Regional Airport Development 2016

The changing nature of air services to New Zealand's regional airports, and lessons from recent developments

Kevin Ward
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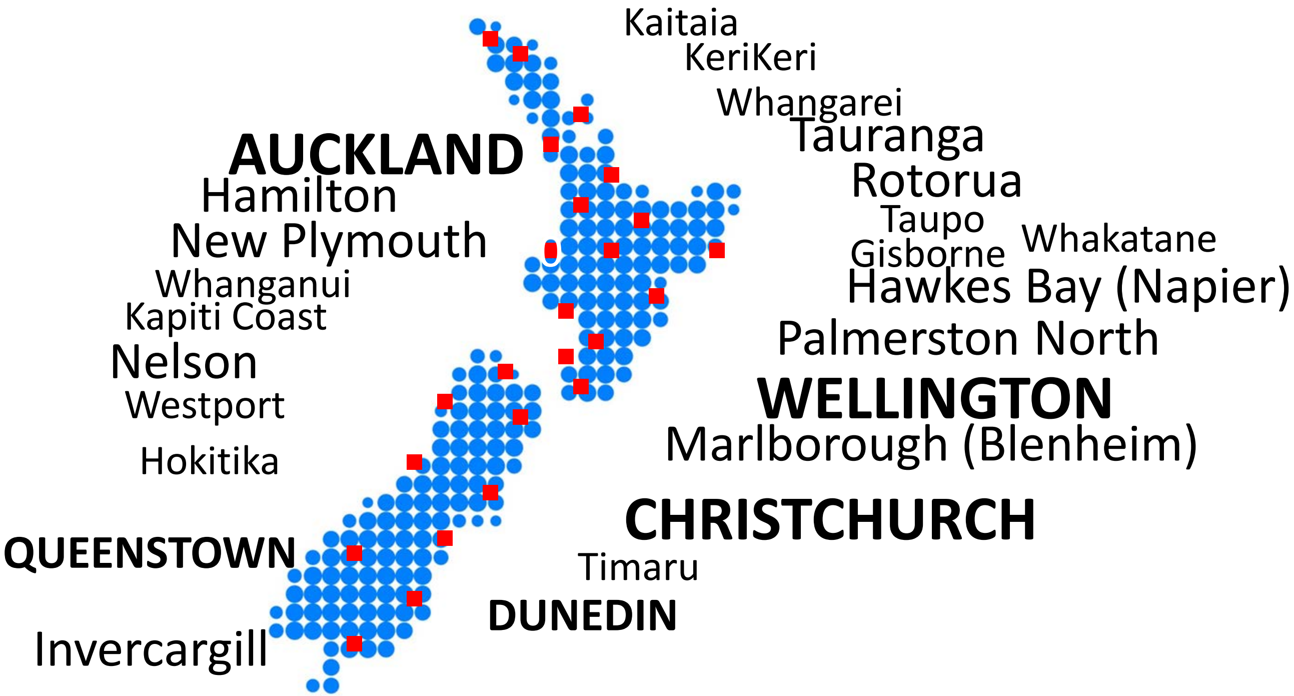
The airports



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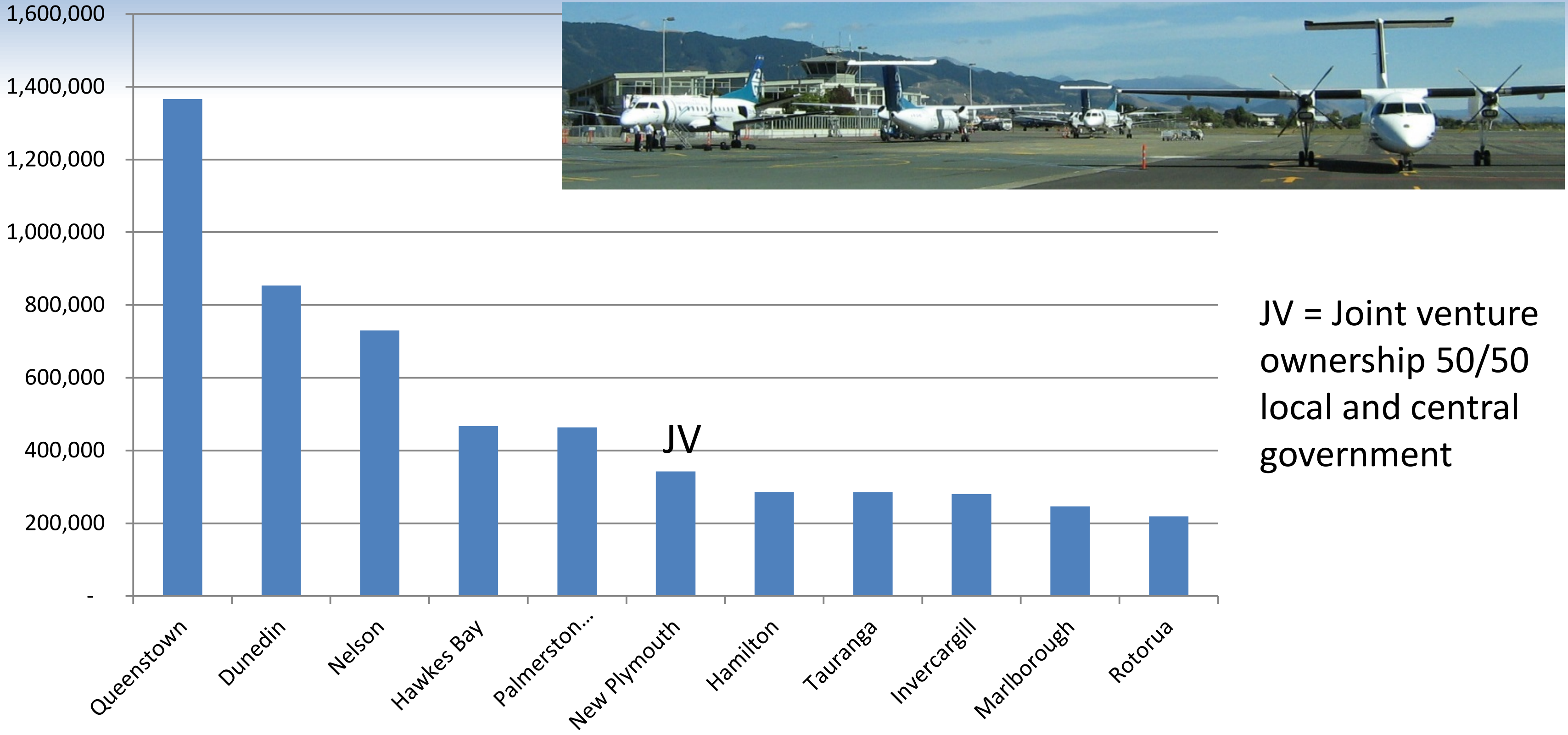
Airports with 200,000+ annual pax



JV = Joint venture ownership 50/50 local and central government

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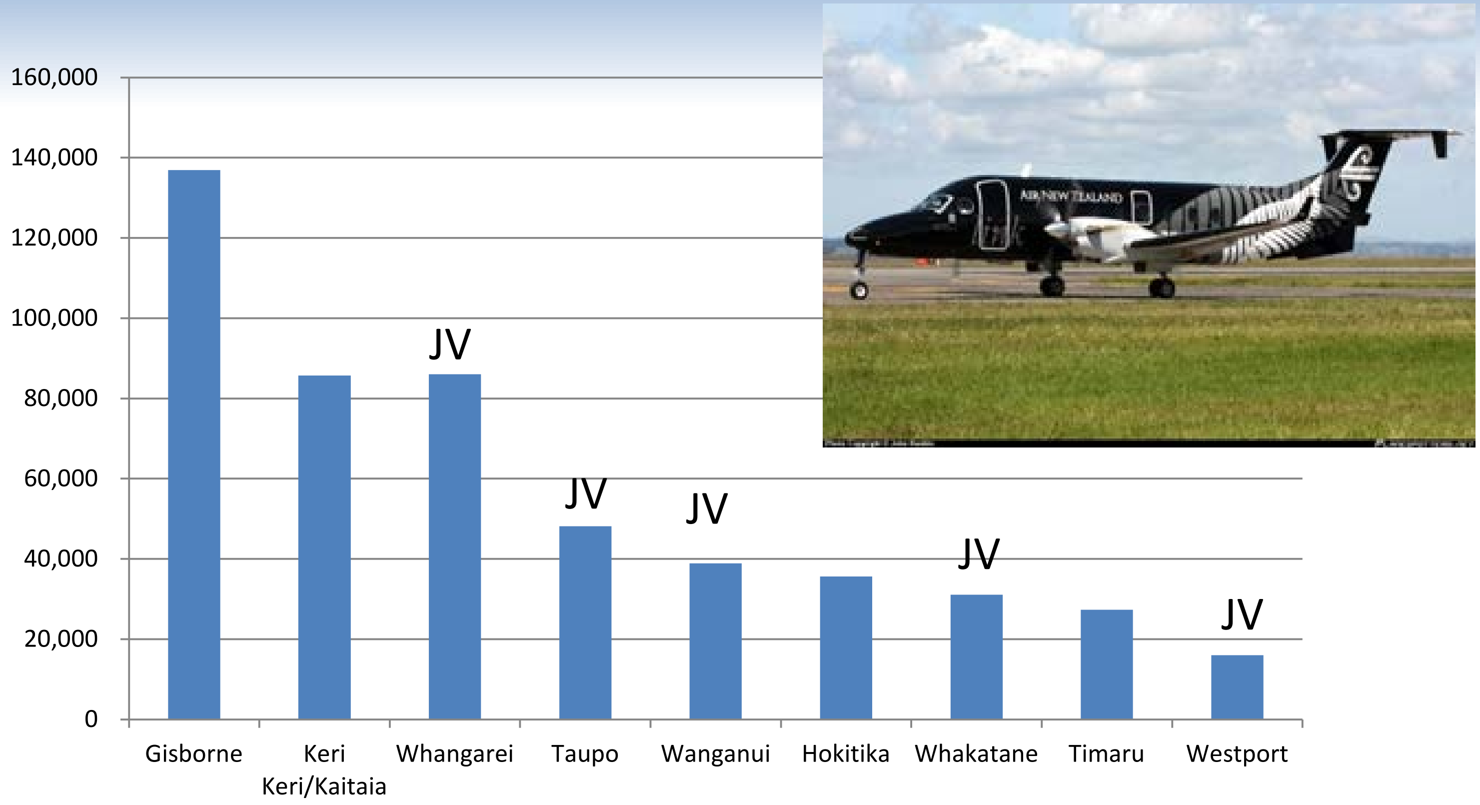
Commercial airports under 200,000 pax



Policy framework

- No provision for ‘social routes’
- No national vision or plan for the air network
- Airport Authorities Act:
  “Every airport operated or managed by an airport authority must be operated or managed as a commercial undertaking”
- Other government policies – e.g. centralisation of medical specialties, civil defence – assume air access available

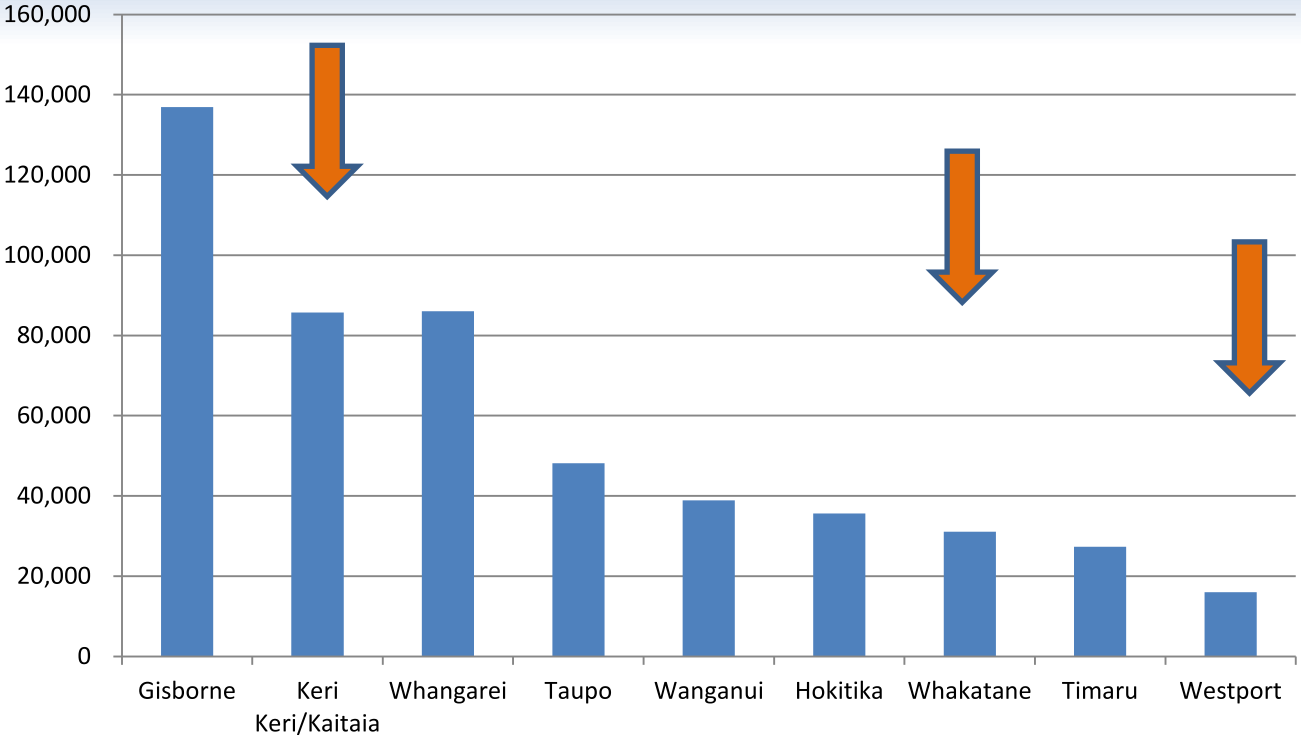
Air New Zealand – 2014 review

- Address poor economics of 19 seat Beech aircraft
- Beech fleet losing $1 million / month for the last 2 years
- Leverage the economies of scale from its 50 seat Bombardier Q300 and 68 seat ATR72 fleets
- Some routes strengthening demand – add capacity
- Fleet growth from 16 ATRs to 24 by August 2016
- Routes gaining larger aircraft - possible fare reductions
- Future sustainable model for regional routes

Outlook for smaller regional airports?

- Air New Zealand the only national network carrier, but…
- Airports aware of impending change, but no details
- Want to provide members with insight into change
- What will drive the shape of the network in next 5 years?
- Current changes are part of longer term trends
- The national air network being determined by one player - will that serve the overall national interest?
- Research commissioned, joined by Ministry of Transport

Withdrawn services, late 2014



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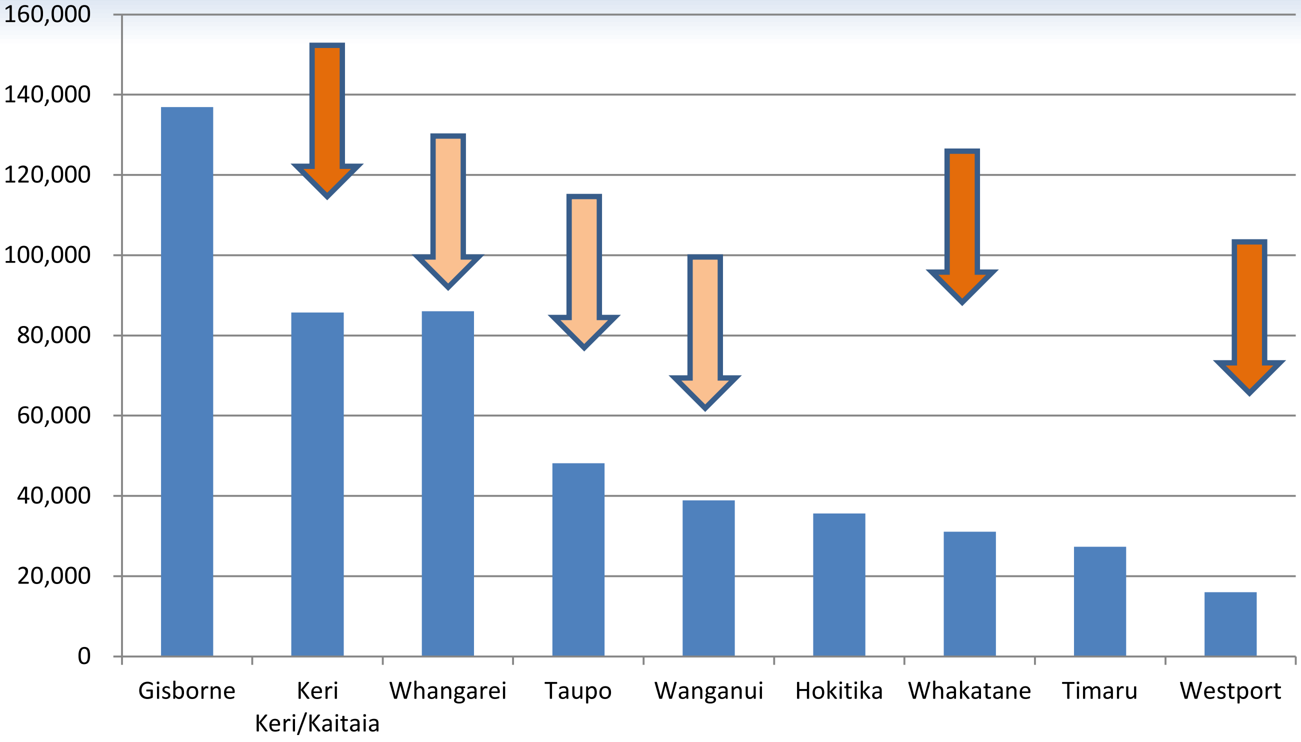
Withdrawn services… and routes cut



Unhappy communities

- Mayors lobby Prime Minister
- “A hammer blow to Kaitaia, Whakatane and Westport
- “No consideration for the social and economic effects
- “Regional air routes are lifelines
- “The regions are being abandoned
- “Travel for patients will take longer and cost more
- Local Government NZ walks out of meeting with Air NZ
- “Even harder to attract the businesses and skills needed

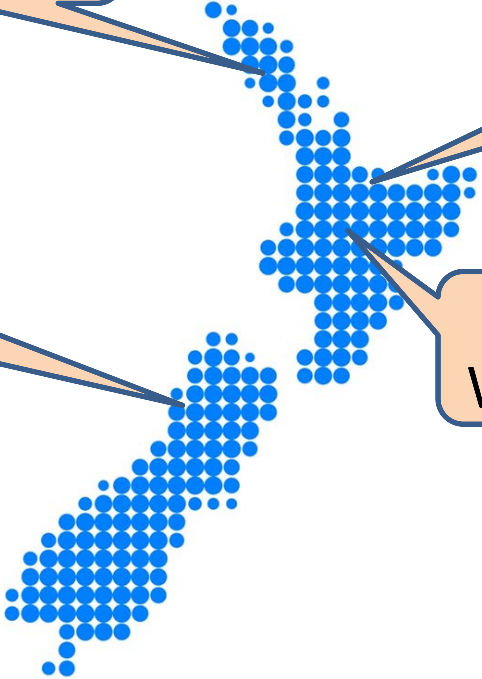
Local responses

- Driven by council owners of airports
- Urgent action – four months to find replacements
- Competitive selection processes
- Some data supplied by Air New Zealand
- Keen interest from established third-level operators

The solutions

Kaitaia to Auckland

Whakatane to Auckland



Westport to Wellington

Taupo to Wellington

Drivers of change

What will shape the air network?

- Factor analysis outcomes:
  - Airline ability to make a profit on various routes
  - The number of direct and indirect air connections passengers can make from an airport
  - The regional economy and employment base
  - Population

Drivers of change

Route profitability

- The potential number of passengers
- The cost of operating the aircraft
- The potential fares

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Drivers of change

Route profitability – operating costs

- Smaller planes are more expensive per seat
  - Under 10 seats av. $134/seat/hour
  - 10 to 20 seats av. $122/seat/hour
  - More than 20 seats $96/seat/hour

Drivers of change

Example – profitability of moving to a larger aircraft

- Assuming a route has 50,000 pax movements/year and the fare is $160
  - Using B1900s the profit potential is $78,000
  - Using Q300s, even if the pax volume is halved due to less frequent flights
    - Potential profit $1.1million

Drivers of change

Rule of thumb for NZ context:

- 33 seat aircraft needs minimum 35,000 pax

  Two inbound flights, two outbound / day
- 50 seat aircraft needs 45,000 to 55,000 pax

  … and the route needs to fit into wider network to maintain effective aircraft utilisation

Drivers of change

Airport connectivity

- International: 11% of passenger movements start or terminate at a regional airport
- Domestic
  - 45% of passenger movements between the three main hubs (AKL, WLG, CHC)
  - 52% of passenger movements were between a regional airport and a hub

Drivers of change

Regional economy and employment

- For regional airports
    - Not just size, but type of economy
        - Knowledge economy sectors demand air travel
        - High value economies
            - Rather than high employment
        - Tourism spending important
        - Primary sector - less strong links to demand

Drivers of change

Population

- Lower ranking relationship
  - Economic and connectivity factors outweigh simple population size

Five year outlook - Technology

Aircraft

- No new aircraft platform expected – no significant change to cost per seat
  - Airline cost sensitivity will continue
- Shift by major airlines to larger aircraft will reduce convenience and flights per day
- Lack of new designs for under 40 seat aircraft
- Aging fleet serving smaller centres

Five year outlook - Technology

Air Navigation

- The shift towards satellite based navigation and surveillance has potential system cost savings, but
  - Ground-based systems still required in NZ
  - New aircraft are fitted out, but re-equipping older aircraft is costly – sometimes prohibitive
    - If ground-based network removed at some point, smaller airlines with older fleets affected

Five year outlook - Connectivity

International

- Strong international tourism growth important to domestic air network – outlook positive
  - Oil prices low
  - International air links increasing
  - But exposed to international economic fluxes
- Potential to build tourism air links to regions

Five year outlook – Regional Economies

Differing characteristics

- Main urban centres strong, support air travel growth
- Many regions rely on primary industries – exposed to commodity price drops and reduced confidence
    - Demand growth may be suppressed
- Demand for point to point services between smaller regional economies likely to be limited

Five year outlook – Population

Uneven growth outlook

- More than half population growth to 2020 expected in Auckland; Waikato, Canterbury, Wellington strong
- Outside the main centres, flat trend
- Passenger demand therefore concentrated on trunk routes

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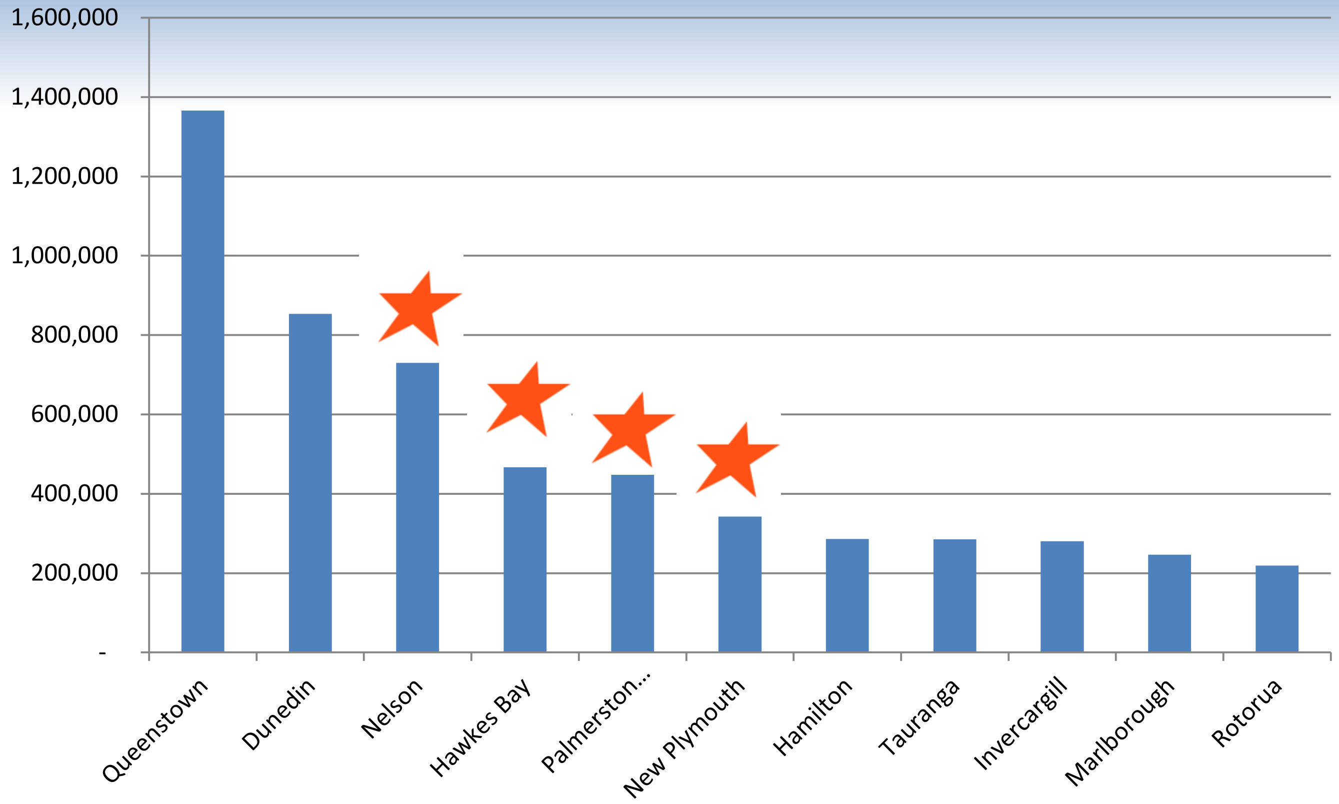
Five Year Outlook – Competition



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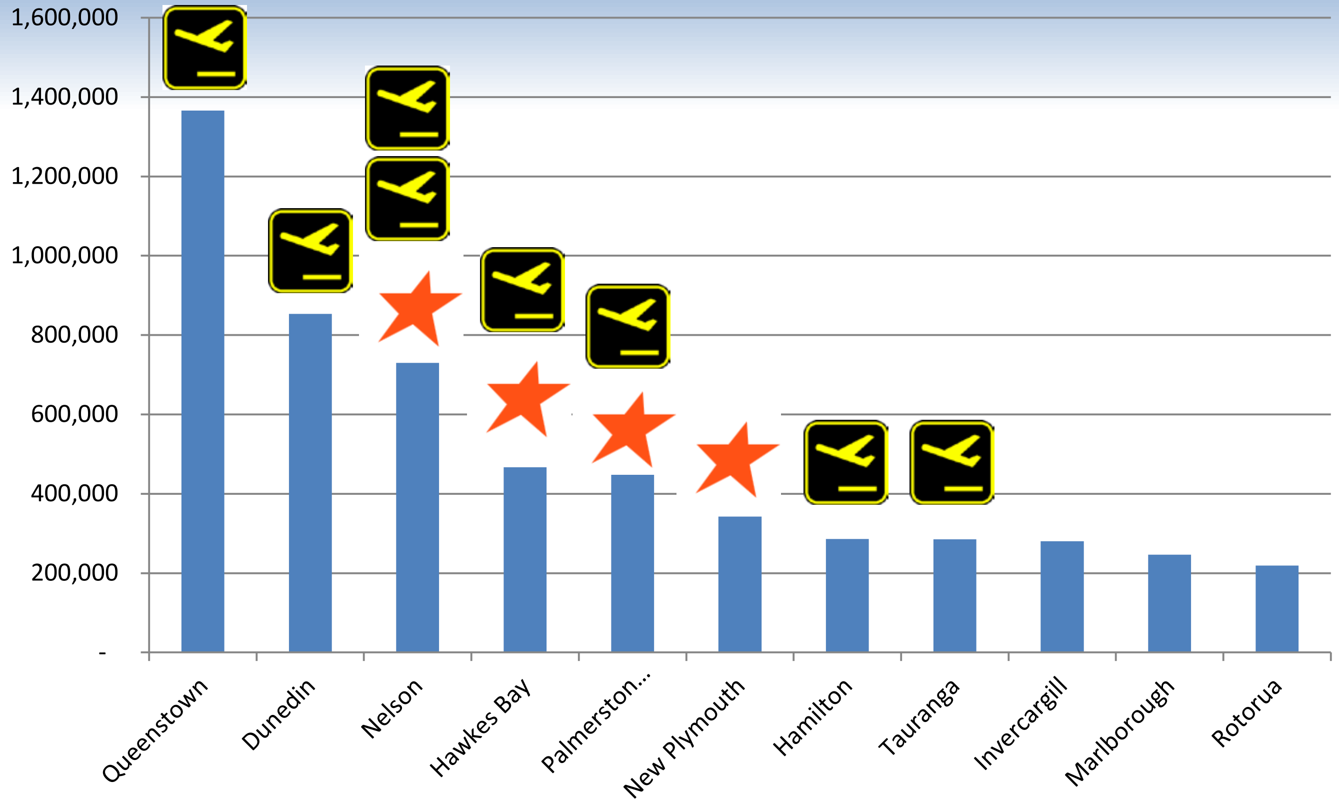
Jetstar – and others - in the regions



Lessons

National carrier	Tendered service
International visibility of destination	*Not part of international ticketing*
National & international connections	*Harder for passengers & bags to connect*
Loyalty perks and lounges	*No travel perks*
Reliability and resilience	*Susceptible to disruptions*
Two-pilots, twin engines	*Some single pilot, single engine and older*
Unwelcome surprises, unconsulted	**Negotiated and agreed**
Less desirable flight times & frequency	**Tailored flight times to suit region**
Unexplained cancellations	**Commitment to route**
High cost fares	**Similar fares**
Dominant relationship	**Service level agreements & contracts**

Policy issues

Future air network

- There is no national vision for the domestic air network in the public interest
- Driven by airline (and air navigation service provider) commercial decisions
- No national consideration of civil defence or health system needs
- No input of regional economic and social factors into route and service level decisions

Policy issues

Airport viability in smaller centres

- Financial pressure on smaller airports with less growth – several recording deficits / breaking even
  - Realistic to operate “as commercial undertaking”?
- Government objective to withdraw from JV airports
  - Access to capital funding lost
- Tendered services in some cases require underwriting – amidst other demands

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