



Are commercial revenues important to today's European air navigation service providers?☆



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ABSTRACT

In this paper we discuss the role of commercial revenues in the economics of European air navigation service providers (ANSPs) starting with the legal definitions of commercial revenues as contained in the respective European Union legislation. Based on the investigation of European ANSPs annual reports and/or strategic documents, we define the attributes of a new commercial model in the provision of air navigation services (ANS). We provide evidence that several European ANSPs have already implemented all or a majority of the attributes typical for the new commercial model. Discussing demand-side and supply-side drivers which could spur or impede the commercial business of European ANSPs, we assume the commercialisation of European ANSPs will be reinforced in future. Therefore, we design a set of partial indicators which enable us to analyse the role of commercial revenues in the economics of ANSPs.

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1. Introduction

While commercial revenues of airports have been studied in several papers - Graham (2009), Tovar and Martín-Cejas (2009), Castillo-Manzano (2010), Kratzsch and Sieg (2011), Fuerst et al. (2011), Lin and Chen (2013), Olariaga (2015) - commercial revenues of air navigation service providers (ANSPs) are ignored by current aviation research. Commercial revenues of ANSPs are not mentioned in CANSO (2014) Global Air Navigation Services Performance Report at all and although Eurocontrol (2015) ATM Cost-Efficiency 2013 Benchmarking Report contains information about so called other revenues of ANSPs (and the other revenue components as well), it does not provide any deeper analysis of commercial revenues. Papers devoted to the benchmarking of European ANSPs written by Mouchart and Simar (2003), Button and Neiva (2014), Bilotkach et al. (2015) did not use revenues (including commercial ones) as an output, thus leaving the revenue side of the ANSPs business untouched. Only Arnaldo et al. (2014) included income from charges and other revenues as outputs in the benchmarking of ANSPs. However, they were not interested more in the role of commercial revenues in the ANSPs performance.

There are several reasons why commercial revenues of ANSPs are not present as an issue in current aviation research. In the past, ANSPs were managed and operated as public utility entities - monopolists on geographical markets copying state borders. As public utility entities, they were focused on the delivery of air navigation services (ANS) in the public, and not commercial, interest. The processes of corporatisation and commercialisation of ANSPs started later in comparison with airports, and privatisation of ANSPs is still rare all over the world. That is why corporatisation, commercialisation and privatisation of ANSPs could not boost commercial revenues at the level recorded for the majority of corporatised, commercialised and privatised airports. Moreover, ANS have a specific nature if we compare them with airport services. While airport activities and airport aeronautical services (or at least some of them) are directly connected to passengers, ANS are predominantly delivered to airspace users. This does not enable ANSPs to exploit the potential of passengers to generate revenues of a commercial nature. However, on the other hand ANS can be (at least potentially) delivered to other ANSPs or other subjects on a commercial basis, if national regulation allows it and such demand exists. The commercial potential of ANS relates not only to core ANS (such as terminal control services within Air Traffic Management - ATM), but also to support ANS services (Communication, Navigation and Surveillance - CNS; Meteorological Services for Air Navigation - MES; Aeronautical Information Services - AIS; Search and

☆ When creating the title we were inspired by Graham (2009) paper: How important are commercial revenues to today's airports?.

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Rescue – SAR) and to supplementary services (training, consultations, projects, publications etc.) as well.

A new situational context in which ANSPs run their business at present - competition of some ANSPs on the market for en-route services in fragmented world regions, deregulation of terminal control services in some countries, pressure on the ANSPs cost efficiency from air carriers driven by sharpening competition among them, capital intensity of the ANS production driven by new technologies, deficits in public budgets, etc. (Tomová, 2015) – encourage ANSPs to conduct their business in a more commercial way. In the European Union, where, under the common European performance scheme and common charging system, the potential profit of ANSPs is regulated, the issue of commercial revenues acquires attention as a regulatory problem¹ - and in the long-term perspective - as a structural problem taking into account more radical structural changes towards more liberalisation, as projected by the European Commission.

In this paper we discuss the role of commercial revenues in the economics of European ANSPs starting with legal definitions of the term contained in the respective EU common charging regulations. To provide evidence of commercial business, we investigated annual reports and strategy documents of European ANSPs, focusing particularly on how European ANSPs declare themselves with regard to commercial activities. We define a new commercial business model of ANSPs, listing its attributes, and design several indicators which could help to analyse the commercial side of ANSPs business. A new approach to the product portfolio of ANSPs is explained here in this context. We discuss which factors could spur or impede the generation of commercial revenues in the business of European ANSPs in future. And finally, we project the rails for further research.

2. Funding of ANS in the European Union by commercial revenues

In general, there are two main models of ANS funding – direct funding from user charges and indirect funding from governmental budgets or specific governmental funds. Actually, the majority of ANSPs in the world are financed by several means, using a combination of direct user charges and indirectly generated sources.² In the European Union, revenues generated by direct user charges for air navigation services (en route charges and terminal ones levied on airspace users) are principal sources of the ANSPs funding, which is fully in line with the ICAO's recommendations contained in Doc 9082 ICAO's Policies for Airport Charges and Charges for Air Navigation Services (ICAO, 2009). Between 2007 and 2011, the Commission Regulation (EC) No 1794/2006, laying down a common charging system for ANS, required the costs of en route services to be financed by means of en route charges imposed on the users of ANS and the costs of terminal services to be financed by means of terminal charges imposed on the users of air navigation services and/or other revenues, including cross-subsidies in accordance with Community law. The nature and components of other revenues were not defined by the regulation at all although, according to the regulation, member states were required to describe the

income from other sources when they existed.

Between 2012 and 2014, i.e. in the first reference period, the common charging system in the European Union was interrelated with the common performance scheme for ANS. In this period, the Commission Regulation (EU) No 1191/2010 amending the Commission Regulation (EC) No 1794/2006 defined other revenues as revenues obtained from public authorities or revenues obtained from commercial activities and/or, in the case of terminal unit rates, revenues obtained from contracts or agreements between air navigation service providers and airport operators, that benefit air navigation service providers with regard to the level of unit rates. Thus, the term revenues obtained from commercial activities (i.e. commercial revenues) was used for the first time in the respective EU common charging regulation. The regulation also required a description of revenues from other sources when they existed. Contrary to the previous regulation, the new rules enabled the funding of the determined costs of en route ANS by en route charges imposed on airspace users and/or other revenues. The determined costs of terminal ANS could be financed by terminal user charges and/or other revenues, keeping an option for cross-subsidies granted in accordance with Union law as set in the previous regulation. Under the common performance scheme in the first reference period, the cost efficiency of en route services started to be regulated as a key performance indicator at European and local level.

Starting from 2015, i.e. from the second reference period, the Implementing Regulation (EU) 391/2013 defined other revenue as revenues obtained from public authorities, including financial support from Union assistance programmes such as the Trans-European transport network (TEN-T), the Connecting Europe Facility (CEF) and the Cohesion Fund, revenues obtained from commercial activities and/or, in the case of terminal unit rates, revenues obtained from contracts or agreements between air navigation service providers and airport operators. As in the previous regulation, a description of other revenues, was required, however, broken down according to the above-mentioned categories. The prescribed unit rate calculation tables for the second reference period distinguished the revenues from Union assistance programmes, national public funds, revenues from commercial activities and the rest called other/other revenues as components of the total other revenues. For the first time, the respective reporting table for calculation of unit rates required to mention separately the value of revenues from commercial activities. This at least indicates an increasing role of commercial revenues in the ANSPs funding. During the second reference period, the cost efficiency key performance indicators have been designed to cover both the cost efficiency of en route ANS and the cost efficiency of terminal ANS (the cost efficiency target for the terminal portion is expected to be announced in the middle of the second reference period).

Why was it so important to make definitions and rules for commercial revenues in the EU charging regulations more precise? Unclear definitions and rules with regard to commercial revenues could lead to ambiguities and any such ambiguity could cause at least misunderstanding at the ANSPs level. Moreover, national strategic gaming under unclear definitions and rules could be supported in this way. If other revenues (and commercial ones too) are deducted when setting the level of cost basis then unit rates (prices) decrease – *ceteris paribus*. This approach to pricing is known as single till in aviation infrastructure economics. This means that profits generated by commercial revenues decrease the cost bases necessary for the establishment of prices. For this reason, the calculation of unit rates for ANS in the first and the second reference period contained also calculation of unit rates (both en route and terminal ones) that would be applied without other revenues.

¹ Under specific conditions given by the respective regulations only some parts of the ANSPs economics are not regulated by the European Commission (for instance, costs of CNS, AIS, MET, SAR, if provided under market conditions, are not required to be included in the cost basis which is relevant in setting regulated charges).

² The provision of air navigation services in the US is primarily funded through the sources of Airport and Airway Trust Fund (AATF) and sources of general budget as well. Indirect taxes are levied to generate income for AATF. However, only overflights are charged by charges with differentiated unit rates for continental and oceanic airspace. The rates are applied on distance flown (FAA, 2015).

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