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Title: The Role of Infrastructure Service Providers in a Liberalized Environment

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INFORMATION PAPER

SUMMARY

This paper provides information on the role of infrastructure service providers in a liberalized environment based on the readiness for airport facility, managing customer's needs and satisfaction and connectivity increase by cooperating airlines, who are main drivers of hub airport.

1. Introduction

Environment around the air transport industry is rapidly changing especially toward liberalization. Liberalization of all industrial areas are increasing customer's needs and satisfaction and making them diversified. The industry leaders like airports, airlines and freighters are continually trying to keep up with the changes in order to survive.

Liberalization of Air Transport has a positive influence on Airport. The new type of airlines like Low Cost Carriers (LCCs) will appear and create new type of service, which is mainly cost effective, to attract new passengers who has never taken flight. In Europe, LCCs has shown good examples creating new routes and customers. Apparently it has increased the number of flights and revenue to the airport.

As an infrastructure service provider, airport considers Liberalization of Air Transport beneficial and shall not be just an infrastructure manager of old times, but aggressive business developer in order to be primary hub airport in the region or to survive.

Regarding the airport's role as a hub airport, the environmental changes and things to develop will be discussed followed preliminary conclusion.

2. Environmental Change of Air Transport around Korea

2-1. Political and Economical Change

Korean Government is trying to increase the number of countries entering into Free Trade Agreement (FTA) in order to keep up with global trade demand. Korea has agreed with Chile and Singapore on FTA and also working on with Japan. The government's policy on expansion of FTA will definitely have influence on air transport in Korea.

The countries in Northeast Asia have shown better economical increase rate than the other region. China 7.7%, Hongkong 3.3%, Taiwan 3.2%, Japan 3.1% and Korea has increased by 4.7% as of 2004. China is growing rapidly which has tremendous influences on neighboring countries including Korea.

Most of all the new air service agreement of China-U.S. signed in July 2004 has a meaning of drastic change in the future of air transport industry in the Northeast Asian region. According to the new agreement, the flight capacity will be increased five fold to 249 flights per week by 2010 from 54 current. This will pose a threat to Incheon in the respect of possible and clear route change from U.S-Incheon-China to U.S-China directly.

2-2. Social Change

The fast-developed "aged society" of Korea has already passed over the UN's average level. Approximately 47% of the aged want to have outdoor life. It will make an effect on the air transportation. The introduction of five-day workweek and the "Hallyu", the "Korean Wave" are very important change, which will have very important effect on air transport industry.

2-3. Environment Change of Transportation

Reorganization of the air transport industry in Korea is required due to development of new and better highways and High-speed Train (KTX).

The advent of Low Cost Carriers (LCC) is asking to change and restructure the airline industry. LCCs with low fare, point-to-point and short time turn-around strategy are actively operating in North America, Europe, Australia and Southeast Asia. LCCs are taking about 20% of total market share. 60% of LCC users are newly created by LCCs and 40% are shifted from the legacy carriers. LCCs' are not active in Northeast Asia compared to the other region, due to the slow liberalization policy. However the liberalization issue is under discussion among the countries in the region and it will not take long to agree on open skies.

3. The Role of Airport in a Liberalized Environment

As mentioned above, the air transport industry is being affected by the changes and experiencing changes itself as well. Airport shall analyze the market and keep up with market needs in order to be a Hub airport or to survive. Airport needs react aggressively to the liberalized airline market with competitive business strategy. It has to be ready with updated airport facility, customer's needs and satisfaction, and most of all airport

connectivity management by making good relationship with airlines, government and related industry cooperators.

3-1. Airport Facilities

As an infrastructure service provider, airport needs to develop and maintain the facility in order to attract the globally networking airlines as well as passengers. Several key factors will be discussed on readiness of an airport facility.

3-1-1. Peak-hour Capacity

Peak-hour capacity is one of factor for an airport wishing to be Hub to develop the optimum level of. In order to increase peak-hour capacity, all the airports around the world are trying to construct new facility or renew them. London-Heathrow developed the 5th runways to prepare for its enough capacity for peak hours making it distinguished from the others in the region. They are even considering construction of 6th and 7th runway to keep the attractive hub airport in the region even for the future. The airports in Northeast Asia such as Hong kong, Kansai, Shanghai, Beijing are also expanding or has expanded capacity to be competitive.

Incheon is also constructing the 2nd phase project, which includes the 3rd runway, new concourse, 64 more aircraft stands and more cargo terminals. With the 2nd phase construction, the annual flight capacity will increase 240,000 to 410,000. Passengers will be to 44million from 30million and the cargo capacity will be from 2.7million tons to 4.5million tons. The peak-hour capacity of check-in-counters will be able to process 9,000 passengers per hour from 6,000 currently.

Terminal design, which is also under renovation, will handle 44million passengers from 30million passenger now. BHS of 32,000 bags per hour capacity, 270 check-in-counters, commercial facilities with more than 200 shops including duty-free shops, restaurants, transit hotels and convenience stores will be all ready for the customers.

3-1-2. Logistics

Logistics has a great portion in Northeast Asian airports. Incheon was ranked the 3rd in the world for cargo traffic with 1.8million tons according to ACI statistics in 2003. In 2004, 2.1million tons of cargo was processed, which is 16% increased from the previous year.

Development of the Free Trade Zone (FTZ), a business area exempt from duties, is currently under way as a part of the plan to strengthen Incheon's logistics capability. The 99.2-hectare site has been completely prepared for construction. With the construction of support buildings in 2005, the area will be in full operation by 2006. The FTZ will eventually be expanded to about 200 hectares, and the current 105-hectare cargo terminal area has been designated a part of the FTZ.

The creation of the Incheon Free Economic Zone (IFEZ) will raise the already high status of Incheon as Northeast Asia's logistical hub. The IFEZ is actually a part of the Korean government's grand plan to transform Korea into the economic center of Northeast Asia, a strategy that places Incheon at the center and forefront. It specializes in airfreight, leisure activities and tourism.

Free Trade Zone and the Incheon Free Economic Zone will cooperate in a mutually beneficial relationship that will advance Incheon International Airport to the leading position in the world logistics market.

3-1-3. Airport Access

Easy access to the airport is one of the strength to be a hub. Railway linking the airport with the Seoul subway will be completed in early 2007 and the High-speed Rail network in 2008.

A second bridge as well as the current bridge will be completed in 2008, providing easier access from the southern parts of the Seoul Metropolitan Area.

3-1-4. Area Developments

Futuristic airport is not a just another place to catch a flight. It shall be a city that satisfies with the needs of all travelers, whether it be for business, shopping, pleasure, or otherwise.

A case in point is the International Business Center (IBC) of Incheon, a sprawling 16.5-hectare zone that boasts two five-star hotels and four office complexes, with a shopping mall to be completed in 2005. The area will eventually encompass 33-hectares and will provide a convenient and refreshing environment for business. 9-hole golf course, 72-hole public golf practice area will allow businessmen and women to hone their golf skills.

The area around the Incheon Airport is being transformed into a massive complex with all the aspects of a regular city: housing, lodging, commercial areas, recreation, and city administration.

3-1-5. Strategies to Attract LCCs

LCCs ask airports to provide more simplified airport system for cost-effective. VIP lounges, loading bridges, complicated BHS are not necessary for them. Airports like Singapore Changi, Malaysia Kuala Lumpur are constructing or plan to construct LCCs only terminal in order to satisfy LCCs needs.

Incheon is also discussing the need of new terminal or incentives for airport user charge to attract LCCs. It is not LCCs are not active in Northeast Asia rather than the other region but there will be a big change in the near future. Incheon has to be ready for the foreseeable change in the air transport industry.

3-2. User's Needs and Satisfaction

Airport needs to increase level of service for various airport users such as passengers, visitors to the airport, cargo transporters in order to satisfy them and go to higher level of airport. For passengers, airport should satisfy their needs for airport access, boarding, waiting, connect, subordinate activities. Visitors must feel comfortable and convenient for airport access and sightseeing. Freighters care for access, logistics, and distribution.

Incheon is operating customer center, and listen and try to help customer's complaints, questions and suggestions in a real time base. Incheon is discussing the one-day settlement policy of customer complaints from 3-day policy current.

Incheon is also monitoring concession operators in regular base and estimates their business operations in a point of customer's view. If it does harm airport image or customer's satisfaction, the results will be reflected to the next contract by giving them penalty points.

3-3. User Charge Policy

Airport is not just infrastructure to service to the public for nothing. It is transforming into a revenue-oriented enterprise. In order to be a successful enterprise, it has to follow the market principle. Airline industry is rapidly changing due to increase in competition, and advent of new type airlines. Airports are also under a severe competition due to supply surplus especially in the region. Most countries around the region are struggling to make their airports a primary hub. Of course the competition causes competitive market price for customers.

Thus, airport needs to plug with user charges to make it attractive for airlines to come. Incentives to the customers, and price differentiation according to the customer's accomplishments shall be considered for airport to make attractive, which will be beneficial for those who have good business record in the airport.

Incheon is giving incentives of 50% of landing fee to the airline that is newly starting service at Incheon or newly developing an air route to/from Incheon. And Incheon is attracting late night flight by giving special discount in order to fertilize and activate 24 hour operational strength.

3-4. Networking

Connectivity in the airport is the vital issue for airlines to choose a hub airport. Airlines are networking on regional basis to keep up with industry needs. Global alliances like Skyteam, Star Alliance and One-world are representative airline networking examples. The main drivers of hub airport, i.e. the home-based national carriers, are assumed to be replaced by a global airline network. And this global network will make a choice of the most attractive hubs per continent. Therefore Incheon Airport will try to make an attractive and competitive hub, so the main drivers can choose Incheon as the main hub in the region.

Incheon has connectivity strength with two mega global airlines alliances based on two national carriers. Especially the routes to China with 26 cities, 731 flights per week and Japan with 23 cities, 624 flights per week have competitiveness compared to the other airports in the region. However it is severely centralized to just two peak hours and negatively affects general connectivity in Incheon. It is most important issue for Incheon to manage their efficiency for airport development and eventually increase the number of peak hours.

Airport can give benefits and penalty to the airlines by appropriate management of check in counters (CIC). The location and time can be economically negotiable with airlines according to the allocation of CIC. Airport can give benefits to the airline that use at non-peak time or decides to use somewhat slow location.

SLOT can be also economically negotiable with airlines. SLOT coordination rights seem to be a shifting form airline-oriented to airport operator now. And it does not seem to be easy but it shall be discussed and managed by airport operator eventually.

3-5. Other Issues to Consider

Other issues for airport to make it attractive can be potential catchment area, location in the core region, intercontinental location.

Incheon is luckily located in the core of Northeast Asia. It covers more than 42 cities, which have over 100 million populations. The Korean peninsula has a better condition than any other region by bridging America and China, Australia and China, Europe and Australia and etc.

4. Conclusions

Political and economical changes as well as air transport change around the world are influencing air transport industry in a way or another. Especially liberalization of air transport is spurring airport to be an aggressive business operator rather than infrastructure manager.

Thus as an infrastructure service provider, airport needs to develop airport facility more aggressively, manage customer's needs and satisfaction, and try to increase airport connectivity to network with airlines in order to be a primary hub in the region. The airports should prepare and strengthen themselves in anticipation of the changes in the near future.

However it is not easy for airport to be a business developer or aggressive manager within the current regulations or liberalization status. The liberalization of Air Transport in Northeast Asia of China, Japan and Korea has to be made first in order to make Incheon a hub airport. - End -