlines can service their own aircrafts (so called self handling) and can provide this service to other carriers (so called third party handling). Consequently, airports and independent handlers provide third party handling only. Most of the independent handlers offer their services at several airports, either worldwide or in certain regions of the world.

Global players serve up to 165 airports in 36 countries and have revenues up to 1 billion USD. They usually have fairly small market volume at these airports with an average of 20.000-30.000 turnrounds per year. The biggest independent supplier at one airport at the other end is Fraport, serving 80% of the turnrounds in Frankfurt which added up to 191.000 turnrounds in 2004.

2. Deregulation – why now?

Liberalisation of the airline industry during the last two decades lead to far-reaching changes in the aviation market structure with strong impact on ground handling business. Competition between airlines lead to the fact that quality is mandatory for airlines. Differences between airlines “in the air” are decreasing, their competitive advantage is more and more on the ground: check-in, lounges, punctuality, transfers, baggage delivery times.

But the financial situation of airlines lead to pressure on ground handling prices and more selective use of services. Structural changes like building of airline alliances and hubbing as well as the emergence of low cost carriers changed the needs of airlines. Multi-station contracting, transfer processes and reduced services becoming more and more important when discussing ground handling contracts. Worldwide crisis with the sudden reduction of flights and increasing security needs complete the view of changes in the aviation industry that have major impact also on the ground handling scene.

In the beginning of the 90´s, right after the deregulation of the European Aviation Sector, airlines demanded competitive structures from their suppliers. Ground Handling being one of them with mainly monopolistic market structures at that time in Europe. This is how the deregulation of ground handling started, which – for now – was finalized in the EU-Directive 96/67/EC.

3. Directive 96/67/EC – what is it about?

The mail goals of the EU introducing competition to a formerly mostly monopolistic market were to lower prices, increase quality and give airlines the possibility to choose. Therefore, the Directive sets standards that have to be met by all member states, who have to transfer the Directive into national law. By the beginning of 1999, almost all member states had implemented the Directive and started opening up the market.

This paper will concentrate on airside activities, not analysing passenger and cargo services. With the possibility to restrict the number of competitors for ramp, baggage, fuel and oil handling as well as some parts of freight and mail handling, the EU acknowledged the special circumstances these services are in. Member states (not airports themselves) have to ask for such a limitation which is only granted, if special restrictions apply at the relevant airport (like capacity or security problems). The threshold for competition on the ramp for airports is 2 Mio. Passengers per year. The tender process is also described in the Directive, it is supposed to be non-discriminatory and licences can be given out for up to seven years. The Directive also allows to keep facilities of the central infrastructure in one hand.

The first results after several years of competition are described in a study, the company SH&E published for the EU in October 2002. Prices fell between 5 and 50%, the development of quality levels differ from airport to airport and from customer to customer. Problems nominating the competitors occurred at several airports, objections were filed by companies that were not given a licence which postponed market entries at several airports. Airlines didn´t use the new possibilities to self handle very often and also the switching handlers took up speed very slowly.

Right now, the EU is already planning on further opening up the market with a revision of the Directive of 1996. The first proposal is supposed to be officially published in the middle of 2005, the revision is expected to be implemented by the member states in 2008. Some of the possible changes affect the increase of the minimum number of third party handlers at airports with more than 10 Mio. Passengers and a wider definition of self handling which would allow airlines to “self handle” alliance partners. Furthermore the industry is expecting a rule concerning the legal unbundling of airports and their ground handling business. This could lead to an forced outsourcing of ground handling for some airport companies. Additionally, the licences are expected to be prolonged from 7 to 10 years.

4. Living the Directive – what is the market like?

An empirical analysis of the competition at six major airports in Europe show similarities as well as differences. Up to now, the five biggest European Airports have been analysed, the Airports visited are LHR, FRA, CDG, AMS and MAD (FCO will soon be analysed). Interviews have been carried out with several experts in the relevant markets to learn from their experience about market entry and competition "on the ramp". The interview partners represent a market share of the ground handling community at the respective airports between 70% and 100%.

All the airports are hubs of their national carrier and the respective Alliance. They handled Passenger volumes between 28 and 67 Mio. and 310 - 500.000 aircraft movements in 2004. The airports all have different situations to deal with concerning their ground handling markets. Some airports have a completely deregulated market, like LHR and AMS, others do have a restricted number of providers.

On the supplier side, this leads to 11 ground handling companies in LHR and on the other end to 2 competitors in MAD and FRA. Three airport companies offer ground handling themselves, while the others leave this field to airlines and third party handlers. On most airports, at least the home carrier and sometimes also other airlines are providing self handling, which is usually combined with third party handling. Only two airports have self handlers that don´t offer additional third party handling and at one airport not even the home carrier uses the possibility of self handling.

The volume of third party handling in percent reaches from 27% in Madrid, having four selfhandlers, to 100% in Frankfurt , having no self handler. In turnrounds (which is ½ movements and commonly used in ground handling) the volumes spread from 54.000 turnrounds in MAD to almost 240.000 in FRA.

On the demand side, the customer structures are very different too. Focussing on alliances, CDG, AMS and FCO are Sky Team-Hubs, LHR and MAD serve as a One World Hubs and FRA is the only Star Alliance Hub. This might be the reason why Lufthansa and Star Alliance have this dominant position at their hub with 72% of total market share of this airport. Compared to the presence of the other alliances at their hubs with One World having 50% in LHR and Sky Team 61% in CDG (and the other three hubs in between), Star Alliance in Frankfurt is by far the most powerful customer group.

In a sustainable market, no additional supplier wants to enter the market, because he doesn´t see a chance to be successful. Looking at the six airports and the ground handling scene, the picture is as different as described above. The markets in Amsterdam and London are fully liberalized and seem to be sustainable. One supplier left London in November 2004 and a new ramp handler entered the market. In Amsterdam, one handler exited after two years of service and wasn´t replaced at all.

In Frankfurt, the market seems to be attractive for further handlers from the competition side. The reason here for the limitation of handlers is capacity related, space on the apron is very limited. Problems concerning the contestable market exist in Paris and Madrid. Paris might be interesting for new handlers but since it has limited the scope of the licences to certain terminals, there might not be enough volume for another handler (only if this artificial barrier to entry would be lifted). Madrid has currently four selfhandlers and just enough third party volume for two suppliers. The airport has capacity problems too, but as soon as the new terminal is opened in 2006, this won´t be an issue anymore. Rome still has to be analysed.

5. My thesis – what is it about?

The scope of the thesis is to analyse the industry, to look at the theoretical background that describes the ideal market situation and to compare the theory with the empirical evidence. Not only the goals of the EU - reduction of prices and increase in quality – will be analysed but mainly the effects of the Deregulation for suppliers, being incumbents and entrants. Finally, propositions will be made on how to improve the situation from a regulatory point of view as well as a an outlook on strategies for ground handling companies to deal with the changes in the industry.