

It's the Economy, Stupid

A report from HACAN ClearSkies argues it is a mistake to see the current debate about airport expansion as the economy versus the environment. Rather, the debate should be about the real value of airport expansion to the economy. **February 2003**

Introduction

The debate about airport expansion has been portrayed as: "the economy versus the environment". The perceived economic benefits of expansion have been set against the social and environmental downsides. In the debate, the economic benefits have been taken as read. This report argues that this is a mistake. The report raises serious questions about the economic justification of airport expansion. It argues that, before government gives permission for any further expansion of airports, it should take a cold, hard look at the importance of aviation to the UK economy.

The benefits of aviation to the UK economy are much less clear-cut than is commonly assumed:

- The aviation industry has attracted considerable inward investment to the UK, **yet** that has been overtaken in recent years by the amount UK firms, encouraged by good air links, have invested abroad.
- The UK's world-wide air links enable millions of tourists to visit Britain, **but** tourist spending in this country doesn't match the amount Britons spend abroad when they fly off on foreign holidays, leaving the UK with an annual deficit in tourism.
- The aviation industry presents itself as a sleek, mean machine, **yet** it receives tax concessions from the Exchequer of over £7 billion a year.
- The argument is made that expansion is essential for business, **yet** only 24% of passenger trips are for business purposes.
- Cheap flights have opened up new travel opportunities for many people, **but** 75% of seats on the low-cost airlines are taken by the wealthier half of the population.
- Many people's livelihoods depend on aviation, **but** there is a lack of hard data on how important a new airport is in regenerating an area.

This report tries to unravel these contradictions and assess the true importance of aviation to the UK economy.

It's the Economy, Stupid has been published by HACAN ClearSkies. It has been compiled by John Stewart, based on research carried out by Gareth Harper. HACAN ClearSkies, which represents residents under the Heathrow flight path, can be contacted at PO Box 339, Twickenham, TW1 2XF, tel/fax 020 8876 0455, email: info@hacan.org.uk Both this report and a 4 page summary can be found on the HACAN ClearSkies website: www.hacan.org.uk

FOREIGN DIRECT INVESTMENT AND AIR TRANSPORT

The Department for Transport argues that expanding airport capacity would attract more overseas investment to the UK, thereby creating business and jobs in the UK that otherwise might not exist. But the Department does not acknowledge that air transport also attracts UK investment overseas, **creating business and jobs overseas rather than in the UK**. It is not clear why the Department gives an incomplete picture of the flow of investment in and out of the UK. Oxford Economic Forecasting, in a study funded largely by the UK air transport industry for the Department, acknowledged that international investment flies both ways:

“ ... the UK received an average \$22 billion of inward investment a year between 1993 and 1997 ... the UK's good air links have also encouraged UK firms to invest abroad by making it easier to manage overseas subsidiaries – between 1993 and 1997 UK investment overseas averaged \$39 billion.”

The Contribution of the Aviation Industry to the UK Economy (1999)

The table below shows that between 1997 and 2001 overseas investment in the UK averaged \$73.2 billion per year and UK investment overseas averaged \$135.8 billion per year: **an average annual deficit of \$63 billion, compared with an average annual deficit of \$17 billion between 1993 and 1997**. These figures indicate that the UK is investing more in jobs and businesses in other countries than other countries are investing in the UK, despite the alleged role of Heathrow (as the world's premier international airport) in attracting overseas investment to the UK.

Table 1: UK international investment 1997-2001: Net deficit: \$313 billion

	Overseas investment in UK	UK investment overseas
1997	\$33 billion	\$62 billion
1998	\$74 billion	\$123 billion
1999	\$88 billion	\$201 billion
2000	\$117 billion	\$254 billion
2001	\$54 billion	\$39 billion
Total	\$366 billion	\$679 billion

Source: United Nations Conference on Trade and Development (UNCTAD): *World Investment 2002: Transnational Corporations and Export Competitiveness* (September 2002).

The UK's track record on international investment suggests that **more business travel by air may result in even more UK funds being invested in jobs and business overseas**, particularly in developing economies where salaries and standards of living are lower than in the UK. Expanding airport capacity at Heathrow or elsewhere in the UK is therefore **no guarantee that the UK will in future attract more funds from overseas than it invests overseas**.

UK BALANCE OF PAYMENTS ON TOURISM BY AIR

- The UK balance of payments deficit on spending by visitors to and from the UK by air was £31 billion between 1998 and 2001.
- Department for Transport forecasts show that in 2020 UK residents will make 88 million visits overseas by air and that foreign residents will make 54 million visits to the UK by air.
- By 2030 UK residents visiting overseas by air will spend £46 billion, compared with £34 billion spending by overseas residents visiting the UK by air.
- The Treasury loses more than £1 billion VAT each year because UK residents spend more overseas than overseas residents spend in the UK

Table 2: Visitors to and from the UK by air: spending on consumer goods and services 1998-2001

	1998	1999	2000	2001
UK residents:				

1. visits overseas (millions)	34	38	41	43
2. spending overseas (£ billions)	£13.1	£15.3	£17.7	£18.7
Overseas residents:				
3. visits to UK (millions)	17	17	18	16
4. spending in UK (£ billions)	£8.6	£8.6	£9.1	£7.6
UK deficit:				
5. visitor spending (£ billions)	-£4.5	-£6.8	-£8.6	-£11.1
6. VATelement (£billions)	-£0.7	-£1.0	-£1.3	-£1.7

Notes: The figures in rows 1 and 3 are taken from *Overseas Travel and Tourism: Business Monitor MQ6: Data for Quarter 4, 2001* (Office for National Statistics, 2002). The figures in row 2 and 4 are derived from data from the same source on spending on visits to and from the UK by all modes of transport. The figures are for the number of visits (**i.e. outward and return journeys by the same visitor are not counted separately**). The figures consist of business and non-business air passengers to and from the UK, but do not include international interlining passengers (i.e. overseas passengers who arrive at a UK airport by air in order to catch a connecting flight to another overseas destination). The figures in row 5 are calculated from the figures in rows 2 and 4. The figures in row 6 represent the amount of VAT the Treasury loses because UK visitors spend more overseas than overseas visitors spend in the UK (see separate note: **Income Tax Pays for Air Transport Tax Exemptions**).

Table 3: Visitors to and from the UK by air: spending on consumer goods and services in 2020 and 2030

	2020 Forecast 1	2020 Forecast 2	2030 Forecast 1	2030 Forecast 2
UK residents:				
1. visits overseas (millions)	88	88	107	107
2. spending overseas (£ billions)	£37.5	£37.5	£45.7	£45.7
Overseas residents:				
3. visits to UK (millions)	54	49	67	62
4. spending in UK (£ billions)	£27.4	£24.9	£34	£31.5
UK deficit:				
5. visitor spending (£ billions)	- £10.1	- £12.7	- £11.7	- £14.2
6. VATelement (£billions)	- £1.5	- £1.9	- £1.7	- £2.1

Notes: The expenditure rate is derived from Table 2 above for 2000 (i.e. excluding the effects on air travel of foot-and-mouth disease and the terrorist attack on New York in 2001). Forecast 1 reflects the Department for Transport assumption that overseas visits to the UK will increase more quickly than UK visits overseas. Forecast 2 assumes that visits to the UK will grow at the same rate as visits overseas. **The historic trend shows expenditure by UK visitors overseas growing more rapidly than expenditure by overseas visitors in the UK.**

INCOME TAX PAYS FOR AIR TRANSPORT TAX EXEMPTION

- Tax exemptions for air transport were worth £7.5 billion in 2000. They will be worth £16.6 billion in 2020 and £21 billion in 2030, if passenger numbers increase as forecast.
- In 2002 a single person earning £25,000 (national average) will pay £557 income tax to meet the costs of air transport's tax exemptions, even if he or she does not fly.
- Air passenger duty (APD) was introduced in 1993 on the grounds that airlines did not pay fuel duty on VAT and were under-taxed compared with other sectors of the economy, according to the Budget Statement of 30th November 1993 by Kenneth Clarke, then Chancellor of the Exchequer - see also statements by Sir John Cope, the Paymaster General, on 1st December 1993 and 31st January 1994 during the debate on the Budget Statement. But the tax collected from the airlines in APD is only a fraction of the tax that would be collected if the airlines paid fuel duty and VAT. For example, as Table 1 shows in 200 the airlines paid £1 billion in APD but did not pay £8.5 billion in fuel duty and VAT, a net saving to airlines of £7.5 billion.

Table 4: Air Transport Tax Balance 2000

Tax paid	£bn	Tax exemptions	£bn
Air passenger duty	£1.0	Excise duty and VAT on aviation fuel	£5.8

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-108-154

Capacity deficit

Notes: The demand figures are taken from the unnumbered table on page 39 of the SERAS consultation document.

Table 9: Passenger capacity and demand at UK airports without tax exemptions in 2000 (millions)

	South East England	Rest of UK	Total UK
Capacity	154	193-239	347-393
Demand	53	29	82
Capacity surplus	+ 101	+164-210	+265-311

Notes: The Department for Transport (*Air Traffic Forecasts for the United Kingdom 2000*) estimates that each 1% increase in air ticket prices reduces demand by 1% as consumers decide to spend their surplus cash on other goods and services. UK airline costs were £13.5 billion in 2000, and would increase by £7.5 billion (55% increase) if air passenger duty were increased to the level of the tax exemptions. The extra costs are too large for the airlines to absorb and would be passed on to passengers. The figures in Table 9 show a 55% reduction in demand in Table 7. See also separate note: *Income Tax Pays for Air Transport Tax Exemptions*.

Table 10: Passenger capacity and demand at UK airports without tax exemptions in 2030 (millions)

	South East England	Rest of UK	Total UK
Capacity	154	193-239	347-393
Demand	135	90	225
Capacity surplus	+ 19	+103-149	+122-168

Notes: The figures in Table 10 show a 55% reduction in the demand forecast in Table 8, using the same basis as set out in the notes to Table 9.

PREVENTING POOR PEOPLE FROM FLYING?

The Government argues in the SERAS Consultation Document (published 23rd July 2002) that flying is “part of the ordinary lives of most people in the UK”; that a “large proportion” of British families take their summer holidays abroad; and that Britons will want to fly in future more “as their prosperity continues to increase”. But the available data indicates that leisure flying is - and will continue to be - undertaken by less than half of UK residents. Table 11 shows that last year 30 million UK residents did not fly; 14.4 million UK residents flew once; and 14.4 million UK residents flew more than once. According to the Office for National Statistics and the Civil Aviation Authority, UK residents made 51.4 million **business or leisure** visits by air in 2001 (42.9 million to an **overseas destination**; 8.5 million to a **UK destination**), indicating that the 14.4 million UK residents who flew more than once in 2001 made 37 million visits, or two and a half visits per person on average.

Table 11: UK residents business and leisure visits by air in 2001

	No visits	One visit	Two or more visits
UK residents (millions)	30	14.4	14.4
% of total	51%	24.5%	24.5%

Notes: Compiled from the Department for Transport report *Attitudes to flying*, which asked UK residents how often they flew on business or for leisure to a destination overseas or in the UK in 2001.

LEISURE TRAVEL DRIVES AIRPORT EXPANSION

- Improved productivity and increased inward investment in the UK - the wider economic benefits that the Government attributes to air transport - stem from international business travel.
- Business passengers accounted for less than 20% of international passengers at UK airports in 2001, and are forecast to account for less than 30% of international passengers in 2030.
- Present passenger capacity at UK airports (347-393 million) could accommodate 99 million business passengers forecast for 2030.

- The case for expanding UK airports rests mainly on forecast increased international leisure travel by air, as consumers cash in on airfares subsidised by the taxpayer and the business passenger.

Table 12: Passengers flying to and from the UK 1998-2001 (millions)

	1998	1999	2000	2001
Business passengers	23	24	26	23
Non-business passengers	81	86	93	95
All passengers	104	110	119	118
Business as % of all passengers	23%	22%	22%	19%

Notes: The figures are taken from *Overseas Travel and Tourism: Business Monitor MQ6: Data for Quarter 4, 2001* (Office for National Statistics, 2002). **The figures have been doubled in order to make easier comparisons with the Department for Transport's figures (which count separately the outward and return journeys of each visitor) upon which Table 2 below has been based.**

Table 13: Percentage of leisure travellers

	2020 Forecast 1	2020 Forecast 2	2030 Forecast 1	2030 Forecast 2
Business passengers	82	63	99	78
Non-business passengers	202	202	252	252
All passengers	284	265	351	330
Business as % of all passengers	29%	24%	28%	24%

Notes: The figures for 2020 (Forecast 1) are taken from *Air Traffic Forecasts for the United Kingdom 2000* (Department for Transport, Local Government and the Regions). The figures for 2030 (Forecast 1) are derived from the overall passenger forecast for 2030 in *The Future Development of Air Transport in the United Kingdom: South East Consultation Document* (Department for Transport). International interlining passengers (i.e. overseas passengers who arrive at a UK airport by air in order to catch a connecting flight to another overseas destination) and domestic passengers (i.e. passengers flying between two UK airports) are excluded from Tables 12 and 13 above. They are forecast to account for 150 million passengers at UK airports in 2030.

Forecasts 1 for 2020 and 2030 reflect the Department for Transport's assumption that business passengers will increase at a faster percentage rate between 1998 and 2020/2030 than leisure passengers. Forecasts 2 for 2020 and 2030 assume that that business and leisure passengers will grow at the same rate. The number of business passengers - and therefore the number of all passengers - is therefore less in Forecast 2 than in Forecast 1 in 2020 and 2030. **The historic trend shows leisure travel by air growing more rapidly than business travel by air.**

PASSENGERS AT UK AIRPORTS: 1998, 2020 AND 2030

The table below sets out the seven categories of passenger that the Department for Transport uses to monitor and forecast passenger demand at UK airports. The table shows that in total 160 million passengers used UK airports in 1998 (outward and return journeys counted separately); and that total passenger numbers are forecast to increase to 401 million in 2020 and 501 million in 2030.

The Department for Transport's forecasts assume that business air passengers will grow at a faster rate than leisure visitors, and that that foreign leisure visits to the UK will grow at a faster rate than UK leisure visits overseas. Both assumptions are contrary to the long-term trend and to the trend in 1998-2001, which show leisure passengers increasing at a faster rate than business passengers and UK leisure visits overseas growing at a faster rate than overseas visits to the UK (see separate notes: UK balance of payments on tourism by air and Leisure travel drives airport expansion).

Table 14: Passengers at UK airports

<i>Passenger categories</i>	<i>Passenger numbers (millions)</i>					
	1998	% of total	2020	% of total	2030	% of total
UK Leisure	50.1	31	114.1	28	140	28
Domestic	33.6	21	71.0	18	90	18

Foreign Leisure	23.6	15	67.2	17	85	17
Miscellaneous	21.2	13	45.7	11	55	11
Foreign Business	12.6	8	40.6	10	50	10
UK Business	10.9	7	34.0	8	40	8
Low Cost Airline	6.9	4	28.2	7	35	7
Total	160.0	100	401.0	100	501	100

Notes: The figures for 1998 and 2020 are taken from *Air Traffic Forecasts for the United Kingdom 2000* (Department for Transport, Local Government and the Regions, 2000). The figures represent the number of passengers at UK airports (i.e. the outward and return journeys of each passenger are counted separately). Column totals may not sum due to rounding.

The total figure for 2030 is taken from *The Future Development of Air Transport in the United Kingdom: South East Consultation Document* (Department for Transport, 2002). In the absence of published Departmental figures for each passenger category in 2030, it has been assumed that the number of passengers in each passenger category will be in the same proportions as the Department forecasts for 2020.

The figures for “UK Leisure” and “UK Business” represent the number of departures and returns by UK residents who fly overseas for leisure or business. The figures for “Foreign Leisure” and “Foreign Business” represent the number of arrivals and returns by overseas residents who fly to the UK for leisure or business.

The “domestic” figures represent the number of passengers flying between UK airports. The Department’s figures do not indicate how many domestic passengers are en route to or from an overseas airport via an intermediary UK airport, or how many passengers are business and leisure. According to Oxford Economic Forecasting, 60% are business and 40% are leisure.

The “miscellaneous” figures represent the number of: (a) diplomatic, armed forces and North Sea oil industry passengers (10 million in 1998, forecast to remain constant until 2020 and 2030); and (b) international interlining passengers who arrive at UK airports by air in order to catch a connecting flight to another overseas destination (11 million in 1998, and forecast to rise to 35 million in 2020 and to 45 million in 2030. See separate).

The “low cost airline” figures represent the number of passengers flying to and from the UK on new airlines such as Easy Jet and Go. The Department assumes that all passengers are UK residents. The number of business passengers on low cost airlines in 1998 was estimated to be 1.7 million, forecast to rise to 7 million in 2020. The number of non-business passengers in 1998 was estimated to be 5.2 million, forecast to rise to 21.1 million in 2020.

PRODUCTIVITY AND AIR TRAVEL

The number of UK passengers flying on business domestically and internationally is forecast to increase from 10.6 million in 1998 to 30.2 million in 2020, and to 36.3 million in 2030. The Department for Transport argues that more air travel by UK businessmen will improve national productivity. But the Department does not support this assertion with any evidence that the global pre-eminence of Heathrow Airport and other UK airports over the last fifty years has enabled the UK to outstrip productivity in “competing” economies.

Any productivity gain from more business flying has to be set against the cost of increased spending on air travel. The table below shows that **business spending on airfares would increase from £4.8 billion in 1998 to £14.9 billion in 2020 and to £17.6 billion in 2030** if the Department’s business passenger forecasts materialise. Airfares are only part of the business cost of flying: there are also hotel and restaurant bills, and the loss of productivity in travel time away from the workplace. If national productivity does not improve with extra business travel, the cost of extra business travel would filter through to price increases for consumer goods and services that rely on air transport, which is likely to reduce demand for those goods and services.

Table 15: UK spending on business travel by air (1998 prices)

	Number of visits	Average return fare	Expenditure
1998			
Domestic	4.4 million	£222	£10 billion
International	6.2 million	£621	£3.8 billion

Total	10.6 million		£48 billion
2020			
Domestic	9.7 million	£222	£2.2 billion
International	20.5 million	£621	£12.7 billion
Total	30.2 million		£14.9 billion
2030			
Domestic	12.3 million	£222	£2.7 billion
International	24 million	£621	£14.9 billion
Total	36.3 million		£17.6 billion

Notes: The data for 1998, including the average business return fares, are from Oxford Economic Forecasting, *The Contribution of the Aviation Industry to the UK Economy* (1999), p.44 and Annex C, Table C.2, p. 62.

The Department of Transport (*Air Passenger Forecasts for the United Kingdom 2020*) predicts that 20.5 million UK businessmen will fly internationally in 2020. The Department predicts an increase in domestic flying by business and non-business passengers from 8.4 million in 1998 to 18 million in 2020, but does not give a prediction for the number of UK businessmen flying domestically. Table 15 assumes that UK business passengers will account for the same percentage (54.5%) of all domestic passengers at UK airports in 2020 as identified by Oxford Economic Forecasting for 1998, without an adjustment for the Department's assumption that business visits will grow more quickly than non-business visits between 1998 and 2030.

The Department predicts that 500 million passengers will use UK airports in 2030 but does not give a prediction for the number of UK business passengers. Table 2 assumes that UK international business passengers will account for the same percentage (10%) of all passengers at UK airports in 2030 as the Department forecasts for 2020, without an adjustment for the Department's assumption that business visits will grow more quickly than non-business visits between 1998 and 2030. The number of UK business passengers on domestic flights in 2030 has been estimated by the same method for 2020.

AVIATION AND JOBS

It is clear that new or expanded airports will create jobs. Considerable doubt, however, has been cast on the claims that an expanded aviation industry will create at least another 36,000 jobs by 2015. That figure emerged from *The Contribution of Aviation to the UK Economy*, (Oxford Economic Forecasting) that was commissioned by the Department for Transport, but largely paid for by the aviation industry. The report, published in December 2000, forms the basis of the Government's Regional Air Studies.

The relationship between airport expansion and job creation is more complex than outlined in the Regional Air Studies:

- **The Regional Air Studies do not take full account of the tax concessions received by the aviation industry.** Nor do they fully factor in the social and environmental costs the aviation industry imposes on society. As a result they are not in a position to compare the cost to the taxpayer of jobs created by airport expansion with jobs created in other less-subsidised industries.

- **The Regional Air Studies are too broad-based to be meaningful.** They estimate the total number of jobs aviation expansion would create UK-wide and then simply divide them amongst the different regions and airports depending on the level of expansion that could take place in each region. They work on the basis that for every 1 million passengers using an airport each year 1,000 on-site jobs are created. This approach is different from the one government uses when assessing the regeneration effects of building roads or railways. The latter approach is the one recommended by the authoritative SACTRA Report on *Transport and the Economy* (1999). SACTRA (the Standing Advisory Committee on Trunk Road Assessment) argued the number of jobs created by new transport infrastructure could only be assessed on a site-by-site basis. This is because a whole host of local factors (such as the sort of labour available) are more important to job creation and regeneration than the provision of new transport infrastructure. The Regional Air Studies have sidelined the SACTRA Report - regarded as one of the most comprehensive of its kind ever published in Europe.

- **The Regional Air Studies fail to consider the extent jobs created by airport expansion reduce job opportunities in other sectors of the economy.** Money spent by the public on air transport is money not available

to be spent on something else. If the money were spent on goods and services other than air transport, the supply of those goods and services would generate jobs.

- **The Regional Air Studies double-count certain jobs.** As well as 'direct' and 'indirect' employment, the Regional Air Studies also assess the number of 'induced' jobs that would be created by airport expansion.. This is the employment generated by employees in the air transport industry spending their wages. But induced jobs in one sector are also direct jobs in another, which leads to double counting. If all the induced jobs from each sector were added in, the total employment would be higher than the UK population, let alone its workforce!

CONCLUSIONS AND RECOMMENDATIONS

❶ **There is little evidence that a significant expansion of aviation will bring any overall benefit to the UK economy.** In fact it could be detrimental to the economy as it is likely to result in more money being invested overseas and a still greater deficit in aviation tourism. But it is equally clear that some businesses depend on good air links. Government's role should be to assess those and ensure they are provided for.

❷ **The forecast increase in demand over the next 30 years is, at best, irrelevant to most business sectors as it largely consists of leisure travellers taking weekend breaks abroad.** The fact that it is clearly relevant to the aviation industry - and some sectors of the travel industry - has clouded the Department's view. It fails to spell out that the demand is being artificially stimulated by the tax concessions the aviation industry enjoys. It fails to spell out that, if these tax concessions were removed, there would be no need for any increase in airport capacity.

❸ **What is required is an independent study** that looks at what sort of air links are best for business; at the ways the tax concessions enjoyed by the industry are distorting the market; at the relationship between airport development, regeneration and jobs; and assesses the true contribution of aviation to the economy.

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