



Why the Economic Case for a 3rd Runway at Heathrow *Still Won't Fly*

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By Ann Pettifor and Jeremy Smith

Ann Pettifor and Jeremy Smith record why – on economic as well as environmental grounds – they remain strongly against the Heathrow extension, and against building any new major airport in the London and south-east region. They therefore also disagree with those who oppose the Heathrow extension but favour a major new airport in say the Thames Estuary.

Introduction

Last Tuesday, 28th August, Ann was invited on to BBC Newsnight to debate the economic case for or against a third runway (R3) at Heathrow. At the last minute, Nick Clegg's unrequited call for a wealth tax became the focus for the programme, leaving little chance to debate the Heathrow issue.

On the panel with Ann was Emma Duncan, Deputy Editor of The Economist. She had that day announced her flightpath-to-Damascus conversion to the pro- R3 camp, joining Tim Yeo MP in what looks like an orchestrated campaign. The Coalition Government has insisted that it is not for turning, for the moment, but there are strong hints that at least the Conservative Party proposes to change its position for the next election. So the issue will not go away, we can be sure.

We thought it worthwhile recording why – on economic as well as environmental grounds - we remain strongly against the Heathrow extension, and against building any new major airport in the London and south-east region. We therefore also disagree with those who oppose the Heathrow extension but favour a major new airport in say the Thames Estuary.

Summary of key points

- We need a planet on which economic life takes place, which means acknowledging the role played by greenhouse gas emissions in warming the planet, changing the climate and harming the life-chances of future generations.
- In the UK aviation makes up a greater proportion of the country's contribution to climate change than in any other major economy.¹
- In contrast to other more sustainable sectors, the aviation industry receives enormous fiscal and financial advantages, including duty-free sales and tax-free fuel.
- Heathrow remains the EU's biggest hub airport already, by a significant margin.
- Heathrow is the third largest airport in the world in passenger numbers, with 50% more passengers than New York, whose economy is also heavily dependent on FIRE sectors.
- In terms of links to BRIC economies, Frankfurt, London and Paris are broadly similar, save for the German hub's more numerous links to Russia, reflecting different foreign policy approaches to Russia.
- The key question is not lack of capacity at Europe's airports but how that capacity is used.
- If a decade of major growth in passenger numbers were significant macro-economically, then France and the Netherlands (whose hubs have expanded rapidly) should be growing faster than the UK.
- Yet, GDP growth rates for France, the Netherlands and UK are broadly similar to the UK, and currently around or below zero.
- There are ways of addressing current destination patterns, without recourse to a major airport capacity increase.
- Government should ensure business needs take priority where required.
- 75% of London's aviation demand is for leisure travel, and only 25% for business.
- Leisure travel involves a net financial outflow as more Britons holiday abroad than vice versa.
- The operator's rationale for expansion is straightforward: BAA can only collect a rent fixed by the current capacity limit; it requires growth in capacity to enable it to increase income and reduce the overall Ferrovial/BAA £5bn debt mountain.
- Looking to the future, Europe's hubs will not grow indefinitely; they will need to co-exist and look at how best to complement each other.
- Far more sensible to get agreement on cooperation which uses the strengths and roles of each hub to mutual advantage.

¹ *From Plane Truths: do the economic arguments for aviation growth really fly?* A report by Victoria Johnson and Martin Cottingham et al from the new economics foundation (nef) and the World Development Movement. September, 2008.

What are the issues and arguments?

UK aviation makes up greater share of UK contribution to climate change than elsewhere

The world's climate is changing rapidly (despite the army of powerful self-interested deniers), and we are experiencing more and more extreme weather events. Ironically, on the day the aviation industry launched a sophisticated, co-ordinated lobbying campaign for a third runway, scientists [announced](#) a record Arctic ice melt. As the Guardian reported, "the 2012 figure has beaten the previous record (2007)... [and] reveals that global climate breakdown is proceeding more rapidly than most climate scientists expected."

At present, the aviation industry is responsible for a high proportion (in the UK 13%) of harmful greenhouse gas emissions, and is estimated to be responsible for almost 5% of man-made climate change. In the UK aviation makes up a greater proportion of the country's contribution to climate change than in any other major economy. ²

Yet it also receives enormous fiscal and financial advantages, including duty-free sales and tax-free fuel.

If we are to have economic life, we first need a planet on which such activity can take place, which means that carbon-fuelled aviation cannot continue an exponential 'flight path' into the future. Once this universal truth – that we have to control our use of finite resources and avoid greater damage to the atmosphere and to future generations - is recognized, a sensible policy for the future of aviation in the UK – and Europe – will be formulated. But that will not require or justify a third runway at Heathrow.

The arguments put forward for a third runway

Ms Duncan writes in the Times of 29th August that her "conversion" is the result of research she has done into London's economy. She sees the city's economy as healthy but fragile, with a real danger that London could "tip into another period of decline." She argues that London has flourished because it is so international. Its success springs from its appeal to foreigners who invest here and "create the jobs that keep London's economy working." For this to continue, we need good flight connections – direct flights to more and more countries, including 2nd tier cities.

² *From Plane Truths: do the economic arguments for aviation growth really fly?* A report by Victoria Johnson and Martin Cottingham et al from the new economics foundation (nef) and the World Development Movement. September, 2008.

Europe's competitors with "bigger airports than London's - Paris and Amsterdam" have increasing numbers of flights to such places, while Hong Kong, Dubai, Singapore want to take over London's position as centre of international finance and have far better flight connections. The problem, says Ms Duncan is not London's airport capacity, but its hub capacity – "airlines want to fly into airports that other airlines fly into". And it is far simpler and cheaper, says she, to go for R3 than to build Boris Island Airport.

The big employers' organisations back the airport expansions:

Jon Cridland, head of the CBI:

"Every day, the UK is losing out to its European rivals on new routes to growing markets".

Simon Walker of the Institute of Directors:

"The lamentable failure to increase airport capacity means that jobs are already being lost to our competitors".

So with all that support, how can you be against? Well, let's look first at some facts on airports, flights and passengers.

Facts on airports and passengers: Heathrow is still the EU's biggest hub airport.

1. Heathrow has long been Europe's biggest hub airport, and remains so today. In 2011 it carried 69 million passengers
2. This compares with a 2011 total for Paris CDG of 61 million, Frankfurt 56 million, and Schiphol 52 million
3. Thus, in 2011 Heathrow still had 8 million more passengers than CDG, 16 million more than Frankfurt, and 19 million more than Schiphol.
4. Heathrow and Gatwick combined carried 103 million passengers in 2011, 15 million more than nearest metropolitan combo of Paris CDG and Orly (88 million).
5. Heathrow and Gatwick passenger numbers have each grown by 6.2% or just under 0.6% per year on average between 2000 and 2011, whilst Paris CDG and Schiphol have increased the number of passengers per year by 27% and 25% respectively over the same period.

6. Frankfurt, the main hub of Germany, has grown in passenger numbers by 14% over the 11 years, or an average of 1.3% per year.
7. Heathrow serves fewer non-domestic destinations (183 in 90 countries) than the other major European hubs, but this is largely because London's European flights are served by several other airports (Gatwick, London City, Stansted..).

Before going further, it is also worth comparing London with New York, which is its main international comparator if not competitor.

8. In 2011, JFK airport came 17th in the list of passenger numbers, with a total of 48 million passengers.

So the argument by the R3 lobbyists has to be that London's and the UK's economy is at risk despite the fact that it remains third largest airport in the world in passenger numbers, and with some 50% more passengers than New York, whose economy is also heavily dependent on FIRE (finance, insurance, real estate) services and tourism.

If we analyse the main European hubs in terms of direct connections to the BRIC countries – Brazil, Russia, India, and China, we find (as far as we could ascertain) the following for 2011:

	Brazil	Russia	India	China	Total BRICs
Schiphol	6	6	5	10	27
Frankfurt	3	10	4	6	23
London HR	2	2	7	4	15
Paris CDG	2	3	4	5	14

Frankfurt, London and Paris are broadly similar, save for the German city's links to Russia, which appears to reflect a different foreign policy approach to that country. Only Schiphol has in recent years built a considerably broader range of BRIC destinations. London remains far ahead in terms of connectivity to North America.

Our information complements (but has been separately researched) that summarised by Airport Watch – an umbrella grouping of environmental and community organisations - in a 2011 briefing entitled “International Air Connectivity for Business”. They concluded:

1. London has better connections to the key business centres of the world than any other European city (All London's airports had 1,113 departure flights in the week

studied to key business destinations, compared with Paris’s 499, Frankfurt’s 443, and Amsterdam’s 282).

2. Heathrow has many more flights to the world’s key business centres than any of Europe’s airports, despite fewer transfer passengers than the other four major hub airports.
3. There is no evidence that an increase in transfer passengers is critical in maintaining Heathrow’s outstanding connections with the world’s business centres.
4. The key question is not lack of capacity at Europe’s airports but how that capacity is used

This last point is crucial, and the briefing continues:

“The vast majority of flights from all the European airports are intra-European, often covering relatively short distances. European governments need to decide whether to continue to permit most of the capacity at Europe’s airports to be taken up with short distance flights or whether to reduce the number of those flights – through fiscal measures, and slot allocation – in order to free up capacity for more intercontinental flights from key business destinations, particularly those in the fast-developing economies of Asia and South America. A carbon cap on aviation emissions will ensure that use of spare capacity does not result in an increase in overall emissions.”

No evidence that faster-growing hubs have a macroeconomic impact

But let us return to the question of whether having a major hub has a positive macroeconomic impact. Whilst Heathrow has grown only modestly in passenger numbers over the 11 years from 2000 to 2011, and Frankfurt not very much more, Schiphol and Paris CDG have both expanded by over 25% in passenger numbers. Can we notice any impact on GDP? The answer seems to us to be negative.

Increase/decrease in GDP from previous year:

	2002	2003	2004	2005	2006	2007	2008	2009	2010	2011
France	0.9	0.9	2.5	1.8	2.5	2.3	-0.1	-3.1	1.7	1.7
Germany	0.0	-0.4	1.2	0.7	3.7	3.3	1.1	-5.1	4.2	3.0
Netherlands	0.1	0.3	2.2	2.0	3.4	3.9	1.8	-3.7	1.6	1.0
UK	2.4	3.8	2.9	2.8	2.6	3.6	-1.0	-4.0	1.8	0.8

If a decade of major growth in passenger numbers was to have any significant impact, it should be in favour of France and the Netherlands. In fact the differences are marginal and the variables so many that it is impossible to assign cause and effect – other than to note Germany’s strength in 2010 and 2011 which no one has suggested results in any significant way from the steady growth of Frankfurt airport. And so far in 2012, the economies of France, the Netherlands and the UK are all around or below zero, while Germany’s early-year growth seems to be ending.

(A more interesting but more localised question is whether the existence of a fast-expanding hub has any material impact on the Gross Value Added of the nearby metropolitan city region. London and the Ile-de-France region around Paris in fact have similar economies and levels of unemployment, but PRIME has not at present found data to take this sub-national analysis forward).

We would not deny the importance of ensuring good air communications with emerging economies with whom commerce is increasing, or planned to increase. We therefore do not argue that the current pattern of destinations served by Heathrow is the ‘right’ one for the future. What we do assert is that – with over 100 million passengers using Heathrow and Gatwick each year – there are ways of addressing this without recourse to a major airport capacity increase. Government can and should regulate the airport industry in the national interest – the industry provides services of general (and genuine) economic interest, and should not be driven just by short-term market forces.

After all, the aviation industry receives enormous and unjustifiable fiscal and other economic advantages, which government can use to ensure that there are direct flights to ‘emerging’ destinations to enhance economic links as necessary. We note that some 75% of London’s demand is for leisure travel, and 25% for business, so there is room to ensure that business needs take priority where this is required – and leisure travel involves a net financial outflow as more Britons holiday abroad than vice versa.

The operator’s financial interest in expansion

We do not doubt that R3 at Heathrow would be to the great financial benefit of the operator, BAA, and its shareholders including the main one, Ferrovial, which is a Spanish infrastructure group. Earlier this year, Ferrovial divested itself of 5.88% of BAA, taking the company’s holding below 50%. According to the FT (23 February 2012):

“The divestment of 5.88% of BAA, to take the company’s overall holding to below 50%, allowed Ferrovial to deconsolidate the subsidiary’s total debt from its own balance sheet, meaning net debt tumbled from €19.7 billion to €5.1 billion over the year.”

We can assume that, from Ferrovial and BAA's perspective, building R3 would allow Heathrow to grow faster than is possible today. The status quo means that in effect, BAA can only collect a rent fixed by the current capacity limit; it requires a growth in capacity to enable its income to grow more rapidly, which would enable it to reduce the overall Ferrovial/BAA debt mountain.

Infrastructure investment alternatives

Of course, major investment and construction at Heathrow would create employment over a period of years on a significant scale. If the overall cost was say £10 billion, this represents around 0.7% of annual UK GDP. That said, it would not come on-stream for several years, and would be spread over several years, so it would not help in the present crisis. But it is not an all or nothing issue. The same (we would argue, a greater) level of productive investment is required for more sustainable transport infrastructure projects – we support larger rail investment, for example, both in new high-speed routes that obviate the need for domestic air travel and enhance access to the rest of the country, and in upgrades to existing routes and facilities.

To the extent that Heathrow is a drag on London's competitiveness, we argue that this relates far more to its poor facilities and problems around security and immigration services. Overall, the airport terminals seem more designed for the retailers than for passengers, and BAA have failed to upgrade the facilities adequately over many years (T5 notwithstanding). Despite (we read) a good recent performance during the Olympic Games, Heathrow has long suffered from excessive and frustrating queues – not just to enter the UK, but in particular for transfer passengers. So for London's reputation as an attractive business centre, a joint programme and commitment by government, BAA and airlines to improve the passenger experience would do far more at lower cost than a new R3.

The future for Europe's hubs – from competition to complementarity

Two final points on economic development of hubs. First, even in economic terms (let alone environmental) it is foolish to assume that air travel will continue to expand exponentially. There are limits, at least in the rate of increase of global air traffic, which will be reached within a relatively short period of a few decades at most – and maybe much sooner. Therefore, our second point, Europe's hubs will not grow indefinitely; they will need to co-exist and look at how best to complement each other.

At present, everything is seen through the prism of 'competition' between hubs, but when one looks at the destinations each serves, there is a general logic related to the economies, politics and historic links of each country. If the concept of Europe as a single market is to have any sense, then we need to do away with the idea that every

member state needs its own hub for all purposes – it is far more sensible to get agreement on cooperation, which uses the strengths and roles of each hub to mutual advantage.

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