

2009

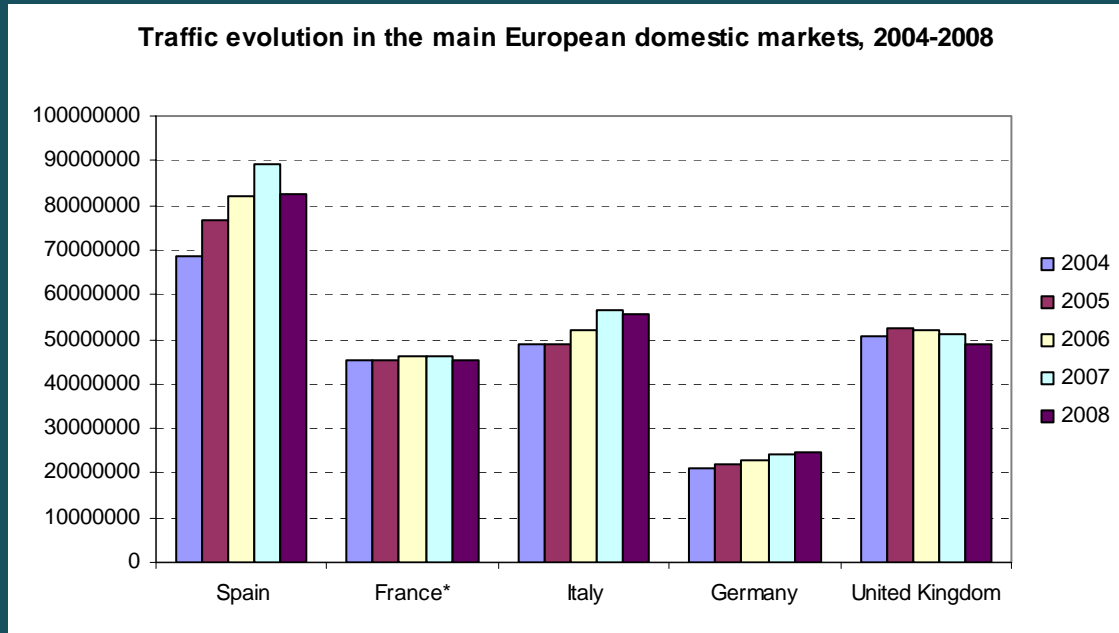
AIR TRAFFIC SPANISH  
DOMESTIC MARKET. A  
QUICK VIEW



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The European air domestic markets recorded a period of stagnation during the last five years. Spain was an exception until 2008 when the impact of the financial crisis hit the local market returning to the 2006 levels. Italy showed some vigorous growth in 2006 and 2007 but like in the rest of the continent 2008 was a year of declining traffic.

Graphic 1.



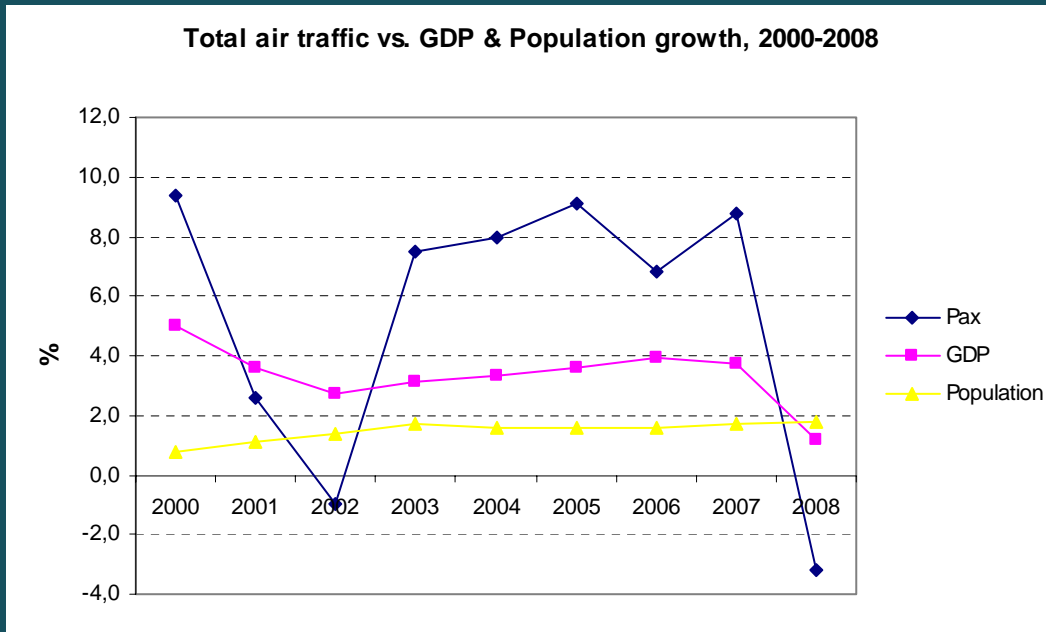
\*French data includes metropolitan traffic only. Source: Aena (Spain), UAF (France, ENAC (Italy), Destatis (Germany) and CAA (United Kingdom).

Air traffic tends to grow faster than the economy and the population. Despite the significant increase of the Spanish GDP during the last decade the demand for air transportation has been stronger during the whole period except in 2001/02. The impact of 11S was painful in the industry and Spain wasn't an exception. Until 2008 the growth rate of the air traffic in Spain doubled the economic growth of the country. The direct relation between the demand and the economy was tested in 2008 when the sudden decline in the economic activity was followed by a dramatic collapse in the number of passengers. This overreaction is consistent with the exceptional growth that characterised the years of intense economic activity in the country.

The role of the population growth in the generation of demand can be easily ignored in the developed countries. However in Spain the impact of massive immigration and the record levels of fertility paved the way for an impressive growth of its population from 41m in 2000 to 46m in 2008 (+12%). And this change in the size of the local market had a positive impact in the demand for air transportation.



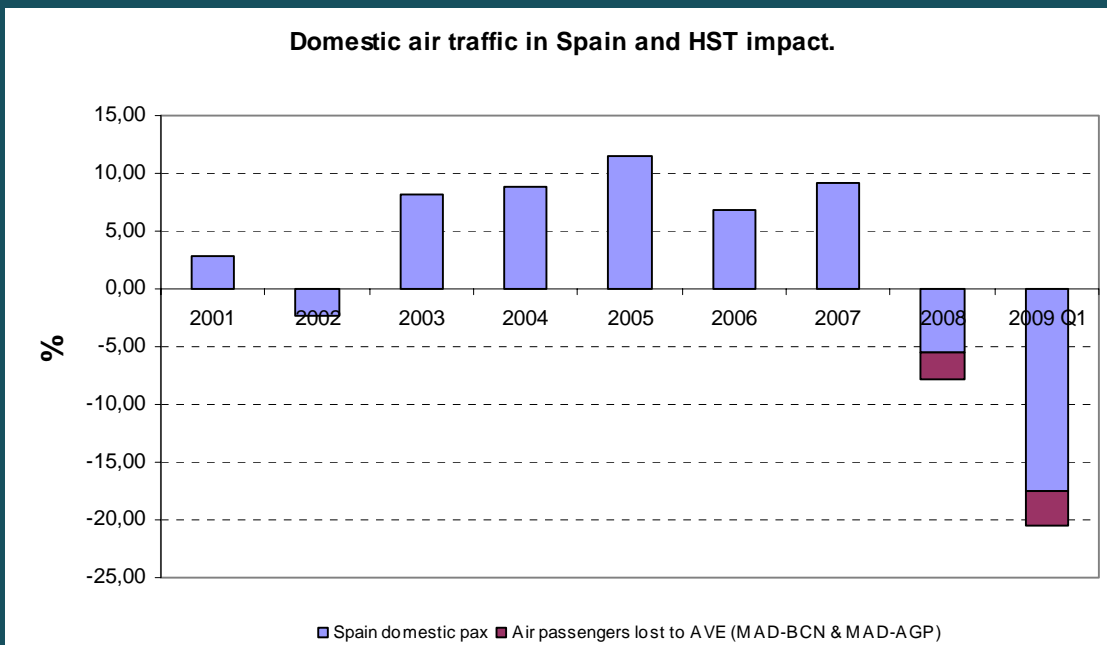
Graphic 2.



Source: Aena & Eurostat.

The increase of the domestic activity in the Spanish airports was strong from 2003 to 2007 with traffic increases well above 5% (11.5% in 2005). The drop in demand experienced in 2008 (7.7%) is especially painful for the local industry even if the third part of it (2.3%) comes from the new High Speed Train, HST, services. The first quarter of 2009 showed dramatic results with a total loss of 20% of the traffic recorded the previous year. The new HST lines to Madrid-Barcelona and Madrid-Málaga represent only 3% of the decline.

Graphic 3.

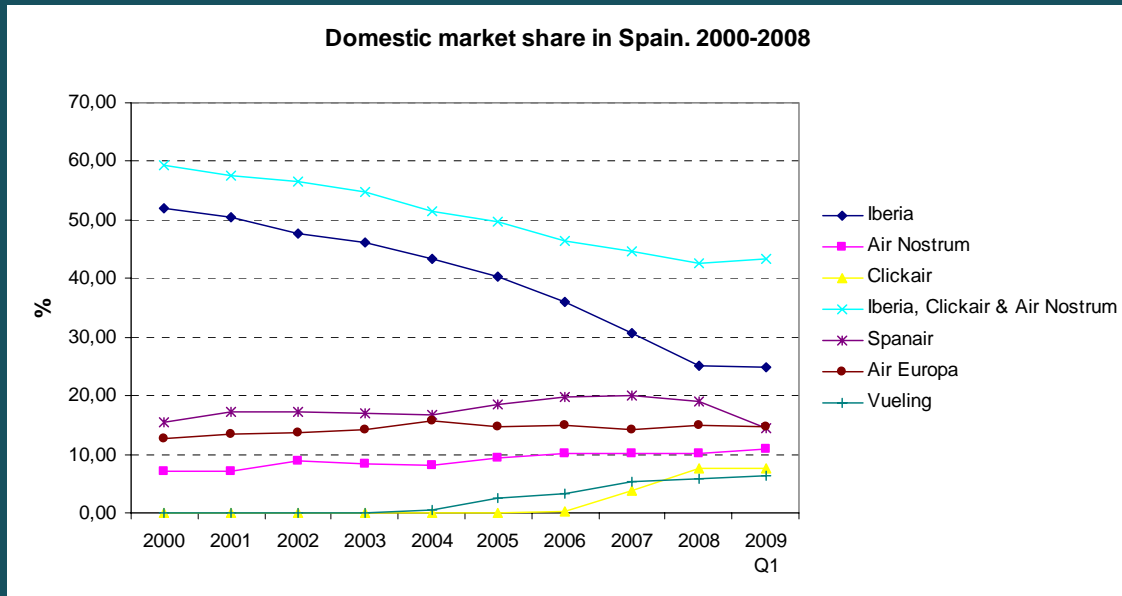


Source: Aena.



Since 2000 Iberia has seen its position eroded uninterruptedly until 2008. The competition of other already established carriers (Spanair & Air Europa) and the irruption of new low cost entrants (Vueling & Clickair) had a deep impact in the market share of the former flag carrier. Adding the traffic of Iberia, Air Nostrum and Clickair (franchisee and participated by Iberia respectively) the scenario is slightly better but still negative for this group of carriers.

Graphic 4.



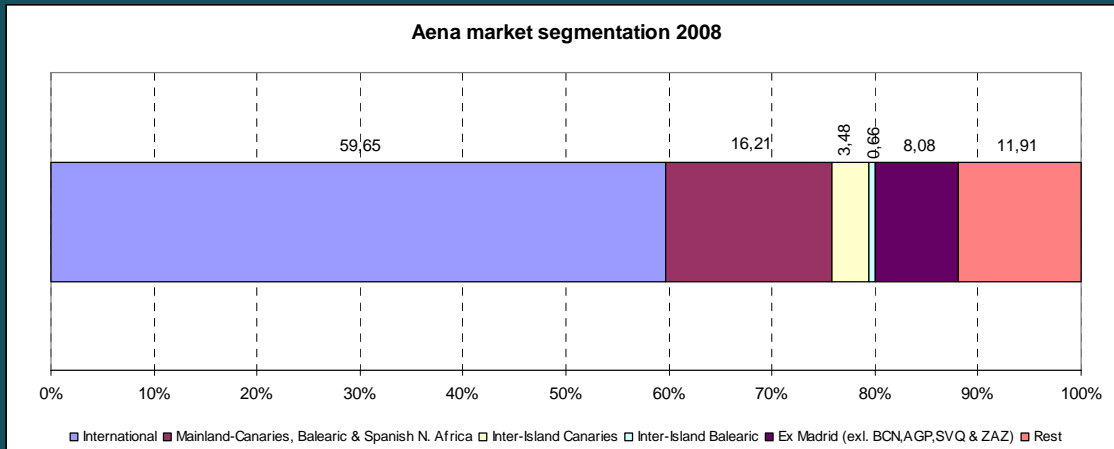
Source: Airlines websites.

The first quarter of 2009 gives an interesting picture of the early consequences of the current crisis. The strongest carrier, Iberia does not lose traffic. Spanair, immerse in a transition period sees its market share plummets and the low cost carriers, Vueling and Clickair, prepare for their merger. The outcome of the current adverse climate for the industry seems to be beneficial for Iberia and its associates leaving their competitors in tatters.

One of the main concerns in the Spanish air transport industry is the impact of the AVE (High Speed Train) in the market. After the new lines Madrid - Barcelona and Madrid – Málaga were put in service in early 2008 the relevance of the destinations potentially affected by new HST lines is quite limited. Essentially only 8% of the market is under threat and according to the current evolution of the above mentioned lines the air carriers would keep at least 50% of the pasengers.



Graphic 5.

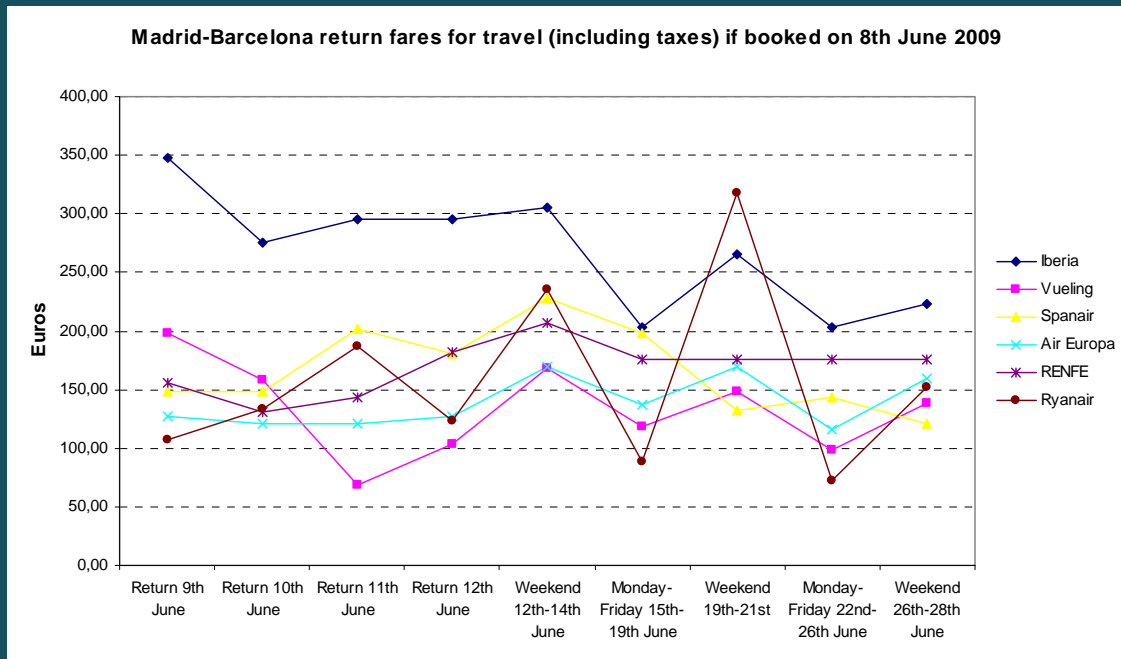


The irruption of the AVE has realigned the offer in the main Spanish corridor. RENFE has introduced a more flexible fare structure in order to compete with the more advanced airlines' capacity management. However, if trips can be planned at least one week in advance the train return fares can be more expensive than those of the airlines except Iberia.

Overall Iberia is the most expensive carrier in the route. It offers the "Puente Aéreo" (air shuttle) a long time established service, very efficient but expensive oriented to the high yield business market. Spanair, after its sale to a group of Catalan investors, maintains its focus on business traffic keeping the short term fares high but attracting low yield passengers through long term cheap prices. Air Europa and Vueling offer a more stable fare structure being the last one the cheapest in the market.

Surprisingly Ryanair operating to Gerona can be a very expensive option during the weekends. It has a volatile fare structure still focused on leisure travellers. Probably the airport is too far away from Barcelona to attract the business demand.

The AVE is relatively expensive and the journey time is longer than by air. Airlines tend to maximise their revenues in the short term converging the fares in the medium term. Iberia is the only air carrier keeping the fares above 200 Euros; the others are consistently under this price.



Graphic 6.

Source: RENFE and airlines websites. The fares shown are the cheapest available excluding the departures that make the trip non viable.

