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Turbulent skies: After a torrid year for the UK aviation sector, what next?

The Covid-19 pandemic has reached into all areas of the UK and world economy. Few industries, however, have been affected as significantly as aviation. It was one of the first industries affected by the pandemic, as national governments closed international borders to prevent non-essential travel and problems have come thick and fast over the following year. In addition to the impact of coronavirus, this snapshot examines the multitude of issues shaping the aviation industry in the UK and what to look out for in the coming year.

97%

The reduction in UK passenger numbers in 2020 compared to 2019

4.8m

The number of direct aviation jobs lost globally in 2020

"2020 has been a year that those within the aviation sector had never thought possible. The impacts of Covid-19 have been collectively worse than the effects of 9/11, the last global recession, the Gulf War and the Icelandic ash cloud of 2010 combined"

John Holland-Kaye, CEO, Heathrow Airport

In the UK, the Foreign and Commonwealth Office advised British nationals on 17 March 2020 against all non-essential global travel. Tens of thousands of holidaymakers and business travellers had their flights cancelled overnight. Around the world thousands of planes were grounded and left idle on the tarmac.

The resultant drastic fall in air travel—a 97% reduction in passenger flights compared to the previous year—has been devastating for the aviation industry, with estimates that the sector in the UK lost over £20 billion in revenue in 2020. The sector is of huge strategic and economic importance to UK PLC. Prior to the emergence of the pandemic, the UK had the largest aviation network in Europe and the third largest in the world, that contributed £22 billion to the UK economy, along with over 230,000 direct jobs.

After a bruising 2020, and to add insult to injury, it was announced in mid January that travel corridors were to be indefinitely suspended as the UK tried to limit the spread of new mutations of Covid-19. This in effect closed the travel industry and removed the few remaining revenue streams still in existence for the aviation supply chain.

Major airports

The debate around aviation in the UK has been dominated by the future of one airport for decades. The first government to propose a third runway at Heathrow was Clement Attlee's in 1949. Although the plans were not advanced in any meaningful way until the New Labour years, the need for additional runway capacity in the South East of England has been understood for some time.

Since the Brown Government announced its support for the construction of a third runway in 2009 the project has been cancelled by the Coalition in 2010, recommended by the Airports Commission in 2015, and finally approved by the House of Commons in 2018. This did not mark the end of the saga with the Court of Appeal declaring the plans unlawful on climate grounds in March 2020. This judgment was then overturned by the Supreme Court in December 2020.

Nevertheless there are still hurdles to overcome; there is the possibility of a further legal challenge calling on the Government to update the plans to take account of its 2050 net zero commitment and there will be a public inquiry. Even if all these hurdles are overcome – and the Planning Inspectorate gives its blessing – the final decision will still rest with the Government, which is currently led by a Prime Minister who is on the record as firmly opposing Heathrow expansion.

The reduction in demand resulting from the pandemic is likely to remove any urgency. Whilst progress has been glacial to date, the fact that demand is likely to be depressed for the next 1-2 years will give those in favour of expansion less ammunition with which to make their case. With all this in mind, it appears likely that it will be quite some time before construction gets underway.

Regional airports

One could be forgiven for thinking that the debate around aviation in the UK starts and finishes with Heathrow. This reflects a wider imbalance in the UK economy, with attention and investment focused on the South East of England. The Government has made much of its ambition to address this problem via the 'levelling up' agenda. Aviation has a role to play in this; growth in regional aviation has the potential to provide a gateway for investment, enhancing domestic connectivity and opening up international connections.

Through the number of jobs they create directly and in their supply chain, and the manner in which they support business growth, airports have the potential to be key drivers of economic rebalancing. In the most remote parts of the UK, aviation is a vital source of connectivity where travel by road or train is prohibitively time-consuming. This regional connectivity also feeds hub airports like Heathrow that provide passengers with onward international connections. The trouble that the Government went to in order to rescue Flybe is indicative of the political value placed on this regional connectivity.

In the ongoing debate over increased aviation capacity, regional airports have a particular role to play. It is government policy to make best use of existing runways. Unlike Heathrow and Gatwick, many regional airports have considerable flexibility to increase capacity without the disruption of building a new runway. Using this latent capacity could be an easy way to help drive regional growth.

In general, most regional airports rely heavily on leisure travel while business travel makes up a larger proportion of traffic at hub airports such as Heathrow. This could have implications for the immediate post-pandemic phase with demand for lesure travel likely to return quicker and more strongly than business travel. In a difficult year, this could be one positive to look forward to for airports outside the South East.

Airlines

While some major household names in other sectors have 'had a good crisis', UK airlines certainly do not fit in this catgeory. Certain airlines have been widely criticsed by politicans for using the pandemic as an excuse to radically restructure their business, including a large number of job cuts, while taking advantage of the Coronavirus Job Retention Scheme (CJRS). Meanwhile, other airlines have been attacked for alleged poor customer service by people who attempted to secure a refund after their flight was cancelled.

Airlines' refusal to offer refunds has also hit tour operators' ability to refund their customers. Under the UK's Package Travel Regulations, package holiday customers are entitled to a refund from their tour operator within 14 days, but unprecedented demand and the refusal of airlines to refund the flight element of the holiday meant operators were unable, or unwilling, to refund within the required timeframe, leaving customers angry and frustrated.

With the arrival of vaccines providing some light at the end of a very long tunnel, the main challenges for airlines are twofold: financial and operational. Airlines across Europe and indeed the world have been forced to go cap in hand to their shareholders and governments to keep the wolf from the door over the past year. A mixture of state aid and equity/debt issuance has kept a number of airlines afloat. However, the long term financial forecast for many businesses does not look rosy as depressed passenger numbers and Covid-induced operational constraints last for the remainder of 2021 and beyond.

Ground handlers

Ground handlers are the backbone of the aviation industry and provide fuelling, ramp services, baggage and cargo handling, cleaning, check-in, catering and security services to commercial planes that take off or land in the UK. Prior to Covid-19, ground handlers in the UK employed 30,000 staff at airports across the four nations. Ground handlers, like others in the aviation supply chain, have been significantly impacted by the precipitous fall in flight volumes and have been compelled to shed large numbers of staff. In the past, handlers have been partially neglected by government in the development of aviation policy with airlines and airports taking centre stage. This trend was continued in the most recent government aviation support package which inadvertently favoured airports over ground handlers.

Government support

The UK Government has implemented a range of measures enabling airlines, airports and ground handlers to benefit from taxpayer support. The Bank of England's COVID Corporate Financing Facility (CCFF) remains available to support companies' liquidity if they are investment grade in addition to the the Coronavirus Business Interruption Loan Schemes and other measures such as business rates relief. Judging by industry comments, the CJRS launched in April 2020 and now extended until the end of April 2021 has proved the most impactful intervention. Generous as this package may seem, it is clear that many businesses are struggling financially and with the return of pre-pandemic flight volumes years away, calls from businesses for a continuation of the CJRS and further sector specific assistance will only grow louder.

One of the most powerful industry-wide arguments is that aviation is unlikely to recover as quickly as domestic industries such as retail and hospitality. Once lockdown is lifted, there will be lingering consumer hesitancy about travelling abroad before the majority of the population is vaccinated. This is before the issues around Covid-19 variants and existing quarantine policy are considered. It will be interesting to see if the UK Government listens to the aviation industry's pleas for tailored ongoing support once restrictions are phased out in the spring.

Brexit

Aviation is one of the sectors seen as being well-served by the Trade and Cooperation Agreement (TCA) between the UK and the EU. Given aviation's exclusion from the WTO General Agreement on Trade in Services, the conclusion of a deal was very welcome. The TCA largely offers continuity and will allow operations to continue in very much the same way as they did before. The majority of air traffic rights will remain the same however carriers will not be allowed to use the fifth freedom of the air – the ability to operate services between destinations in the other jurisdiction. The TCA does however give the UK the ability to negotiate with individual member states to allow cargo flights to travel to an EU member state and then travel onward to a non-EU country, a common practice in cargo aviation.

The TCA offers continuity in other areas such as code sharing, licences and ownership, and control restrictions with flexibility maintained in regulations around leasing. Whilst providing continuity and connectivity there is clearly scope for further discussion between the two parties on a range of issues including further liberalisation of ownership and control restrictions.

There is also room for the UK to diverge in some specific areas of aviation regulation. Perhaps the most obvious area for a change would be the rules on runway slots. The 80-20 rule that only allowed an airline to retain an airport slot on the basis that it had used it for 80% of the time has been suspended across the EU in order not to incentivise nearly empty 'ghost flights' during the pandemic. This suspension has been 'grandfathered' into UK law and will stay in place until at least the end of March, although it appears likely that this will be extended further.

In future, the UK may wish to move towards its own slot regime. One possible avenue – that would be consistent with the Government's stated ambition of pursuing a 'Green Recovery' – would be to develop regulations stipulating that a certain share of slots must be dedicated to the most efficient aircraft with lower noise profiles. This links with the Government's wider approach of bringing together Brexit with the environmental agenda.

Aviation's role in the journey to net zero

Aviation businesses are understandably focused on their own survival at present along with the health and livelihoods of their of workers. However, in the longer term, aviation is likely to undergo structural changes with regard to demand and the degree of industry consolidation as a result of the unprecendeted disruption over the past 10 months. That transition provides an opportunity to rebuild the industry for a low-carbon future, something that airlines, airports and ground handlers have been grappling with for some time.

Even before the pandemic started, the industry was facing the challenge of reducing its carbon emissions in line with international goals to reach net-zero emissions by 2050. External forces that have lifted the case for sustainability—including customers and regulators worried about emissions and unpredictable future carbon policies—have shifted with the pandemic, as the industry's very survival seems to be at stake.

The industry has a good record on fuel efficiency: fuel burn per passenger-kilometer has dropped by half since 1990, according to the International Air Transport Association. The current crisis could provide forward-thinking businesses with a chance to prioritise

sustainability and justify the retirement of older, less-fuel-efficient aircraft and other assets.

Modernising fleets and improving operational efficiency are important; however, in the best case, estimates that annual industry growth will counter the emissions that they could save in this area. Carbon offsetting holds more promise, and it can help serve as a bridge while the industry takes action needed to reduce its own emissions over time.

The game changer in the fight against climate change however, aligning the industry's growth ambitions with Paris Agreement targets, is sustainable aviation fuel (SAF). Made from renewable feedstocks such as municipal waste and agricultural byproducts, SAF has already fueled more than 250,000 commercial flights. In addition, it is fully compatible with existing aircraft and fuel infrastructure. However, the scale of the challenge to shift to meainigful usage of SAF in the coming decade is daunting. In 2019, fewer than 200,000 tons of SAF were produced globally, a tiny fraction of the roughly 300 million tons of jet fuel used by commercial airlines. If announced SAF projects are completed in the next few years, capacity will scale to at least four million tons—about 1 percent of projected global jet fuel demand in 2030. To make SAF economically viable and scale production, a multilateral global regulatory framework alongside measures to stimulate demand and innovative ways to finance the transition will be required. In the UK, the Jet Zero Council, a partnerhsip between industry leaders and government, has been established to drive the delivery of new technologies and innovative ways to cut aviation emissions, including a focus on facilitating the delivery of large SAF plants and supporting R&D initiatives.

Conclusion

The aviation sector has had a torrid year, and the difficulties the industry faces are unlikely to subside rapidly. It is likely that – once restrictions are lifted – consumer confidence will only return slowly, with many having a lingering unease with regards to travel. Nevertheless, forecasts suggest that demand is expected to return to pre-Covid levels within the next two-three years, and it remains possible that many people will want to make up for lost time and venture abroad when given the chance.

Whilst the pandemic has presented enormous challenges, all crises also provide opportunities. In the case of aviation, there is clearly room for the industry to play a role in the Government's objective to 'build back greener' with progress on SAF and new engine technology likely to accelerate in the coming years.

More broadly, aviation will continue to be important to the Government's wider objectives. The 'Global Britain' agenda will necessitate the deepening of international trade links. Whilst remote means of communication have become more prevalent, there remains no substitute for meeting someone face to face. Aviation will be central in creating these links.

Having withstood a very bumpy 2020, aviation businesses large and small will be hoping for clear skies and smooth flying conditions as the long journey to recovery commences.

George Morris Seers
Director
+44 (0) 7971 744 895
George.Morrisseers@fticonsulting.com

Tom Pridham
Director
+44 (0) 7976 987 997
Tom.Pridham@fticonsulting.com

FTI CONSULTING