European Parliament

Low-cost air carriers and tourism

The liberalisation of air transport, which resulted in the creation of new routes and new business models for airlines, in particular the development of low-cost carriers, has led to lower fares and wider access to air transport. In many countries, air transport is a catalyst for tourism development. As low-cost carriers in the EU have experienced substantial growth, serving mostly short-haul destinations, they are increasingly looking into investing into the long-haul market for their future development.

Connection between air transport and tourism

According to the United Nations World Tourism Organization (UNWTO), the growth of air transport is strongly related to the expansion of tourism, as the large majority of international passengers travel for tourism reasons, and in many countries air transport is a catalyst for tourism development. For some experts, the relationship is more complex. While air transport triggered the development of international leisure travel, airlines have taken tourism into account to develop their strategies in terms of pricing, positioning and new routes, a process which has intensified with the emergence of low-cost carriers.

According to UNWTO figures, in 2015, air transport represented over half (54 %) of all international arrivals, while road, water and rail accounted for 39 %, 5 % and 2 % respectively. In the past three decades, air transport grew faster than other modes, at an annual average rate of 5.2 %, while the figure is 3.4 % for land/sea. Air and road transport are by far the primary choices for international tourists, while rail and water, for instance international train stations, have a key role in distributing visitors to and around their destination.

Low-cost carriers' growing importance

The rapid growth of tourism and air transport is explained by two major factors. The availability of higher incomes and a growing middle class in emerging economies, inclined to increase their travel expenditure; and air transport liberalisation, which resulted in the creation of new routes, new business models for airlines, such as charter and low-cost carriers (LCCs), and has led to lower fares and wider access to air transport.

In the EU, the liberalisation of the intra-EU aviation market in particular boosted traffic growth. While the different types of airlines (network carriers, charters and low-cost carriers) had similar growth rates in 1992-2002, the low-cost segment subsequently began to increase its market share substantially. Almost non-existent before 1995, by 2012 the low-cost sector had left the network carriers' sector behind and by 2015 represented 48 % of seat capacity.

Liberalisation of the airline industry has an impact on the size and location of airports. In the countries or regions that witness a substantial expansion in the low-cost sector, such airlines tend to offer single-class services that are point-to-point, rather than hub-and-spoke system integration. They also tend to operate from the low-cost terminals of traditional airports or from smaller regional airports. Low cost carriers in turn contribute to improving accessibility, the number of destinations available, and enable some destinations served by regional airports and their local economy to grow. Although the choice of a tourist destination relies primarily on the location's assets in terms of natural, cultural and local resources, it also relies heavily on the costs and time needed to reach the destination. Passengers increasingly perceive air travel as routine. However, they are also price- and value-conscious, willing to use non-traditional carriers, routings and airports to get the best fares – including low-cost carriers to smaller or regional airports, which are not always as well connected as airport hubs near major cities. Some experts go further, pointing out that LCCs have modified traveller behaviour. Visitors now integrate into local society and use the web to buy their tourist package directly. LCCs also spur interest in secondary destinations, and newly developed areas, as opposed to

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Author: Ariane Debyser, **Members' Research Service**
PE 607.263

eprs@ep.europa.eu – http://www.eprs.ep.parl.union.eu (intranet) – http://www.europarl.europa.eu/thinktank (internet) – http://epthinktank.eu (blog)

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traditional Mediterranean and beach destinations. Other commentators underline, however, that traditional carriers will maintain their position because there is a segment of travellers who find traditional transport more useful and because of the limited expansion to date of low-cost carriers on long-haul routes.

Beyond Europe, while the share of LCCs is strong in the EU and in the United States – the birthplace of LCCs – they are also expanding worldwide. LCCs have taken advantage of the progressive deregulation of domestic markets and of the fact the market-orientated air services agreements are becoming increasingly the new international norm. However, in some world regions, such as Africa, market access barriers remain high.

Evolution of business models and outlook

The low-cost airlines' business model tends to focus on point-point routes, mostly short-haul, and is less complex than the hub-and-spoke networks of legacy airlines, which operate one or more hubs and combine feeder traffic with long-haul routes. The LCC model also involves frequent flights along profitable routes, focuses on fleet productivity, with most aircrafts in the air most of the time, and uses only limited types of aircraft. In the EU, low-cost airlines also concentrate on intra-EU services or on countries covered by EU-level comprehensive agreements that ease pan-European operations.

Over the last ten years, however, convergence between low-cost and traditional airlines has increased. Confronted with increased competition from LCCs, traditional airlines have started to dissociate charges for seat selection and luggage for instance, and to streamline operating costs. Conversely, to maintain growth, LCCs have begun to place greater emphasis on customer services, some offering assigned seats and frequent flyer cards, features associated with established airlines. Low-cost carriers have also increased their presence at hub airports and widened the distribution network for their products.

As LCCs are particularly strong in the USA and the EU, and tend to saturate the short-haul market, they will increasingly rely on the long-haul market for future growth. Growth opportunities through use of secondary airports will also reach their limit. A change of strategy will imply fleet diversification, operations through a wider network, and developing access to strategic hubs, which raises fixed costs and reduces flexibility. Nonetheless, LCCs have yet to demonstrate their ability to capture the long-haul market. While new middle class travellers from emerging economies are likely to demand lower cost travel solutions, traditional and LCC operators may continue to compete, maximising their comparative advantages, such as price versus service.

In the Commission staff working document accompanying the aviation strategy for Europe, different possible scenarios for the future of European airlines are outlined, and may be combined. As far as LCCs are concerned, these covered: continued LCC and legacy carrier co-existence on short and medium haul flights as at present, with no significant breakthrough from LCCs on long-haul flights; legacy or traditional airlines positioning themselves on the long-haul market only, while LCC predominate on short and medium-haul routes; or Europe progressively losing transfer traffic to Middle Eastern hubs, with Western-oriented hubs reduced to secondary hubs. In a last scenario, LCCs dominate European airports and traditional carriers shrink and disappear. In its resolution of 16 February 2017, the European Parliament stressed the vital importance of the aviation sector for the development of tourism.

Developments in the low-cost long-haul market

In December 2016, the US Department of Transportation (DOT) granted Norwegian Air International (NAI) a foreign air carrier permit to operate transatlantic flights to the USA. The authorisation, expected to substantially increase low-cost transatlantic flights, was subject to criticism from European and US network airlines and labour organisations. This was notably on the grounds that the authorisation is counter to Article 17 bis of the EU-US air transport agreement, which mentions that 'opportunities created by the agreement are not intended to undermine labour standards or the labour-related rights and principles contained in the parties' respective laws'. Although recognising, the above concerns, the DOT decision nonetheless concluded that the EU-US agreement was not a basis for rejecting the application. Pilot and labour associations filed a petition in court challenging the decision, and might appeal to the US Congress and the new administration to reverse the order. NAI is expected to begin operating between European and US cities in mid-July 2017. Another LCC step towards the long-haul market segment is the International Airlines Group (IAG), parent company of British Airways, Iberia, Aer Lingus and Vueling, decision to launch a new low-cost long-haul carrier, named 'Level', in June 2017. This new entity will initially operate flights from Barcelona to Los Angeles, San Francisco (Oakland), Buenos Aires and Punta Cana. Some analysts nonetheless challenge the applicability of the LCC business model to long-haul flights.