

STATE AID AND THE PROVISION OF AIR SERVICES IN SPANISH AIRPORTS (1996-2010)¹

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INTRODUCTION

This paper quantifies State aid to airlines in Spain for the first time. Results are based on a compilation of the subsidies granted by Spanish regional and local governments to various air transport companies during the period 1996-2010. The first part offers an overview of the mechanisms provided in European Union legislation to channel state aid, as well as the existing relationship between subsidies and the increasing competition among airports. We then present the different sources of the compiled data, discussing the difficulties in obtaining accurate information on payments. In the third section we analyse in detail the resulting amounts of subsidies and their distribution among airports and companies. Finally we explore the variable cost of transporting an air passenger, depending on the company or airport involved. We conclude with a reflection on the advisability or otherwise of financing new air services, indicating an urgent need to include social, environmental and energy questions in the debate if we want to avoid a decision making process based on overly simplistic arguments.

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I. STATE AID TO AIR TRANSPORT IN EUROPEAN UNION REGULATIONS

The triumph of neoliberal economic theory in the last quarter of the 20th century had a clear effect on transport policies throughout the world: market mechanisms were widely used in the provision of transport services, limiting the role of the State to a mere market regulator or an investor in infrastructures which were not profitable enough for private enterprise. The liberalisation of transport markets and privatisation of the former public operators were the usual corollary of these positions. In this context it can be better understood why at the end of the eighties the former European Community started to liberalise the air transport market. Liberalisation meant State subsidies for air transport were prohibited, and public administrations could not directly subsidise any airline to ensure its profitability, even if publicly owned, or grant specific support for the operation of certain air links.

Liberalisation rules had some exceptions to allow some types of existing State subsidies, although using mechanisms ensuring greater transparency. In certain circumstances public funds could be transferred to flagship companies (DOCE, 1994) and some air links within the European Community could be declared public service obligations (PSOs), opening the door to direct subsidies for those routes.

However, these two mechanisms are not the only ones currently used to subsidise airlines in the EU market. There are others that fall outside the law but are widespread within the European Union. This is why in February 2005 the European Commission presented a proposal for guidelines, later adopted (DOCE, 2005), authorising State aid to airlines to start new routes to regional airports with an annual traffic of less than five million passengers.

The adoption of these guidelines seemed to open a new phase, with competition between airports as well as between airlines. This was predictable in a context of market liberalisation and increased private capital in airports. This led to a growing number of airports focusing on attracting airlines and diversifying their air links. Hence the boom in recent years of airport marketing, a set of techniques designed to achieve those objectives, which besides advertising and attending trade fairs, includes economic incentives to facilitate the opening of new routes (Graham, 2003; Halpern and Niskala, 2008).

But these new rules did not prevent a continued flow of government subsidies to airlines through informal channels, not recognised in European legislation. This was reflected in regular news items in the European media, and officially confirmed by a detailed audit of French airports by the French Court of Audit (Cours des Comptes, 2008).

II. SOURCES FOR THE STUDY OF STATE AID TO AIRLINES IN SPAIN

In the first section we showed that there are only two legal mechanisms through which governments can promote air links: they may impose a public service obligation (PSO) on routes which are vital for the economic development of a region, or subsidise the opening of new routes, according to the conditions set in the 2005 guidelines. However, official data provide a very partial picture of reality; in fact, many more air routes operate thanks to funds from public administrations. The greater transparency, public disclosure and control required by legal funding channels are, paradoxically, among the factors explaining the lack of interest in these instruments from the institutions promoting air links.

This behaviour, far from the transparency that should guide public management, explains the difficulties found when attempting to obtain detailed information about such grants. Despite this opacity we compiled a database enabling an approach to the phenomenon, based on four types of sources:

- Local press provided a very useful overview of the spatial distribution of these subsidies and different formulas used to promote the opening of new air routes.
- The Official Gazettes of autonomous regions and provinces allowed us to trace funds awarded through public tenders and, therefore, included in these official publications.
- The minutes of plenary sessions of regional governments record the various interventions of these bodies. As in recent years the political debate about the appropriate formulas for attracting low-cost carriers reached several regional governments, in some cases the minutes record the amounts paid to certain companies.
- Finally, in the case of the Valencia Region, reports from the regional Court of Accounts, an independent body created to control the public sector, were extremely useful.

The information from these sources, although incomplete, lets us identify different mechanisms used to channel funds and provide a first estimate of the amount of such aid and its spatial distribution.

III. AMOUNTS AND DISTRIBUTION OF STATE AID

From 1996 to 2010, several Spanish regional governments paid a minimum of 297 million euros to facilitate the start up or ensure the viability of air links in 26 airports. Undoubtedly, this figure is lower than what was actually transferred, but it gives a rough idea of how extensive the practice had become. The amount per year shows a gradual increase in investment over the period considered, becoming more marked from 2005. In 2010, the last year considered, investment was about 42 million euros, nearly matching the 2006 peak (Figure 1).

Over 80% of these funds were allocated to Air Nostrum and Ryanair (Table 1). In third place is Lagun Air, a short-lived company that received preferential treatment from the Junta de Castilla y Leon in its attempt to boost the region's airports. In fourth place we find Vueling and Clickair, now merged, which received a major injection of public funds from 2007 on. Although Air Nostrum, a franchisee of Iberia, has been a privileged aid recipient, in 2010 Ryanair virtually matched it, both in the amount of subsidies it receives and in the number of airports where it operates thanks to this aid. Its gradual expansion into domestic routes which had hitherto relied on Air Nostrum is the most plausible explanation for this change.

As expected, most of the airports benefiting from these grants have low traffic figures (Figures 3 and 4). Of the twenty-six airports with public support, fourteen have annual traffic of less than half a million passengers (Table 1). They are part of what we have defined as small regional Spanish airports (Gámir Orueta and Ramos Pérez, 2011), serving small or medium provincial capitals located in areas with low economic dynamism. As significant investment in road and rail networks has reduced access times to other nearby airports with a wider choice of flights, we can understand that potential demand is limited.

While a majority, they only account for 35.3% of the funds transferred to the airlines during the period studied. Their difficulties in ensuring a minimum of traffic are attested by the fact that seven of them were completely dependent on aid in 2010. Zaragoza and Valladolid are the only ones in which Ryanair already has a established presence. In the remaining airports Air Nostrum operates almost exclusively.

A second group consists of eight airports with traffic volumes of one to two million passengers. These airports are located in the geographical periphery of Spain, mainly on the Cantabrian coast and in the Southeast. This group has captured 28.3% of aid, although investment has been heavier in Santander and Reus. Except for Reus, these airports have a wider range of airlines than in the previous group, giving greater ability to cope with changes in airline strategy.

Finally, Alicante, Valencia, Girona and Fuerteventura airports handle well over four million passengers, but still benefit from generous State aid to Ryanair and Air Nostrum, accounting for 36.4% of grants since 1996, in a notable concentration of aid. These funds are notably highest for Valencia and Alicante. Both airports are the major beneficiaries of the outstanding contribution made by the Regional Government of Valencia to Air Nostrum during the studied period.

IV. HOW MUCH DOES IT COST TO START A NEW AIR ROUTE?

Latent demand for a route is no longer the sole determinant for the establishment of an air link: a route with low or very low traffic demand can start up if financial assistance is provided to absorb losses. Thus, it seems that the relevant question has become how much it costs to attract an airline to operate at an airport (Otto, 2010). The answer to this question depends on the airports and airlines considered. The database compiled tells us the annual cost per flight and per passenger for a large number of cases. Table 3 presents a selection of cases, grouped by airlines, which give a fair idea of the diversity of situations that arise.

The data show that the cost per passenger transported in routes operated by Ryanair is much lower than in routes operated by regional airlines such as Air Nostrum, Portugalia or the defunct Lagun Air. In fact, the cost of a connection served by Air Nostrum is very similar to that seen in multiple routes declared as public service obligation in the European Union (Williams and Pagliari, 2004).

The wide range of observations we have for Ryanair and Air Nostrum allows us to see that both companies do not always pose the same requirements. Thus, the lower the airline traffic at an airport, the greater the subsidy per passenger received for operating a route from it. At airports served by Ryanair this ratio ranges from 0.82 euros per passenger in Girona to 5.47 in Vitoria, or a ratio of 1 to 7. The differences between the airports where Air Nostrum operates are greater, from 4.7 euros per passenger in Murcia to 51.8 in Zaragoza, a ratio of 1 to 11. These variations in costs per passenger are also observed in other countries, as a study by the French Court of Audit reveals. Based on these data, Air France estimates that subsidies received by Ryanair would range between 9 and 32 euros per passenger in French airports (Amedeo, 2010a).

From the above it may be concluded that if Ryanair can provide a greater number of passengers at a cost far below that of Air Nostrum, governments could begin to sideline

the Iberia franchisee. The key question is whether Ryanair could take over the domestic flights operated by Air Nostrum. The answer is not simple, for several reasons. We recall that the presence of Air Nostrum in most airports, especially those with low traffic figures, ensures wide territorial coverage for the Iberia network, which is very important for the development of its Madrid hub. This key role was strengthened after Iberia's decision to boost intercontinental flights from Barcelona, as Air Nostrum and Vueling will be responsible for bringing passengers to those flights. Other questions concern transversal routes connecting airports outside Madrid and Barcelona. In fact, the entrance of Ryanair in some of these has already led to the withdrawal of multiple Air Nostrum links between airports in the North/Centre and in the South of the Iberian Peninsula (Santander-Alicante, Santander-Málaga, Valladolid-Málaga and Zaragoza-Sevilla).

V. CONCLUSIONS

To find out how much State aid is received by airlines and to assess the extent of this practice in Spain, the authors developed a detailed database providing the first reliable approach to the phenomenon. However, the difficulties found in compiling it and the need to use practically unpublished sources reveal a remarkable lack of transparency in handling public funds.

Whether one agrees or not with the widespread use of incentives to airlines to offer more flights from an airport, clear and detailed rules, accessible to all operators and linking economic aid to quantifiable objectives (number of passengers, routes opened, and number of flights per week) is much more desirable than the opacity prevailing to date. Only then would the principles of openness, transparency and free competition that should guide government actions be secured.

Transparency in allocation results in better monitoring of the use of public funds. A clear relationship between incentives and targets means governments are less subservient to the interests of airlines. As noted repeatedly by the Regional Court of Accounts for the case of Valencia (Sindicatura de Comptes, 2006, 149), the lack of assessment of the results obtained from such contracts is a marked weakness of the mechanisms used so far. This assessment would also show the real viability of the routes, a very important question for compliance with European legislation, which requires a gradual reduction of State aid over a maximum of three years, conditions which are rarely met in Spain.

While incentive schemes would be an option for tourism-related routes, public service obligations would be a better choice for those intended to open up landlocked peripheral areas. However, this should be strongly justified: as rail is consolidated as an alternative means of fast transport, it seems illogical to subsidise a concurrent air link.

On the other hand, it should be emphasised that low cost airlines mean lower costs for local and regional governments using economic incentives to start an air route. If governments end up preferring low-cost carriers, we should ask whether low fares mean maximum wellbeing, or conversely, if the social (O'Sullivan and Gunnigle, 2009), environmental (EEA, 2008) and energy costs (Nygren et al., 2009) involved foster a negative balance. The widespread low fare model has led to an extreme culture of competition among broad swathes of society, with companies and territories fighting for a piece of market share.

