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## ETRC contribution to the EU Consultation on how retail activity can improve the competitiveness of European Aviation

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Over the past few decades, the EU aviation market has changed considerably. It is now widely agreed that Europe needs to improve the commercial competitiveness of its airports. ETRC believes that duty free and travel retail can make a significant contribution to this goal.

Creating a policy framework which will allow Europe's airports to fully exploit their commercial opportunity is a sensible and straightforward way to help solve what is becoming a systemic funding problem. Without a solid retail and commercial income, airports struggle to invest for the future and to maintain world class facilities.

The income provided by the Duty Free and Travel Retail (DFTR) industry is an important revenue stream for all airports and in some cases allows smaller airports to continue to operate when otherwise they would no longer be commercially viable without government subsidies, which will no longer be permissible under EU rules. DFTR also directly employs tens of thousands of people in Europe and provides a vital shop window for many European produced goods.

European aviation over the last 60 years has grown in parallel with, and been supported by, the growth of airport retailing. For passengers, the opportunity to shop at the airport has become an integral part of the travel experience; 47% of passengers list shopping as one of their favourite airport activities and 60% of European passengers regularly make purchases at airports, a significantly higher figure than in the US for example. Shopping at the airport has replaced mandatory charging with discretionary spending.

Airport retailing contributed around 15% of total airport revenues in 2011, growing from 11% in 2008. For most small to medium sized airports, retailing generates a revenue contribution equivalent to around €2-3 per passenger, with the largest airports generating €4-5 per passenger. Income per passenger can vary wildly depending on the route concerned with certain nationalities being particularly high spenders.

**ETRC believes that improving airport retail will make Europe's airports more commercially viable. Support and recognition for the important role played by airport retail will make that much easier to achieve. In this paper we set out our rationale and the initial policy areas which we believe need to be addressed. Fundamentally however, we wish to see the EU recognise the role played by duty free and travel retail, and to take the necessary steps to help us expand and grow the business.**

In 1947 the world's first airport duty free shop opened its doors in Shannon, Ireland. The purpose of this shop was simple – to satisfy the needs of passengers and to provide the necessary revenues to improve and maintain essential airport facilities. Almost seventy years later, we believe that need is still there, and that with EU support, we can help keep Europe's airports thriving.



## Changes in the Airport market, and DF&TR's contribution to airport finances

Airport retailing, which is a key element of broader commercial revenues, has been subject to significant challenges over the last twenty years. The ending of duty-free sales on intra-EU flights in 1999 removed the fiscal advantage of much of European airports' retail offering, forcing airports and retailers to re-fashion their offerings to passengers.

The accession of a further ten countries to the European Union in 2004, and two more in 2006, and most recently Croatia in July 2013, further reduced the scope for tax-advantaged shopping at Europe's airports. Retail revenues have also been subject to the same demand shocks that affected air travel in general since 2000, yet the sector has shown itself to be remarkably resilient and continued to deliver significant income to airports.

Just as the industry faced geo-political and economic challenges in the past, the move from bricks and mortar retailing towards online purchasing is making it increasingly hard to attract passenger demand in a world where individuals have a much wider choice of retail purchasing options..

*Retail revenues contributed around 15% of the total aeronautical and non-aeronautical revenues of European airports in 2011, increasing from 11% in 2008. In absolute terms, they rose from €3.1 billion in 2008 to €4.1 billion in 2011. Retail is the largest single component of non-aeronautical revenues at 43% of the total and its share is growing.*

The DF&TR industry advocates the creation of a 'virtuous circle', whereby retail revenues may be both the result of success in attracting passengers but also a platform for assisting in the finance of future expansion and improvement of Europe's airports.

The need for such investment, combined with the pressures from airlines on airport charges suggests a growing reliance on retail revenues. Anything, therefore, that holds back the development of retail revenues - whether it be government regulation, external economic shocks or airline commercial practices - runs the risk of impeding future airport development.

## The growth in competition between airports

Airport competition has been growing strongly in Europe over the past two decades. Most airports, particularly the small to medium sized airports, face significant competition as airlines switch routes and bases depending on cost as well as passenger demand and passengers are able to switch to neighbouring airports.

Facing competitive pressure on aeronautical charges, and with little or no state funding, airports are seeking to develop more commercial opportunities, especially retail services. Most airports in Europe compete strongly on price and service with their rivals. Those airports which are profitable generate on average normal returns on capital, although a substantial minority (almost 50 %) are currently loss-making.

Airline competition is also strong and dynamic, driven primarily by the continued growth of the leading low cost carriers. There has been some concentration in this market in recent years, with Ryanair and EasyJet growing large pan-European fleets, two to three times the size of their next tier rivals.



Smaller airports therefore often face a strong single airline with buyer power - over 70% of the smallest airports (less than 5 million passengers per year) have one airline accounting for over 40% of traffic.

Airline buyer power can benefit passengers, if keener airport charges are passed onto passengers. But this buyer power can also undermine development of the airport, for example if airline rules, such as including airport shopping in the 'one bag' rule, undermine airport retailing, at the expense of passenger choice, experience and of airport financing of facilities.

**Retail revenues make a major contribution to overall airport profits. For most small to medium sized airports, retail revenues represent at least 50% of overall net operating profit per passenger. Most importantly, this contribution arises from discretionary spending, at the passengers' choice, rather than any mandatory levy or charge.**

### Market Relationships

Airports are businesses which serve two main distinct but closely related markets: airlines on the one hand, and passengers on the other: airlines value the airport being popular amongst travellers and passengers value the airport being able to offer a wide range of airlines and destinations.

The consequences of this model for an airport's overall financial health is that it must consider carefully the impact of changes in demand conditions for passengers at the airport which may be brought about by changes in prices and practices adopted by airlines.

Today's European aviation market is characterised by more 'footloose' airlines and airports have had to respond to this and become more commercially focused as they themselves undergo change to being privately owned or run at arms-length from government.

Unlike airlines, airports are fixed-cost businesses requiring major investments in runways, terminals and equipment, and a large proportion of their operating expenses varies little with scale. This means that airports are hugely dependent on attracting new airlines, new routes and more passengers. For many airports, it only takes a change of a few aircraft and/or the withdrawal of a few routes to markedly affect profitability.

Airports need to compete both to retain and attract this highly mobile traffic through their price and service offerings to airlines, not least because of the vulnerability of their business to the loss of routes.

The increase in the number of airports (often through use of previously military airfields) and, more importantly, the range of routes now available at airports generally means that passengers have, within reasonable travelling distance, more choice of airport available to them. Nearly two-thirds (63%) of European citizens are within two hours' drive of at least two airports. This gives significant scope for airports to compete for passengers.

In part, airports exposed to competition from near neighbours compete for passengers by competing for airlines and increasing the range and depth of routes available. But, increasingly, they also need to appeal to passengers directly through the quality of service they offer and the ease of travel through the airport.



## The Passenger Experience

According to a survey of European residents, travellers from Europe are regular Duty Free & Travel Retail (Duty Paid) buyers - they buy on average every second time that they are on an international trip (5 out of 10 times). 60% of travellers from Europe regularly purchase something at Duty Free & Travel Retail shops, nearly half of whom (27% of all travellers) are frequent buyers (buying almost every time). 40% of travellers hardly ever purchase anything when flying. Evaluating the time spent at the airport, 16% of the time is spent on shopping. Based on the average time spent at airports before a flight, 14 minutes are devoted to shopping

Looking more broadly at the experience of a major airport retailer operating at UK airports, typically around one in eight passengers on flights within Europe (13%) make purchases in the main tax-free shopping centre at European airports, rising to one in four (25%) for flights outside the European Union.

Research by one major UK airport places airport shopping as the sixth most important factor for passengers at the airport in contributing to their overall satisfaction assessment, behind overall comfort, cleanliness and travel information, but ahead of security, catering and baggage handling. Furthermore, airports increasingly offer innovative ways for passengers to shop at the airport. Some airports are entering on-line retailing as a complement to their physical sales outlets within terminals.

Participation in airport retail, whether shopping or merely browsing, has become an integral part of passengers' airport experience - just as the resulting revenues are an integral part of airport finances. The growth of retail revenues over the years clearly demonstrates that passengers positively value the opportunity they are given; and that the choice of goods now generally available is conducive to deciding on impulse whether and what to buy.

## Our proposed way forward

Airport retail in Europe needs a supportive regulatory framework in order to thrive. Duty free and travel retailing in Europe requires urgent recognition of its unique nature and of its innate value. Overall a concerted EU policy is required that will encourage EU airports to invest in commercial activity.

A precedent exists in Espace Voyageur, the legal framework governing travel retail in France which allows different interpretation of Regulations to take account of our particular retail channel. A similar approach at EU level would be very much welcomed. The one-size fits all approach of EU Regulation often does not work well in DFTR, impeding growth. All we are asking is a greater understanding of our retail channel at EU level, and a greater willingness to help the retail channel continue to flourish.

At the outset, we have identified the following policy areas where EU support is needed to ensure that policy objectives can be met without restricting retail growth and passenger choice. However we see this very much as a starting point to be built on over the years.

## Labelling/packaging Legislation

Airport retail is different to the domestic market. We sell to an international audience that speak a multitude of languages.



We stock a significant proportion of travel retail exclusive products which are packaged differently or simply not available in the domestic market. The recent introduction of the Food Information to Consumers Regulation threatens to change that considerably as all goods will have to be labelled in the language of the country they are sold in, and the relatively small production runs preclude differential labelling. Furthermore this is causing a logistical nightmare for our suppliers and distributors and is impossible to fulfil as suppliers do not know what the end market will be for the goods they ship to the retailer who may have stores in every single EU Member State. Furthermore, EU labelling & packaging rules are being supplemented by Member States introducing requirements for their own markets. This complicates even further the supply chain to DFTR, especially in smaller Member States.

Many products are set to be discontinued as it is no longer economically viable to supply. The EU is now considering extending this Regulation to alcohol products. This will further exacerbate our unique problems with the Regulation.

ETRC is not advocating that we are exempted from these rules. We do however need flexibility in how we communicate with our customers. For example, through the use of modern technology we can provide multilingual solutions which cater for our passenger profile. We believe we can not only meet the policy objectives of the Regulation, we can do so in a more effective manner than that required by the Regulation – in this case by providing information in several languages, not just that of the country in which the product is being sold.

### **Customs Allowances**

Duty free allowances for alcohol and tobacco have been in place in Europe since civil aviation began and are the cornerstone of the offer we make to our customers. These allowances need to be maintained so that passengers can shop with confidence.

### **Passenger Rights**

The dynamics of the air transport industry are forever evolving. It is now commonplace for airlines to charge for hold luggage. This has led to a significant increase in congestion for hand luggage space on-board which we believe will get worse as airlines increase their hold baggage fees.

Duty free and travel retail is not the cause of this congestion, but it has been the victim of over-zealous airlines implementing strict 'one bag' rules and forcing passengers to either discard shopping or pay outrageous 'fines' to bring their goods on-board.

The only way we can stop this and give the customer confidence is by Regulation. A very simple amendment to the Air Passenger Rights Regulation which will restore to passengers the right to bring on board their airport shopping in addition to their hand luggage would have a transformational impact upon consumer confidence.

### **Airport Security**

ETRC fully supports the efforts of the European Commission and the Member States to secure Europe's airports. The introduction of STEBs in 2006 in order to protect airport retail revenues is a prime example of industry and government working together effectively.



Airport security is paramount and all stakeholders including retailers must play their role. Nonetheless we do believe that when calculating the cost of security, due attention must be given to the impact upon commercial income. Airport shops in Europe lose millions in revenue each year because of delays in processing passengers through security.

## **External Relations**

The EU is currently negotiating Open Skies agreements with a number of Third countries. ETRC supports these initiatives and is happy to help in any way it can to progress negotiations. New traffic means new customers for our shops so anything that makes that happen has our full support. We would also advocate priority be given to agreements with countries that traditionally have high-spending passengers. ETRC and its members have developed very advanced research of the spending patterns and tastes of most nationalities which we are very happy to share with the European Commission and Member States.

## **Conclusions**

Airports in Europe are currently faced with many challenges, particularly as it relates to long-term commercial viability and airport retail offers one avenue to ameliorate this situation. However, DFTR in Europe needs a supportive regulatory framework in order to thrive. Duty free and travel retailing in Europe needs urgent recognition of its unique nature and of its innate value. ETRC is therefore calling for the European Commission as part of its consultation on EU aviation competitiveness to recognise the important and growing role that retail can and does play in airport funding, and to come forward with a wider plan for support for airport commercialisation on issues such as; advertising, property income/rent, rental car concessions, car parking, food & beverage and last but not least retail concessions which are such a key generator of airport income.

## ***About the European Travel Retail Confederation (ETRC)***

*The European Travel Retail Confederation (ETRC) is an industry association representing the interests of the duty-free and travel retail industry in Europe, focused on creating the right environment to allow the industry to operate and achieve its potential. The organisation works closely with European and international governments, regulatory authorities and other stakeholders. ETRC is composed of 11 national and regional affiliated trade associations representing over 200 European companies, Tax Free World Association (TFWA) representing 500 brand companies, and direct corporate membership from 33 individual companies working in the duty free and travel retail trade across Europe and beyond.*

*The European Travel Retail Confederation's operations are directed by its Supervisory and Managing Boards and carried out by a full-time secretariat. For more information about the organisation, please see our website – [www.etruc.org](http://www.etruc.org)*