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Chair
Public Accounts Committee
Welsh Parliament
Cardiff Bay
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12 November 2020

Dear Chair

CARDIFF AIRPORT

I am writing in advance of the further scrutiny session with Welsh Government officials on 16 November 2020.

I am grateful to you for your agreement to hold part of the Committee session in private. The international situation with regard to aviation and airports in the context of the COVID-19 pandemic remains very uncertain. Due to the degree of commercial sensitivities around Cardiff Airport's own recovery from the impact of COVID-19, there will be a limit to what officials will be able to share with the Committee, even during a private session. However, in the latter I hope we can discuss more candidly some of the complexities of the challenges the Airport is now facing.

COVID-19 has had a catastrophic effect on the global aviation industry this year, leading to the curtailment of virtually all passenger flights, deserted airports and the grounding of entire fleets. The pandemic continues to have profound global impacts and we are now firmly into a second wave of infections across the UK and Europe which has instigated a number of confinement measures and border restrictions by different countries and states. Whilst emerging news this week about a successful vaccine is promising, a long and protracted recovery is inevitable.

Aviation has been one of the sectors most heavily affected by the COVID-19 pandemic, which in turn has caused an existential crisis for the aerospace industry more widely. The impact has, and will continue, to be stark for many companies. It is already clear that COVID-19 has had a much greater impact than any previous crisis, with significantly reduced aircraft production expected for the remainder of the year, global supply chain disruption and future

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order deferrals. Industry redundancies are already widespread and will have a significant impact on communities throughout the UK that rely on the highly skilled manufacturing jobs our sectors provide.

In the wider sector, aerospace production rates will be severely affected to 2025 and beyond. Within the space of eight months we have seen new aircraft production down over 30 percent and the regular maintenance, repair and overhaul activities drop to around 50 percent of levels seen in 2019.

Globally, the impact of COVID-19 has caused a significant reduction in passenger numbers, resulting in flights being cancelled or planes flying empty, which has impacted in massively reduced revenues for airlines and has forced many airlines to lay off staff or declare bankruptcy. Some have attempted to avoid refunding cancelled trips in order to lessen their losses. This has had a knock-on effect on supply chains as airliner manufacturers and airport operators have also laid off employees.

World recovery of passenger demand to pre-COVID-19 levels is estimated to take anything between two and six years, with large regional differences anticipated: currently the Asia-Pacific region has the shortest estimated average recovery time, followed by North America, and Europe. For air freight demand, a shorter average world recovery time is predicted when compared to passenger demand.

Earlier this year, the International Air Transport Association (IATA) estimated aviation industry revenue losses of US\$30 billion due to COVID-19; by April it had revised its estimates to US\$314 billion.

Due to the sudden and large losses of revenue, airlines have offered vouchers and the option to change flights over refunding cancelled flights and tickets in order to conserve cash. In Europe, airlines have successfully negotiated to defer some US\$1.2 billion in air traffic control charges, and as traffic may not return to pre-pandemic levels until the mid-2020s, retirement of older, less fuel-efficient, and higher maintenance aircraft is accelerating.

The sudden drop in air traffic has led to almost complete paralysis of both aeronautical and non-aeronautical revenues across the globe. As airlines cut capacity, the aeronautical revenues airports receive from airlines, such as landing charges for aircraft and security charges, fall. As people have stopped flying, non-aeronautical revenue, derived from airports' parking facilities, restaurants, or duty-free, have also plummeted. According to the Airports Council International (ACI), total airport revenues fell by 35 percent worldwide in Q1 2020 (equivalent to \$14 billion) and by 90 percent in Q2 2020 (equivalent to \$39 billion), and it has warned of a "collapse of significant parts of air transport system" following the announcement of a continued downward trend in passenger traffic.

The impact of COVID-19 on the UK specifically has been profound and the future of the industry remains stark. Due to the current English firebreak restrictions, Manchester Airport has moved all of its operations to its Terminal One until further notice and has announced 465 job losses. The decision to consolidate its operations has involved shutting down Terminal Three from 11 November. Terminal Two, which closed on 2 September, will continue to remain shut. UK-based Manchester Airports Group (MAG), which also owns the London Stansted and East Midlands airports, is reportedly planning to cut more than 900 jobs across its airports. Gatwick Airport is forecasting it will take four to five years to recover to pre-COVID-19 passenger numbers, and airlines continue to lose money. EasyJet is predicting a £845m loss this year and continues to review its liquidity position along with assessing further funding opportunities, including sale and lease backs of its fleet.

UK airports generally have paused expansion plans with an estimated value of £1 billion.

Data recently published shows a year-on-year decrease of 73 per cent in passenger traffic at Europe's airports in September. The loss of an additional 172.5 million passengers in September bringing the total volume of lost passengers since January 2020 to 1.29 billion. As of mid-October, passenger traffic stood at 75 per cent down from the same period last year, reaching an 80 per cent decrease for airports in the EU/EEA/Switzerland/UK footprint – a clear downward trajectory.

In late October 2020, ACI Europe stated that 193 (mostly regional) of the 740 airports in Europe were risking insolvency in the coming months if passenger traffic does not start to recover by the year end. These airports between them facilitate 277 thousand jobs and €12.4 billion of European GDP. The threat of airport closure means Europe faces the prospect of the collapse of a significant part of its air transport system – unless governments step up to provide the required support.

Since March, Welsh Ministers have repeatedly called for the UK Government to provide a bespoke package of support for the aviation industry. Ministers continue to pursue the devolution of Air Passenger Duty to Wales, along with the introduction of a suite of new domestic PSO air services in order to help revitalise the sector when national and local lockdown measures are eased. Ministers have also called on the UK Government to change its position on the provision of allowable assistance to airports in relation to safety and security costs which are disproportionately high for smaller regional airports such as Cardiff. Other major European countries and even the United States have provided billions of support for their aviation sectors; as such, we stand ready to work with the UK Government to support the aviation industry which is essential to the UK's economic long term success.

The cessation of all passenger flights in March 2020 created an immediate funding need for Cardiff Airport. Our short term solution to this was to repurpose £4.8m of an existing £21m loan facility to provide a bridging loan under MEOP state aid cover until other funding can be agreed and accessed. This was undertaken on commercial terms with a high interest rate in recognition of the high commercial risk and extraordinary international circumstances. The loan repurposing continues to enable Cardiff Airport to meet its short term liabilities as they fall due.

The repayment of Cardiff Airport's capital, and interest, was envisaged to come from seeking and securing COVID-19 related damages under a notification, which was recently submitted to the European Commission. The repurposing of loan funds was designed to cover the Airport's short-term liquidity needs before the airport receives any COVID-19 damages compensation. We are currently waiting to hear the outcome of that damages application from the Commission.

In response to the crisis, Cardiff Airport initially closed its passenger terminal facility until it was reopened in July and the management team have been working hard to reduce costs as much as possible and generate new sources of revenue. Alongside emergency funding, the Airport has taken a number of cost-saving measures including: taking advantage of UK Government's Job Retention Scheme; banning all non-essential overtime; providing parking facilities to a number of British Airways jets which were grounded during the COVID-19 crisis; and negotiating discounts to various contracts across the business. These measures saved the airport c£2m by the end of July, but inevitably the business still requires substantial ongoing financial support.

We recognise that the loan finance being made available to the airport is a short-term solution and that a longer term solution needs to be found to support the significant impact COVID-19 is having on the airport and the aviation industry in general.

A detailed review is underway to enable us to carefully consider the future strategy of the airport and the funding options available to us. This is particularly challenging in relation to EU state aid implications and the implications of leaving the EU with uncertainty as to the future arrangements that will apply. Officials are working closely with Cardiff Airport to evaluate the impact of the COVID-19 pandemic on the Airport including future funding actions in relation to recovery options.

Our headline ambitions for Cardiff Airport, beyond recovery from the impact of COVID-19, remain focussed on the airport becoming financially independent through growth and airline development, whilst having a keen focus on environmental sustainability. However, these ambitions are subject to the business and industry recovering from the pandemic.

Officials continue to work with Cardiff Airport's senior management team to develop a suitable and realistic business plan which will see the airport adapt to new ways of working and living in an ever changing world.

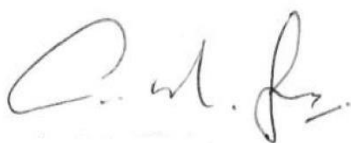
The Airport remains open as vital a transport hub and a legitimate pass through location for people. However, during the course of the national restrictions in England and in line with FCDO advice, Cardiff remains open for essential travel and for those with a legitimate reason to travel (such as education).

Welsh Ministers look to the UK Government to review its aviation policy (a reserved matter) to reflect the extraordinary situation we are now in, and to create and fund a substantial package of support that can support the regulatory and financial costs on critical regional airports such as Cardiff. Welsh Government awaits the work of the Department for Transport's Regional Connectivity Review and an understanding of the outcome of HM Treasury's review of the devolution of Air Passenger Duty to Wales.

My team and I look forward to discussing these matters further with the Committee during our evidence session on 16 November.

With best wishes.

Yours sincerely



Andrew Slade
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