



EUROPEAN COMMISSION

DG Competition

Case M.6447 - IAG/Bmi

Only the English text is available and authentic.

REGULATION (EC) No 139/2004
MERGER PROCEDURE

Decision on the implementation of remedies -
Art. 6(1)(b) in conjunction with 6(2)
Date: 04.11.2016



In the published version of this decision, some information has been omitted pursuant to Article 17(2) of Council Regulation (EC) No 139/2004 concerning non-disclosure of business secrets and other confidential information. The omissions are shown thus [...]. Where possible the information omitted has been replaced by ranges of figures or a general description.

Brussels, 4.11.2016
C(2016) 7220 final

PUBLIC VERSION

Dear Sir/Madam,

Subject: **Case No COMP/M.6447 – IAG/bmi**

Assessment of the viability of the Flybe Group Plc and evaluation of its formal bid pursuant to Clauses 1.4.4 and 1.4.9 of the Commitments attached to the Decision in the above-mentioned case following the Monitoring Trustee's opinion of 24 October 2016 – Summer 2017 IATA Season

1. FACTS AND PROCEDURE

- (1) By decision of 30 March 2012 ("the Decision") based on Article 6(1)(b) in connection with Article 6(2) of Council Regulation No 139/2004,¹ the Commission declared the concentration by which the undertaking International Consolidated Airlines Group ("IAG", United Kingdom) acquired sole control of the undertaking British Midlands Limited ("bmi", United Kingdom) compatible with the internal market subject to conditions and obligations (the "Commitments").
- (2) Pursuant to Clause 1.1.1 of the Commitments, IAG procures *inter alia* that slots are made available at London Heathrow airport ("Heathrow") in order to allow one or more Prospective Entrant(s)² to operate or increase their services on the following city pairs identified as routes of concern in the Decision:

¹ OJ L 24, 29.1.2004, p. 1 ("the Merger Regulation"). With effect from 1 December 2009, the Treaty on the Functioning of the European Union ("TFEU") has introduced certain changes, such as the replacement of "Community" by "Union" and "common market" by "internal market". The terminology of the TFEU will be used throughout this decision.

² Prospective Entrant is defined in the Commitments as "*Any Applicant that is not a member of the one-world Alliance or affiliated with any member of that alliance, able to offer a Competitive Air Service individually or collectively by codeshare and needing a Slot or Slots to be made available by IAG in accordance with the Commitments in order to operate a Competitive Air Service*". A Competitive Air Service is in turn defined in the Commitments as a non-stop scheduled passenger air transport service operated on one or more of the routes for which slots are requested.

- the "Identified UK City Pairs": London Heathrow–Aberdeen and London Heathrow–Edinburgh and;
 - the "Identified City Pairs": London Heathrow–Aberdeen, London Heathrow–Edinburgh, London Heathrow–Nice, London–Cairo, London Heathrow–Riyadh and London Heathrow–Moscow.
- (3) The number of slots to be made available enables prospective entrant(s) to operate up to a total of seven frequencies per day in total on the Identified UK City Pairs and in addition, up to six³ frequencies per day in total on the Identified City Pairs (including the Identified UK City Pairs).
- (4) On 18 August 2016, [CONFIDENTIAL] and the Flybe Group Plc ("Flybe" or the "Applicant") informed the Monitoring Trustee of proposed slot requests under the Commitments for the Summer 2017 IATA Season in accordance with Clause 1.4.1 of the Commitments.
- (5) On 1 September 2016, the Monitoring Trustee provided the Commission with its assessment that [CONFIDENTIAL] and Flybe fulfilled the eligibility criteria set out in Clause 1.4.4 of the Commitments.
- (6) On 5 October 2016, [CONFIDENTIAL] informed the Monitoring Trustee that it did no longer intend to submit a formal bid for slots for the Summer 17 IATA season. Therefore, [CONFIDENTIAL] application will not be discussed further in this decision.
- (7) On 6 October 2016, the Slot Request Submission Deadline for the Summer 2017 IATA Season, Flybe submitted to the Monitoring Trustee its formal bid for slots pursuant to Clause 1.4.7 of the Commitments.
- (8) Table 1 below provides a summary of the slot requested by Flybe which will be assessed in the remainder of this decision⁴:

Table 1: Summary of slot requests and compensation offers

Identified City Pair	Applicant	Number of requested weekly frequencies	Compensation offered Yes / No
London–Aberdeen	Flybe	18	[CONFIDENTIAL]
London–Edinburgh	Flybe	25	[CONFIDENTIAL]

³ The number of frequencies available for the Identified City Pairs increased from five to seven pursuant to Clause 1.1.3 of the Commitments, as the two slots provided by British Airways to Transaero were returned to IAG at the end of Summer 2015 IATA Season. Furthermore, one slot pair was awarded to Aeroflot on Moscow during the 2016/17 application process thus bringing the total number of frequencies available for all the routes to thirteen.

⁴ [CONFIDENTIAL].

- (9) For the purpose of this decision, the London Heathrow–Aberdeen, and London Heathrow–Edinburgh routes are also referred to as the "Relevant City Pair(s)".

2. REPORTS OF THE MONITORING TRUSTEE ON FLYBE'S SLOT APPLICATION FOR SUMMER 2017

2.1. Assessment pursuant to Clause 1.4.4 of the Commitments

- (10) In its report of 1 September 2016, the Monitoring Trustee assessed that Flybe fulfilled the eligibility criteria set out in Clause 1.4.4. of the Commitments.
- (11) The Monitoring Trustee notes that Flybe has small number of commercial arrangements with the IAG group. However, it considers that these arrangements do not breach the independence requirements of the Commitments as they do not affect the operations on none of the Relevant City Pairs.⁵
- (12) In addition, currently Flybe does not have any London Heathrow slots.
- (13) The Monitoring Trustee concluded that Flybe is independent of and unconnected with IAG and has exhausted its slot portfolio at Heathrow pursuant to Clause 1.4.4 of the Commitments.

2.2. Assessment pursuant to Clause 1.4.9(a) of the Commitments

- (14) In its report of 24 October 2016, the Monitoring Trustee assesses whether Flybe is a viable existing or potential competitor with the ability, resources and commitment to operate the proposed services in the long term as a viable and active competitive force, pursuant to Clause 1.4.9(a) of the Commitments. To this end, the Monitoring Trustee took into account a number of criteria, including:

(i) Financial health & regulatory approvals:

- The financial health and robustness of the airline – through evaluation of the financial statements, current and planned access to capital;
- The airline's regulatory approvals to operate in the territories relevant to the routes requested; and
- Any key risks to long term viability.

(ii) Operations and on-board offers:

⁵ In particular, Flybe has commercial agreements in place with British Airways, including code share arrangements on the London Gatwick to Newquay service and with British Airways' subsidiary Loganair on operations between the Scottish mainland (Glasgow, Aberdeen, and Edinburgh) and its islands. Flybe has an arm's length codeshare with Aer Lingus pursuant to which the latter places the Aer Lingus code on certain Flybe operated flights as part of a connecting journey on Aer Lingus' flights (i.e. not on point-to-point). Moreover, Flybe is part of the Avios Frequent Flyer Programme (which is part of IAG), an arms' length commercial relationship with IAG.

- Whether the slot times in the business plan are consistent with those offered by IAG and are operationally robust;
 - Whether the business plan demonstrates that sufficient aircraft and crew are available to the Applicant, or that it has a credible plan to obtain the aircraft and crew within the timescale indicated;
 - Whether the business plan demonstrates that sufficient ground handling, catering and engineering support are available, and appropriate check-in and lounge facilities; and
 - Whether the proposed on-board product is competitive with that offered by IAG, and whether it is consistent with achieving similar yields to those achieved by IAG.
- (15) Concerning Flybe's financial health, the Monitoring Trustee considers that *[CONFIDENTIAL]*.
- (16) *[CONFIDENTIAL]*.⁶
- (17) Furthermore, the Monitoring Trustee considers *[CONFIDENTIAL]*.
- (18) As a conclusion, *[CONFIDENTIAL]*.
- (19) According to the Monitoring Trustee, Flybe has all the necessary approvals to start operating on the Relevant City Pairs.⁷ Moreover, while Flybe presents some concerns due to its lack of existing operation at London Heathrow,⁸ this is not a fundamental concern and the Monitoring Trustee believes it is reasonable to assume that such operations will be organised in advance of commencement of the Summer 2017 season.
- (20) Concerning the competitiveness of Flybe's on-board service offering, the Monitoring Trustee concludes that Flybe's service will be more comparable in the future as British Airways ("BA", also referred to as "IAG" hereafter) confirmed that it will start to charge, from 11 January 2017, for food on short-haul flights.
- (21) In an overall assessment as regards Flybe's compliance with Clause 1.4.9(a), the Monitoring Trustee concludes that concerns in one or more areas could, in the event of adverse circumstances, be material to the effectiveness of the implementation of the Commitments.⁹

⁶ *[CONFIDENTIAL]*.

⁷ *[CONFIDENTIAL]*.

⁸ Flybe will be able to provide suitable ground handling and maintenance services from Heathrow, but there remains *[CONFIDENTIAL]*.

⁹ Versus the assessment made by the Monitoring Trustee in relation to Flybe's application for Winter 2016/2017 IATA Season, the composite score remains similar, but the mark for "on on-board service offer" increases.

2.3. The Monitoring Trustee's route-by-route assessment

- (22) In its report of 24 October 2016, the Monitoring Trustee assesses Flybe's slot application for Summer 2017 IATA season with regard to each Relevant City Pair.
- (23) Given that applications have only been received from Flybe for Summer 2017, for less than the full portfolio of 13 slots available under the Commitments,¹⁰ the Monitoring Trustee considers that it is necessary for the Commission to assess whether Flybe is a viable existing or potential competitor pursuant to Clause 1.4.9(a) of the Commitments, but it is not necessary for the Commission to rank Flybe's slot requests in order of preference pursuant to Clause 1.4.9(b).
- (24) Clause 1.4.10 provides the criteria to guide the Commission's assessment of formal bids under Clause 1.4.9. In this context, the Monitoring Trustee has conducted its analysis of the merits of the formal bid of Flybe in this application process.
- (25) The Monitoring Trustee assesses the level of effective competitive constraint that Flybe may be expected to impose on IAG, pursuant to Clause 1.4.10 of the Commitments. For this assessment, the Monitoring Trustee took into account:
- The promise of a year round service and the intended use of the slots in future years, as well as the total number of services/frequencies and total additional capacity proposed over the summer and winter seasons combined;
 - The pricing structure proposed, taking account of the expected service offering;
 - The network characteristics offered by Flybe, including feed onto Relevant Long-haul Destination/ Origin cities;
 - Passenger loadings, yield and revenue projections;
 - Cost projections;
 - Net profit projections; and
 - Sensitivity analysis.
- (26) In addition, the Monitoring Trustee assessed (i) Flybe's level of commitment to support its application; (ii) the consistency of Flybe's assumptions on airport charges with published charges, or agreed negotiated charges; and (iii) the differences between the assumptions used for the Summer 2017 application as compared to the Winter 2016/17 application.
- (27) In relation to those three additional criteria, the Monitoring Trustee concludes that (i) Flybe's commitment to enter the Relevant City Pairs is supported by the approval obtained at the Executive Committee level [*CONFIDENTIAL*]; (ii) [*CONFIDENTIAL*]; and finally, (iii) the main differences between Flybe's Summer 2017 and Winter 2016/17 applications relate in particular to [*CONFIDENTIAL*].

¹⁰ See footnote 3 above.

- (28) Finally, the Monitoring Trustee has reviewed the slot requests of Flybe and assessed that, based on the arrival times offered by IAG, no combination of awards of slots which could be awarded under the Commitments violate the condition of Clause 1.4.10 that no more than 5 arrival slots should be awarded before 12.00 local time, no more than 5 between 12.00 and 16.00 and no more than 5 after 16.00.

2.3.1. *London Heathrow–Edinburgh*

- (29) The Monitoring Trustee considers that Flybe demonstrates being a viable and effective competitor with regard to slot use, frequency, capacity, the pricing and service level of its proposed offering, as well as the cost projections of its business plan. With regard to network characteristics and long-haul feed, loadings, yield and revenue projections, profitability, as well as sensitivity robustness, the Monitoring Trustee considers that Flybe weakly demonstrates being a viable and effective competitor.

- (30) In its overall assessment, the Monitoring Trustee concludes that Flybe weakly demonstrates that it would be a viable and effective competitor on the London Heathrow–Edinburgh route.¹¹

- (31) *[CONFIDENTIAL]*

2.3.2. *London Heathrow–Aberdeen*

- (32) The Monitoring Trustee considers that Flybe demonstrates being a viable and effective competitor with regard to slot use, frequency, capacity, the pricing and service level of its proposed offering as well as the cost projections of its business plan. With regard to network characteristics and long-haul feed, Flybe weakly demonstrates being a viable and effective competitor. Finally, with regard to loadings, yield and revenue projections, profitability, as well as sensitivity robustness, the Monitoring Trustee considers that Flybe does not demonstrate being a viable and effective competitor.

- (33) In its overall assessment, the Monitoring Trustee concludes that Flybe does not demonstrate that it would be a viable and effective competitor on the London Heathrow–Aberdeen route.¹²

- (34) *[CONFIDENTIAL]*

¹¹ Versus the assessment made by the Monitoring Trustee for the previous season, the scores remain identical.

¹² Versus the assessment made by the Monitoring Trustee for the previous season, some of the scores and, as a result, the composite score, decrease.

3. COMMISSION'S ASSESSMENT

3.1. Conditions pertaining to slots and independence

- (35) According to the definition of Prospective Entrant in the Commitments¹³, an applicant must have the intention to operate new or additional frequencies on the Relevant City Pairs. Flybe fulfils this requirement with respect to its slot application.
- (36) Moreover, pursuant to Clause 1.4.4 of the Commitments, an applicant must be independent of and unconnected with the Parties. The Commission notes that Flybe is not an associated carrier belonging to the same group as IAG. It does not have common ownership with British Airways (or IAG or any of IAG's subsidiaries) and it does not belong to the oneworld alliance.
- (37) Flybe has no codeshare agreement with IAG on the Relevant City Pairs nor does it cooperate with IAG on the Relevant City Pairs in the provision of passenger air transport services. In line with the Trustee's assessment, the Commission thus considers that Flybe meets the independence criteria set out in the definition of the term "Prospective Entrant" as well as in Clause 1.4.4 of the Commitments.
- (38) Besides, the Commission considers that Flybe has exhausted its own slot portfolio at Heathrow according to Clauses 1.2.1 and 1.2.2 of the Commitments.

3.2. Assessment of the application pursuant to Clause 1.4.9(a)

- (39) Pursuant to Clause 1.4.9(a) of the Commitments, the Commission shall assess whether each applicant is a viable existing or potential competitor, with the ability, resources and commitment to operate services on the Relevant City Pairs in the long term as a viable and active competitive force.¹⁴
- (40) Flybe is one of Europe's major regional carriers and has a long track record of operating regional services throughout Europe and in particular in the UK.¹⁵ Flybe directly serves 176 routes, from 25 UK departure points and 37 European departure points. It has 10 UK bases, including Aberdeen and Edinburgh.
- (41) Flybe future plans appear in particular [*CONFIDENTIAL*].

¹³ See footnote 2 above.

¹⁴ Given that there is only one single applicant for the slots, and that there are enough slots available under the Commitments, there is no need to proceed to any ranking.

¹⁵ In Year 2015/16, Flybe had a 51.2% UK Regional Domestic Sector Share (+0.4 ppts increase vs Year 2014/15), Full Year Results –Year ended 31 March 2016, Analyst and Investor Presentation, 9 June 2016 (retrieved 9 June 2016). Year 2015/16 information and figures used in this Decision are set out in FLYbe's "Annual Results 2015-16" note, which does not constitute the company's statutory accounts for the years ended 31st March 2016 or 2015, but is derived from those accounts. Moreover, in January 2016, Flybe was named Best Short-Haul Airline at the 2016 Business Travel Awards; in January 2015, it was named top UK airline for punctuality in report issued by UK consumer watchdog Which?

- (42) In particular, in a broad, medium/long-term perspective, Flybe [*CONFIDENTIAL*].¹⁶ In this context, entry on the London Heathrow–Edinburgh and London Heathrow–Aberdeen routes could be seen as [*CONFIDENTIAL*]. According to Flybe, [*CONFIDENTIAL*].¹⁷ [*CONFIDENTIAL*].
- (43) [*CONFIDENTIAL*]¹⁸, [*CONFIDENTIAL*].
- (44) From Aberdeen Flybe serves the following markets for 2016/17: Birmingham (BHX), Belfast (BHD), Jersey (JER)¹⁹, London City (LCY), Manchester (MAN), Newquay (NQY)²⁰. From Edinburgh Flybe serves the following markets: for 2016/17 – Belfast (BHD), Birmingham (BHX), Paris Charles de Gaulle (CDG)²¹, Cardiff (CWL), Bergerac (EGC)²², East Midlands (EMA), Exeter (EXT), Jersey (JER)²³, London City (LCY), Liverpool (LPL), Manchester (MAN), Knock (NOC), Newquay (NQY)²⁴ and Southampton (SOU).
- (45) Flybe already competes on the direct markets between Aberdeen and Edinburgh to London against BA with operations from both cities into London City Airport.
- (46) Flybe holds a valid operating certificate.
- (47) The 2015/16 financial year (which ended 31st march 2016)²⁵ was the second full financial year of Flybe's three year transformation plan. Material progress appears to have been achieved. In its results for the year ended 31 March 2016, Flybe reported GBP 2.7 million profit before tax²⁶ (GBP 35.6 million loss before tax in

¹⁶ See Press clippings provided by Flybe on 24 October 2016. One slide mentions in particular "*Flybe – Potential new routes from an expanded Heathrow – connecting Britain's regions and nations to the world*". The Commission notes that Edinburgh and Aberdeen are not explicitly mentioned in these documents, but these press articles focus on longer-term projects of the company, which are linked to the evolution of expansion plans of London Heathrow airport (as slots become available on existing runways or a new runway if Heathrow is given permission). The possible entry of Flybe on the Edinburgh and Aberdeen routes would by contrast occur as of Summer 2017 season.

¹⁷ [*CONFIDENTIAL*](agreed minutes of a conference call with Flybe of 21 October 2016).

¹⁸ Flybe LHR Slots Business Plan Proforma Summer 17, page 4.

¹⁹ Summer only.

²⁰ Summer only.

²¹ Operated by Air France.

²² Summer only.

²³ Summer only.

²⁴ Summer only.

²⁵ Flybe's results for the 1st half of its 2016/17 year are expected to be announced on 9 November 2016, after the start of the IATA slot conference on 8 November 2016.

²⁶ Excluding revaluation of aircraft loans the group adjusted profit before tax reached GBP 5.5 million.

2014/2015). Group revenue increased by 8.7% to GBP 623.8 million (GBP 574.1 million in 2014/15). On the balance sheet Flybe reported net funds of GBP 62.2 million (i.e. funds offset by debt) and total cash of GBP 171.4 million.²⁷

- (48) Flybe considers in this context that "*Flybe resolved its final key legacy issue through re-deployment of the remaining E195 jets, returned to revenue growth and achieved profitability after five years of losses. Flybe is now in its final year of turnaround and focused on delivering profitable growth.*"²⁸
- (49) There was indeed a 8.2% increase in passenger revenue and 5.9% increase in passenger numbers; total revenue per seat was close to year 2014/15 (GBP 53.23 vs GBP 53.51 in 2014/15); seat capacity grew by 9.7%, and yields improved by 1.7% while the load factor was reduced by 2.6 ppts to 72.6%. Moreover, 52 new routes were launched, and 47 existing business routes had additional daily frequencies. Cost per seat was reduced by 2.2% (excluding fuel, at constant currency). New codeshares were signed, in particular with Emirates and Virgin Atlantic. Finally, Flybe was named Best Short Haul Airline at the 2016 Business Travel Awards (January 2016).²⁹
- (50) The airline industry environment will continue to be challenging in the coming months. Flybe faces a number of uncertainties, e.g. as the evolutions of oil prices and of the USD/GBP exchange rate.
- (51) Being already present in Edinburgh and Aberdeen airports, Flybe has access to the necessary ground facilities. Moreover, Flybe is expected to be able to make the requisite arrangements at London Heathrow.
- (52) Flybe intends to operate the London Heathrow–Edinburgh and Aberdeen routes with Q400 aircraft configured in a single cabin with 78 seats.³⁰
- (53) Flybe intends to operate the service throughout the year (both IATA summer and winter seasons) and to continue the service indefinitely on the two routes.
- (54) Flybe demonstrates its firm intention to entering the Relevant City Pairs in Summer Season 2017. The business cases for entering the Relevant City Pairs were

²⁷ Flybe Annual Results 2015-16, released 9 June 2016, <http://otp.investis.com/clients/uk/flybe/rns/regulatory-story.aspx?cid=59&newsid=738890> (retrieved 9 June 2016). It is also recalled that the cash increase recorded in 2013/14 was a result of a GBP 150.1 million net equity issue (12 March 2014) and the proceeds of a GBP 10.5 million sale of Gatwick slots.

²⁸ Flybe considers in particular that "*with the redeployment of the E195s, all of the Company's key legacy issues have been resolved with circa GBP 750m of liabilities eliminated.*"

²⁹ Flybe Annual Results 2015-16, released 9 June 2016, <http://otp.investis.com/clients/uk/flybe/rns/regulatory-story.aspx?cid=59&newsid=738890> (retrieved 9 June 2016).

³⁰ Flybe has a fleet of over 50 of these aircraft. Flybe has agreements in place to take an additional 10 aircraft deliveries between April 2016 and October 17, made up of 1 ATR-72 and 9 Bombardier Q400 aircraft.

presented to, and endorsed by, Flybe's Executive Committee. *[CONFIDENTIAL]*.³¹ In that respect, Flybe noted the importance of being awarded the slots on both the London Heathrow–Edinburgh and the London Heathrow –Aberdeen routes, in order to be able to generate sufficient economies of scale as well as to offer a more attractive portfolio of routes to connecting passengers at London Heathrow.³²

- (55) Flybe also confirmed that what prevented it from operating the slots during the Winter 2016/17 IATA Season (i.e. the impossibility to postpone the beginning of operations at Heathrow to 1st January 2017, when airport charges would be reduced by GPB 10) would not materialise this time. Flybe also confirmed that no other external or internal factors could influence its ability to start operations on the Relevant City Pairs for the Summer 2017 IATA Season.³³

3.2.1.1. London Heathrow–Edinburgh

Frequency and capacity

- (56) Flybe intends to operate an average of 4 daily frequencies on the London Heathrow–Edinburgh route³⁴ to be compared with the 12 frequencies advertised to be offered by IAG.³⁵ The frequencies are spread across the day. In terms of annual capacity, Flybe would offer 2 604 flights and 203 112 total seats on this route.
- (57) While Flybe would offer a lower frequency than that operated by BA, the Commission is of the view that this is a reasonable level of service in the context of the slots intended for UK domestic use available under the Commitments.
- (58) Overall, in terms of capacity and frequency, which are two important parameters of competition, the Commission concludes that Flybe will have the ability to act as a material competitive force on the London Heathrow–Edinburgh route.

Pricing and services

- (59) Flybe will offer a single cabin product available through all channels with an offering towards multiple services. Furthermore, Flybe will propose a hierarchy of fares, as currently used on its short-haul routes, *[CONFIDENTIAL]*. Fares will

³¹ Agreed minutes of a conference call with Flybe of 21 October 2016. *[CONFIDENTIAL]*.

³² Agreed minutes of a conference call with Flybe of 21 October 2016.

³³ Agreed minutes of a conference call with Flybe of 21 October 2016. Besides, on 26 October 2016, Flybe announced its Chief Executive would step down. *[CONFIDENTIAL]*.

³⁴ The minimum number of frequencies is four per day between days one to five, two on day six and three on day seven. *[CONFIDENTIAL]*.

³⁵ IAG would use a mix of Airbus 319, Airbus A320, Airbus A321, and Boeing 767 aircraft.

usually be available as non-refundable, non-changeable one-way fares (with return fares at twice the one-way fare).³⁶ [CONFIDENTIAL].³⁷

- (60) Besides, Flybe's service offerings will be comparable to those of British Airways, which will remove its complementary refreshment offer from 11 January 2017.
- (61) Flybe will have [CONFIDENTIAL] seat density [CONFIDENTIAL].
- (62) Overall, the Commission therefore concludes that in terms of service offerings and pricing, which are important factors taken into consideration by travellers, Flybe will have the ability to act as a material competitive force on the London Heathrow–Edinburgh route.

Network and long-haul feed

- (63) Flybe will rely on partners to provide long-haul feed, in particular [CONFIDENTIAL].³⁸ Flybe may however be at some disadvantages in comparison to BA's flights, e.g. with a lower frequency, [CONFIDENTIAL]
- (64) With four rotations per day, Flybe passengers will be able to connect to a range of Flybe partners' flights at Heathrow Airport.
- (65) Overall, the Commission concludes that, in terms of network characteristics and long-haul feed, Flybe will have the ability to act as a material competitive force on the London Heathrow–Edinburgh route.

Load factor, yield, and revenue projections

- (66) In terms of projected performance on the route, Flybe expects an average load factor [CONFIDENTIAL] during the first 3 years. During the same period, Flybe projects the average yield by passengers [CONFIDENTIAL].
- (67) The Monitoring Trustee considers that Flybe's assumptions [CONFIDENTIAL] on the London Heathrow–Edinburgh route.
- (68) However, the Commission considers in particular the following.
- (69) As concerns the load factor, Flybe achieved a [CONFIDENTIAL]% capacity utilisation on the London City–Edinburgh route from March 2015 to February 2016. Flybe's overall UK domestic network load factor was [CONFIDENTIAL]

³⁶ Furthermore, change of date, time, route, or even the name of the passenger is possible at a fee.

³⁷ [CONFIDENTIAL].

³⁸ In March 2016 Virgin Atlantic and Flybe launched a new codeshare that involved 18 short haul routes operated by Flybe, both domestic UK and international.

TIAL]%. [CONFIDENTIAL].³⁹ The Commission also considers that it is likely that a route flying into London Heathrow would [CONFIDENTIAL].⁴⁰

- (70) Taken against these figures, Flybe's projections for London Heathrow–Edinburgh seem to be [CONFIDENTIAL].
- (71) Regarding yield, [CONFIDENTIAL], as Flybe's forecast for the first three years would [CONFIDENTIAL].⁴¹
- (72) For connecting passengers, it seems that Flybe's forecast [CONFIDENTIAL].⁴²
- (73) To sum up, the Commission considers that, in terms of load factor, yield, and revenue projections, Flybe's application [CONFIDENTIAL].
- (74) In light of the above, the Commission therefore concludes that load factors, yield and revenue projections sufficiently demonstrate that Flybe will have the ability to act as a material competitive force on the London Heathrow–Edinburgh route.

Cost projection

- (75) Regarding costs, while the Monitoring Trustee [CONFIDENTIAL], the Commission considers that Flybe, as one of the major European regional carriers with a long-standing track record of providing air transport services, possesses the necessary business expertise to provide strong reliable estimates of its projected costs.
- (76) The Commission concurs with the Monitoring Trustee that the assumed [CONFIDENTIAL].
- (77) Overall, the Commission therefore concludes that, in terms of costs projections, Flybe's application indicates that Flybe will have the ability to act as a material competitive force on the London Heathrow–Edinburgh route.

Profitability and sensitivity analysis

- (78) Flybe projects [CONFIDENTIAL].⁴³

³⁹ Flybe LHR Slots Business Plan Proforma Summer 17, Appendix 5.

⁴⁰ On e.g. the comparative London City–Edinburgh route, there would also likely be a lower number of connecting passengers. Risk of lower load factor is also assessed as part of the sensitivity analysis.

⁴¹ Paragraph 105 of the Monitoring Trustee's report. This remains however subject to BA's price strategy, which could have a material impact on the average yield achieved on the route. [CONFIDENTIAL] (Flybe - Network development forum – 11 October 2016, slide 9).

⁴² Paragraph 106 of the Monitoring Trustee's report. [CONFIDENTIAL].

⁴³ [CONFIDENTIAL]. Paragraphs 118-119 of the Monitoring Trustee's report. [CONFIDENTIAL] for the three years: [CONFIDENTIAL], Flybe - Network development forum – 11 October 2016, slide 8.

- (79) In particular in case of adverse developments (identified for instance in the sensitivity analyses conducted by the Monitoring Trustee)⁴⁴, Flybe's financial situation, for instance with net funds of GBP 62.2 million and total cash of GBP 171.4 million according to its latest annual results 2015-16, is such that Flybe [CONFIDENTIAL].⁴⁵
- (80) A time perspective somewhat longer than three years would also provide further useful insights as to the new entrant would be a viable competitor with the ability, resources and commitment to operate services in the long term as a viable and active competitive force. [CONFIDENTIAL]⁴⁶, [CONFIDENTIAL].
- (81) In light of the above and all the other available evidence, overall, the Commission therefore considers that Flybe will have the ability to act as a material competitive force on the London Heathrow–Edinburgh route.

Conclusion

- (82) Based on the above and all the other available evidence, and considering in particular (i) Flybe's ability to compete with BA in terms of frequency, capacity, service offerings and pricing, which are all important parameters of competition, (ii) its cost and revenue projections over the initial three years of operation and beyond, and (iii) Flybe's commitment to develop [CONFIDENTIAL], the Commission concludes on balance that Flybe is a viable potential competitor of IAG on the London Heathrow–Edinburgh route, with the ability, resources and commitment to operate services in the long term as a viable and active competitive force.
- (83) In any event, to mitigate any risk that Flybe would not operate on the route as stated in its application, and in particular in case of risk of Misuse⁴⁷, the Commission proposes, as a precautionary measure and without prejudice to its assessment on the viability of Flybe's operations, that the Monitoring Trustee closely and regularly monitors Flybe's performance activities on the London Heathrow–Edinburgh route under the relevant provisions of the Commitments, in particular Clause 6.2.1(f), which allows ad hoc reports to be produced by the Trustee to the Commission, at the Commission's request, on matters falling within the scope of the Commitments, as well as Clause 1.3.6 of the Commitments, which more spe-

⁴⁴ The Monitoring Trustee applied the following sensitivity tests, by making adjustments to the relevant lines in the business plans submitted by Flybe: (i) increase in USD/GBP exchange rate by 20%; (ii) oil price increases to either USD 70 or USD 100 per barrel; (iii) passenger load factor reduces by 5 points, 10 points and 15 points; (iv) average revenue yield reduces by 5%; and (v) a combined sensitivity test where the load factor is assumed to decrease by -10 points, the yield is assumed to decrease by -5% and the USD/GBP exchange rate to appreciate by 20%.

⁴⁵ [CONFIDENTIAL]

⁴⁶ Flybe projected operations for up to [CONFIDENTIAL] (Paragraph 105 of the Monitoring Trustee's report).

⁴⁷ Misuse is defined in Clause 1.3.5 of the Commitments.

cifically relate to the reporting procedure in case of envisaged risk of Misuse.⁴⁸ The Monitoring Trustee may in particular monitor factors such as slot utilisation, load factors, route performance, and adherence to banking covenants.

3.2.1.2. *London Heathrow–Aberdeen*

- (84) Considering the opinion of the Monitoring Trustee, the Commission has conducted an even deeper assessment of Flybe's application on the London Heathrow–Aberdeen route than that on London Heathrow–Edinburgh route.

Frequency and capacity

- (85) Flybe intends to operate around three daily frequencies on the London Heathrow–Aberdeen⁴⁹ route to be compared with the 8 frequencies planned to be offered by BA⁵⁰. The frequencies are spread across the day. In terms of annual capacity, Flybe would offer 1 874 flights and 146 172 total seats on this route.
- (86) While Flybe would offer a lower frequency than that operated by BA, the Commission is of the view that this is a reasonable level of service in the context of the slots intended for UK domestic use available under the Commitments.
- (87) Overall, in terms of capacity and frequency, which are two important parameters of competition, the Commission concludes that Flybe will have the ability to act as a material competitive force on the London Heathrow–Aberdeen route.

Pricing and services

- (88) Flybe will offer a single cabin product available through all channels with an offering towards multiple services. Furthermore, Flybe will propose a hierarchy of fares, as currently used on its short-haul routes, [CONFIDENTIAL]. Fares will usually be available as non-refundable, non-changeable one-way fares (with return fares at twice the one-way fare).⁵¹ [CONFIDENTIAL].⁵²
- (89) Besides, Flybe's service offerings will be comparable to those of British Airways, which will remove its complementary refreshment offer from 11 January 2017.
- (90) Flybe will have [CONFIDENTIAL] seat density [CONFIDENTIAL].

⁴⁸ When Virgin's subsidiary Little Red, which had been awarded slots to operate on the London Heathrow–Aberdeen and London Heathrow–Edinburgh routes, decided to cease operations on those routes in 2015, the appropriate application of the Commitments and the slot release agreement between Virgin and IAG lead to an orderly hand-back of slots.

⁴⁹ The minimum number of frequencies is three per day between days one to five, one on day six and two on day seven. [CONFIDENTIAL].

⁵⁰ IAG would use a mix of Airbus 319, Airbus A320, and Airbus A321 aircraft.

⁵¹ Furthermore, change of date, time, route, or even the name of the passenger is possible at a fee.

⁵² [CONFIDENTIAL].

- (91) Overall, the Commission therefore concludes that in terms of service offerings and pricing, which are important factors taken into consideration by travellers, Flybe will have the ability to act as a material competitive force on the London Heathrow–Aberdeen route.

Network and long-haul feed

- (92) Flybe will rely on partners to provide long-haul feed, [CONFIDENTIAL].⁵³ Flybe may however be at some disadvantages in comparison to BA's flights, for example it will offer a lower frequency, [CONFIDENTIAL]
- (93) With three rotations per day, Flybe passengers will be able to connect to a range of Flybe partners' flights at Heathrow Airport.
- (94) Overall, the Commission concludes that, in terms of network characteristics and long-haul feed, Flybe will have the ability to act as a material competitive force on the London Heathrow–Aberdeen route.

Load factor, yield, and revenue projections

- (95) In terms of projected performance on the route, during the first three years of operations, Flybe expects an average load factor [CONFIDENTIAL] and projects the average yield by passengers [CONFIDENTIAL].
- (96) According to the Monitoring Trustee the actual load factors on the London Heathrow–Aberdeen route would likely [CONFIDENTIAL].
- (97) In relation to these elements, the Commission considers in particular the following.
- (98) As concerns load factor, Flybe achieved a [CONFIDENTIAL] capacity utilisation on the London City–Aberdeen route from March 2015 to February 2016, in a mature market where it is the only operator, and Flybe's overall UK domestic network load factor was [CONFIDENTIAL]%.⁵⁴ Besides, BA, which is well established on the London–Aberdeen route, attained a load factor of [CONFIDENTIAL] over the same period [CONFIDENTIAL].
- (99) The Commission notes however that [CONFIDENTIAL].⁵⁵ The Commission also considers that it is likely that a route flying into London Heathrow would [CONFIDENTIAL].⁵⁶

⁵³ In March 2016 Virgin Atlantic and Flybe launched a new codeshare that involved 18 short haul routes operated by Flybe, both domestic UK and international.

⁵⁴ [CONFIDENTIAL](Flybe - Network development forum – 11 October 2016, slide 9).

⁵⁵ Flybe LHR Slots Business Plan Proforma Summer 17, Appendix 5.

⁵⁶ On e.g. the comparative London City–Aberdeen route, there would also likely be a lower number of connecting passengers. Risk of lower load factor is also assessed as part of the sensitivity analysis.

- (100) Besides, with the withdrawal of Little Red⁵⁷ from the London Heathrow-Aberdeen route, the capacity on the route decreased materially since 2015.⁵⁸ Such decrease in capacity appears to have had a two-fold effect, [CONFIDENTIAL].
- (101) While Flybe's entry would add some capacity on the London Heathrow-Aberdeen route (thereby increasing consumer choices), it would not reach the same capacity that Little Red deployed. This would give Flybe better possibility in this regard to operate the route in a more sustainable manner.
- (102) Flybe's calculations on load factors are based *inter alia* [CONFIDENTIAL].⁵⁹ [CONFIDENTIAL].⁶⁰
- (103) In this context, Flybe estimates that [CONFIDENTIAL]. The Commission notes that based on these [CONFIDENTIAL]⁶¹. Flybe's business plan shows that [CONFIDENTIAL].⁶²
- (104) The evidence provided by Flybe shows that Flybe's Executive Committee approved the entry on the route [CONFIDENTIAL].⁶³
- (105) As concerns yields, Flybe bases its assumptions [CONFIDENTIAL].⁶⁴ [CONFIDENTIAL]. For connecting passengers, [CONFIDENTIAL].⁶⁵
- (106) However, [CONFIDENTIAL].
- (107) Moreover Flybe's forecast for the first three years would [CONFIDENTIAL].⁶⁶
- (108) The Commission considers that [CONFIDENTIAL].⁶⁷

⁵⁷ Little Red operated Airbus A320s aircraft wet leased from Aer Lingus. The airline ceased operations in 2015.

⁵⁸ [CONFIDENTIAL], Flybe - Network development forum – 11 October 2016, slide 5.

⁵⁹ [CONFIDENTIAL].

⁶⁰ Flybe - Network development forum – 11 October 2016, slide 6

⁶¹ [CONFIDENTIAL]. A similar reasoning would apply to the London Heathrow-Edinburgh route.

⁶² Flybe - Network development forum – 11 October 2016, slide 4.

⁶³ Flybe - Network development forum – 11 October 2016, slide 9. [CONFIDENTIAL].

⁶⁴ Flybe - Network development forum – 11 October 2016, slide 6.

⁶⁵ Paragraph 164 of the Monitoring Trustee's report.

⁶⁶ Paragraph 163 of the Monitoring Trustee's report. This remains however subject to BA's price strategy, which could have a material impact on the average yield achieved on the route. [CONFIDENTIAL] (Flybe - Network development forum – 11 October 2016, slide 9).

⁶⁷ [CONFIDENTIAL]. Flybe - Network development forum – 11 October 2016, slide 6.

- (109) Finally, Flybe, which has a long track record of operating regional services in particular in the UK, is already present in Aberdeen, and in London (London City Airport). While presenting risks, starting operation on the London Heathrow–Aberdeen route would build e.g. on existing reputation and customer bases, so that the commercial risk attached to the new route would remain acceptable.⁶⁸
- (110) To sum up, the Commission considers that, in terms of load factor, yield, and revenue projections, Flybe's application may appear [CONFIDENTIAL]. However, load factors and yield projections are based on [CONFIDENTIAL]. In addition, the Commission considers that some weight in the assessment of Flybe's assumptions should be given to the increased opportunities [CONFIDENTIAL] as well as to Flybe's proven track record to operate in the Scottish and the London markets.
- (111) In light of the above and all the other available evidence, the Commission therefore concludes that load factors, yield and revenue projections sufficiently demonstrate that Flybe will have the ability to act as a material competitive force on the London Heathrow–Aberdeen route.

Cost projection

- (112) Regarding costs, while the Monitoring Trustee [CONFIDENTIAL], the Commission considers that Flybe, as one of the major European regional carriers with a long-standing track record of providing air transport services, possesses the necessary business expertise to provide strong reliable estimates of its projected costs.
- (113) The Commission concurs with the Monitoring Trustee, that the assumed [CONFIDENTIAL].
- (114) Overall, the Commission therefore concludes that, in terms of costs projections, Flybe's application indicates that Flybe will have the ability to act as a material competitive force on the London Heathrow–Aberdeen route.

Profitability and sensitivity analysis

- (115) Flybe projects [CONFIDENTIAL].⁶⁹
- (116) The Commission is of the view that it is normal in the air transport sector that, over the first years of operating new routes, profitability is lower than when operations have been in place for a number of years. This would be even more the case when a carrier starts operating from and to an airport where it has not been present. A time perspective somewhat longer than three years would then provide further useful insights as to the new entrant would be a viable competitor with the

⁶⁸ A similar assessment can be made for the London Heathrow–Edinburgh route.

⁶⁹ [CONFIDENTIAL]. Paragraphs 176-177 of the Monitoring Trustee's report. [CONFIDENTIAL] for the three years [CONFIDENTIAL]; Flybe - Network development forum – 11 October 2016, slide 8.

ability, resources and commitment to operate services in the long term as a viable and active competitive force. *[CONFIDENTIAL]*.

- (117) In this regard, the Commission notes that profitability on the route can be expected to *[CONFIDENTIAL]* beyond the first three years of operations. Flybe projected operations for up to *[CONFIDENTIAL]*.⁷⁰
- (118) Moreover, in particular in case of adverse developments (identified for instance in the sensitivity tests conducted by the Monitoring Trustee)⁷¹ Flybe's financial situation, for instance with net funds of GBP 62.2 million and total cash of GBP 171.4 million according to its latest annual results 2015-16, is such that Flybe *[CONFIDENTIAL]*.⁷²
- (119) In addition, *[CONFIDENTIAL]*. This may act as an additional incentive for Flybe to operate the two routes in the medium/long term.
- (120) Finally, the Commission notes that Flybe has in place *[CONFIDENTIAL]*.⁷³ *[CONFIDENTIAL]*.⁷⁴
- (121) The Commission is of the view that Flybe *[CONFIDENTIAL]* evaluate the performance of *[CONFIDENTIAL]* operations and, notwithstanding *[CONFIDENTIAL]* projections in its business plan, and even if the events foreseen by the Monitoring Trustee's sensitivity analyses were to occur, it appears unlikely that *[CONFIDENTIAL]*.⁷⁵
- (122) To sum up, the Commission considers that Flybe's profitability projections and the Monitoring Trustee's sensitivity analysis indicate that *[CONFIDENTIAL]*. *[CONFIDENTIAL]* the Commission considers that *[CONFIDENTIAL]* the commitment demonstrated by Flybe to start operations on the Relevant City Pairs and *[CONFIDENTIAL]* in the medium/long term. In addition, Flybe, which has material available cash reserves, can count on *[CONFIDENTIAL]*.
- (123) In light of the above, overall, the Commission therefore considers that Flybe will have the ability to act as a material competitive force on the London Heathrow–Aberdeen route.

⁷⁰ Paragraph 163 of the Monitoring Trustee's report.

⁷¹ See footnote 44 above.

⁷² *[CONFIDENTIAL]*.

⁷³ *[CONFIDENTIAL]* would apply to the Relevant City Pairs.

⁷⁴ Agreed minutes of a conference call with Flybe of 21 October 2016.

⁷⁵ The Monitoring Trustee reports that *[CONFIDENTIAL]* (Paragraph 43 of the Monitoring Trustee's report).

Conclusion

- (124) Based on the above and all the other available evidence, and considering in particular (i) Flybe's ability to compete with BA in terms of frequency, capacity, service offerings and pricing, which are all important parameters of competition, as well as (ii) the available cash reserves of Flybe, which might help to withstand a temporary poorer performance on the routes than planned, (iii) together with its [CONFIDENTIAL], the Commission concludes on balance that Flybe is a viable potential competitor of IAG on the London Heathrow–Aberdeen route, with the ability, resources and commitment to operate services in the long term as a viable and active competitive force.
- (125) In any event, to mitigate any risk that Flybe would not operate on the route as stated in its application, and in particular in case of risk of Misuse⁷⁶, the Commission proposes, as a precautionary measure and without prejudice to its assessment on the viability of Flybe's operations, that the Monitoring Trustee closely and regularly monitors Flybe's performance activities on the London Heathrow–Aberdeen route under the relevant provisions of the Commitments, in particular Clause 6.2.1(f), which allows ad hoc reports to be produced by the Trustee to the Commission, at the Commission's request, on matters falling within the scope of the Commitments, as well as Clause 1.3.6 of the Commitments, which more specifically relate to the reporting procedure in case of envisaged risk of Misuse.⁷⁷ The Monitoring Trustee may in particular monitor factors such as slot utilisation, load factors, route performance, and adherence to banking covenants.

3.2.2. Conclusion

- (126) In the light of the above and all the other available evidence, taking into account the relevant evidence and the assessment of the Monitoring Trustee, the Commission concludes that overall Flybe meets the criteria in Clause 1.4.9 (a) in that it has the ability, resources and commitment to operate services in the long term as a viable and active competitive force on the Relevant City Pairs.

4. OVERALL CONCLUSION

- (127) Based on the foregoing considerations and all the other evidence available to it, the Commission decides in relation to the Flybe's slot application on the Relevant City Pairs that:
- i. Flybe is independent of and unconnected with IAG and has exhausted its own slot portfolio at Heathrow within the meaning of Clause 1.4.4 of the Commitments; and

⁷⁶ Misuse is defined in Clause 1.3.5 of the Commitments.

⁷⁷ When Little Red, which had been awarded slots to operate on the London Heathrow–Aberdeen and London Heathrow–Edinburgh routes, decided to cease operations on those routes, the appropriate application of the Commitments and the slot release agreement between Virgin and IAG lead to an orderly hand-back of slots.

- ii. Flybe is a viable potential competitor of IAG on each Relevant City Pair for which it has requested slots under the Commitments, with the ability, resources and commitment to operate services on each of the Relevant City Pairs in the long term as a viable and active competitive force.
- (128) This decision does not constitute a confirmation that IAG has complied with its Commitments.
- (129) This decision is based on Clauses 1.4.4 and 1.4.9 of the Commitments.

For the Commission,

(Signed)

*Johannes LAITENBERGER
Director-General*