INTERNATIONAL AIRLINES GROUP

23rd August 2024

Luke Manning
Irish Aviation Authority
The Times Building
11-12 D'Olier Street
Dublin 2, D02 T449

Ref: Consultation on RP4 Performance Plan for Air Navigation Services Charging and Performance in Ireland

Dear Luke,

Thank you for the opportunity to respond to your consultation on the RP4 Performance Plan for Air Navigation Services Charging and Performance in Ireland.

On behalf of our Group airlines (Aer Lingus, British Airways, Iberia, LEVEL and Vueling), IAG sets out our views and position on the proposals below.

We support and endorse Aer Lingus' own separate response to this consultation in its entirety.

Executive summary

We are in general pleased that the IAA had adopted many of the comments that Aer Lingus made in response to IAA's previous consultation on RP4 methodology, and we are consequently broadly supportive of the approach the IAA has taken.

However, at the same time we believe the IAA's proposal is unnecessarily generous to AirNav, particularly in the area of cost, cost efficiency and proposed increases in unit prices.

We, like others, place the highest priority on safety and resilience of airspace and recognise and accept the decision to increase numbers of ATCOs and engineers. However, that said, AirNav should not be given the freedom to unrestrainedly recruit and deploy staff and pay inefficiently.

The IAA should subject AirNav's proposals for extra staff to scrutiny on salaries, grade profiles, job roles, proper management of leave and sickness absence etc.

We do not see any evidence to support the scale of the recruitment proposed.

Capacity/ cost trade-off

Capacity targets appear to be disproportionately stretching in the light of relatively good recent capacity performance, potentially leading to a detrimental impact on cost efficiency targets.

Although we clearly support, in principle, ambitions to improve capacity performance and the minimisation of delays, further improvements should remain in proportion with their effect on cost.

We would like to understand how these capacity projections would alter should the cost/capacity balance be readdressed so that cost efficiency becomes compliant with Union-wide targets.

Cost base and unit rate increase

We acknowledge that AirNav has been under-resourced with respect to ATCOs and that staff costs will increase to readdress the under-resourced starting point.

However, the cost base should, at worst, increase in line with volume and should in fact increase less due to volume efficiencies. Instead, we see a 10% increase in Opex vs an 8% increase in forecast volume.

Although we accept a cost base increase, we do not accept a level of unit rate increase which points to inefficiencies and poor cost control during previous regulatory periods.

Phasing of unit rates

We suggest that the unit rate profile be flattened to reduce the signficant detrimental year-on-year impact for users in Year 1 and instead graduated over the period.

Traffic

We support the use of STATFOR base-case with regard to traffic forecasts.

Capital investments

We support the reduction in AirNav proposals on capital costs from €40m to €35m based on asset life adjustments and reductions to new investment estimation.

However, based on previous regulatory periods, we are sceptical on delivery ambition and we encourage an assessment as to whether the blanket reduction on forecast capital investments goes far enough.

We clearly expect to see the benefits of Capex investment demonstrated through efficiencies and Opex reduction. We would encourage greater levels of governance and accountability within the Capex process to ensure both delivery and effectiveness of investment.

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Traffic forecasts

Traffic forecasts are vital to the overall economics of the price control and to establishing the suitable allowances for operating and capital expenditure necessary for delivering appropriate service quality outcomes.

We support the use of STATFOR base-case forecasts, noting that AirNav had themselves proposed the high-case which is not supportable as per the IAA draft decision.

The use of STATFOR base-case provides a consistent approach across Eurocontrol and the RP4 process and should not be deviated from. The base-case forecast should be updated where possible, noting the current forecast was taken from February and should be supplemented with airline forecasts and planned fleet deployment.

Capacity targets

More ambitious targets then implied by Union-wide targets are proposed for en-route capacity, with the 2024 target (0.03 mins/flight) being retained as the 2025-6 target and then reduced to 0.02 mins from 2027 onwards.

In the light of relatively good recent capacity performance, we perceive a risk that this increase in ambition on capacity may disproportionately affect cost and cost efficiency targets.

Both short-term and long-term DUC trends at +2.2% and +0.7% respectively deviate significantly from the Union-wide targets of -1.2% and -1.0%.

Although we clearly support ambitions to improve capacity performance and the minimisation of delays, further improvements should remain in proportion with their effect on cost.

We would like to understand how capacity targets and forecast would alter should the cost/capacity balance be readdressed so that cost efficiency becomes compliant with Union-wide targets.

Unit rate forecasts

We do not support the significant increase in real-term unit rates from €27 to €30 from Year 1 onwards.

We'd strongly like to understand what a Performance Plan would look like that was compliant with short and long-term DUC targets and did not deviate from them as have been proposed.

We took a sense from the consultation that cost efficiency was, to AirNav, somewhat of an afterthought and merely a resulting factor of all other KPIs. We would like to reinforce our statements made during the consultation that cost efficiency (ie price to the user), as one of the four KPIs, is of critical importance to IAG.

Further, within the industry we typically aim to at least offset inflation to remain competitive in a market environment. These increases go well beyond normal levels of inflation and are damaging to users and indeed the industry. We expect all of our key suppliers to adopt this mindset of committing to offsetting inflation and avoiding above-inflation increases.

Phasing of unit rate

We understand the phasing of the unit rates to increase (in real terms) from €27 to €30 in Year 1 of the regulatory period and then remain flat for the remainder of the period.

We suggest that, regardless of the final determined unit costs for the period, that the unit rate profile be flattened to reduce the signficant detrimental year-on-year impact for users in Year 1 and instead graduated over the period.

Operational expenditure

AirNav must only include efficient operating expenditure in the RP4 price control and they must be appropriately incentivised to become more efficient over the course of the regulatory period.

We note that total Opex is forecast to increase by around 10% in real terms over RP4 ie greater than the forecast increase in IFR movements at 8%.

Although we understand that the rationale behind this non-correlation is primarily due to a starting point of an under-resourced operation, we suggest that AirNav should find sufficient efficiencies in a growing operation and from its investment plan that over the regulatory period, Opex growth should be less than forecast volume growth, not more.

We also support the introduction of an efficiency challenge in relation to corporate services, In this respect we believe that the level of 5% is modest and would hope to see at least a 10% challenge in final proposals.

Staff costs

We acknowledge there is a requirement to resource staff and particularly ATCOs versus an under-resourced position in RP3. However, we urge that staff costs, as a critical and significant factor of overall cost base, be managed and scrutinised to ensure that wages are in line with market benchmarks and meet the level required to ensure the appropriate resource is met, without over-reward.

With the increase in ATCOs, we nevertheless expect to see efficiencies to be forecast and demonstrated in the use of these ATCOs with relation to airspace, and we expect overtime costs to become negligible.

We support the IAA position that headcount increases for engineering and corporate services staff are disproportionate to the required level of staffing.

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Capital investments

We support the reduction in AirNav proposals on capital costs from €40m to €35m based on adjustments to proposed asset lives and a blanket reduction to the estimate of new investments to be delivered within RP4.

However, given AirNav's significant under-delivery in previous regulatory periods we are sceptical whether AirNav will achieve their required level of delivery even after a blanket 20% reduction in forecast capitalisations vs their proposal. We would encourage IAA to revisit this assessment and further consider whether the 20% reduction goes far enough, based on previous performance.

Charges and financeability

We note that the real cost of capital has been proposed at 4.26% vs AirNav's proposal of 4.91% at which is a reduction of 65 bps.

We welcome the scrutiny that was applied to this subject and welcome the reduction from an over-stated WACC proposed by AirNav. However, we reserve the right to provide further comments on the WACC at a later date, and would welcome discussion with the IAA on this topic, and particularly the choice of a mid-point in the range of possible variable values.

We remain concerned that the WACC suggested by IAA still over-rewards AirNav in a post-Covid environment.

In particular, it would be useful to understand whether the asset beta was calculated using the correct forecast criteria, and whether the equity risk premium was appropriate and in line with market expectations.

Moreover, with the Traffic Risk Sharing scheme protecting AirNav from downside risk, we are concerned that we are essentially double-paying, via both penalisation on high inflation on the regulatory asset base and through covering AirNav's Covid losses.

MET ASD

We support the views and comments within Aer Lingus' response in their entirety on the poor quality of the MET ASD business plan, and the lack of meaningful customer engagement that went into its construction and support concerns expressed around lack of justification of pricing, opex, capex and resourcing proposals.

Next steps

IAG, as always, welcomes further engagement as the NSA/regulator refines its proposals prior to publishing its final Performance Plan.

Yours sincerely,

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Group Head Airport Affairs, IAG

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