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Directorate-General for Competition  
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The Malta Hotels and Restaurants Association (MHRA) would like to put forward to the European Commission its point of view on 'Procedures Relating to the Implementation of Competition Policy, State Aid – Malta, State aid SA.33015 (12/c) – Air Malta plc' published on 21<sup>st</sup> February 2012.

## **1.0 Introduction**

The Malta Hotels & Restaurants Association was formed in 1958 and is the leading organisation representing the interests of hotels and restaurants across the Maltese islands worth an estimated 2 billion euro.

As the major association in the tourism sector, the MHRA represents not only the interests of its members, but also speaks for the local tourism industry in general. The MHRA sits on several important national policy making bodies, including the Malta Tourism Authority Board and the Malta Council for Economic and Social Development. The Association's endeavours and achievements over the years earned it recognition as one of the main constituted bodies in Malta. Its contribution towards the improvement of the industry remains continuous and valuable. The vast majority of hotels and restaurants in the Maltese Islands, which are its members, confirm its place of importance amongst Malta's employers' unions.

## 2.0 Impact of Tourism on the Local Economy

As acknowledged in the Commission's decision, tourism is one of the leading pillars of Malta's economy. In fact, (as per *Tourism Policy document 2012-2016*, just published) tourism accounts directly for: 10% of our GNP; 14% of government income; 10% of employment; and to 6% on imports and outflows. When other indirect impacts are taken into account, these figures increase to 29% of GNP, 33% of government income, 29% of employment and 16% of imports and outflows. These figures provide an indication of how important tourism expenditure is for the Maltese economy. The tourism income flows stimulate various other economic activity and it is therefore crucial that we maintain a steady, all-year round inflow of tourism. Our diverse tourism product offering has led to tourism expenditure permeating throughout the economy and society. As an industry it employs skilled and unskilled workers, it generates income to big investors on one end, to small outlets and individuals on the other end. Various service providers, retailers and shop owners throughout the islands depend on tourism to earn their keep. The multiplier effect of tourism on the economy of Malta is second to none.

## 3.0 Tourism Industry Reliance on Air Malta

There is a strong correlation between the growth of Air Malta and the growth of the tourism industry. Since its inception Air Malta was fundamental in investing and opening up new market opportunities for our industry. Statistics demonstrate that the airline played a major role in this success. The MHRA stresses that Air Malta must retain this pivotal role in the tourism industry, with a minimum 50% share of the tourism market.

This is important because, as an island destination, Malta is dependent on air connectivity, as can be seen by the table below.

| <b>Total Departures by Air and by Sea</b> |             |             |             |             |             |             |
|---|-------------|-------------|-------------|-------------|-------------|-------------|
|   | <b>2006</b> | <b>2007</b> | <b>2008</b> | <b>2009</b> | <b>2010</b> | <b>2011</b> |
| Air                                       | 1,104,273   | 1,223,693   | 1,270,082   | 1,166,417   | 1,309,783   | 1,375,681   |
| Sea                                       | 19,965      | 19,828      | 20,774      | 16,072      | 26,558      | 35,319      |
| Totals                                    | 1,124,238   | 1,243,521   | 1,290,856   | 1,182,489   | 1,336,341   | 1,411,000   |

Sources: National Statistics Office and Malta Tourism Authority

Malta's geographic location, as an island state at the Southern periphery of Europe makes it highly dependent on reliable air transport as much as any central European country is dependent on rail and road connections. In addition to its cross border travel disadvantage, Malta also loses out on domestic tourism, which is virtually non-existent, unlike most other member states. These two factors make Malta more vulnerable to airline accessibility, and having a national airline like Air Malta is even more critical, as it can adapt to the island's needs in a more timely and appropriate manner.

The inbound-tourism market, although important for Malta, is too small in absolute terms to attract other major airlines. Apart from Air Malta, which makes up to 50% of all seat capacity, the major full service airlines that operate on a daily basis are Lufthansa, Alitalia and Emirates. There is a significant presence of low cost airline operators (LCCs) however, these have been attracted to operate from under-served routes through costly development schemes put in place by the Malta Tourism Authority. These airlines are highly beneficial to Malta's tourism industry, especially because of their strong distribution channels, which are vital to market with individual travellers. However there are a number of reasons why they can never completely substitute full service airlines, especially a national airline. The risk of increasing dependency on LCC's is also another area of concern. LCC's tend to enter and exit markets, even from one season to the next, at short notice, whereas Air Malta has traditionally provided reliable and consistent air transport to and from Malta over many years.

By its very existence, Air Malta's name, presence and activities contributes heavily to marketing the islands of Malta as a tourist destination. Its very presence would be difficult, in fact impossible to replicate through other marketing efforts.

There are other considerations which are not directly related to Tourism and the hotel industry. A case in point is the social aspect the airline is rendering when it carries stretcher cases and sick people travelling to major cities in Europe for treatment. No other airline, full service or otherwise, offer these service to the Maltese community.

#### **4.0 Tour Operator Business & Air Malta**

Another factor which makes Air Malta crucially important to the industry, is its support to tour operator business to Malta, which despite its decline over recent years, remains a hugely important source market to our islands. In fact a number of our hotels have been specifically developed to cater for this market segment, and these are entirely dependent on this source market. Tour operator traffic also contributes handsomely to a better seasonability spread, which makes it even more important for local tourism. Air

Malta is a key player in this regard, the following table shows how important tour operator business is to Maltese tourism. Substituting this business with other airlines has, over the years, proven to be extremely difficult. Tour operators have limited access to LCCs' seat inventory, as LCC's generally discourage the sale of their seats to tour operators, which makes the former, more amenable to working with full service airlines, like Air Malta.

|                           | 2006    | 2007    | 2008    | 2009    | 2010    |
|---------------------------|---------|---------|---------|---------|---------|
| Individual & other Travel | 373,388 | 560,464 | 695,877 | 652,612 | 744,656 |
| Tour Operator             | 750,848 | 683,046 | 594,979 | 529,878 | 591,735 |

*Source: National Statistics Office*

## **5.0 MICE Business & Air Malta**

Air Malta is also particularly important for MICE business (Meetings, Incentives, Conferences and Events). The conference and incentives business in Malta has grown as has the investment by local stakeholders in this sector. Malta has an array of facilities that makes it capable of holding anything from small meetings to large conferences with over five thousand delegates. Malta has over the years been successful to attract a number of large conferences leaving a very positive effect. MICE tourists have the highest daily average spending capacity making this sector a very competitive one. Connectivity remains key in this sector and Air Malta is a main source to this market. In fact local tourism stakeholders work very closely with Air Malta to address the needs of this segment. Malta hotels, especially the 5-star and 4-star ones rely heavily on group business especially conferences and incentives in the shoulder and winter periods. By their very nature such businesses can only be marketed through, and travel on, full service airlines, as the LCCs focus on the individual traveller. This business requires network carriers like Air Malta that can offer daily services to major European capitals. Any measures on Air Malta that risk diminishing this market segment which is crucial particularly during the low season, would be highly detrimental to the viability of Malta's hotels.

## **6.0 Air Malta & Seat Capacity - Critical to Tourism's Sustainability**

The MHRA has always maintained that the two most important and challenging factors affecting the industry's sustainability and economic growth are accessibility and seat capacity. Measures that can translate into a drop in seat capacity can have devastating affects, not only on tourism, but indeed on the economy.

The MHRA has recently conducted an in depth study by economist Clyde Caruana (Sept 2011) which focused on airline seats and tourist arrivals; and the economic affects of a drop in seats to Malta. The

findings of this report follow the findings of an earlier report commissioned by the MHRA which was conducted by Deloitte and Touché (September 2009). Both reports highlight the robust correlation between the number of passenger seats and the number of tourist arrivals to Malta.

| <b>Airline traffic 2006-2010</b> |             |             |             |             |             |
|----------------------------------|-------------|-------------|-------------|-------------|-------------|
|                                  | <b>2006</b> | <b>2007</b> | <b>2008</b> | <b>2009</b> | <b>2010</b> |
| Pax                              | 2,692,019   | 2,970,830   | 3,109,868   | 2,918,664   | 3,293,524   |
| Seats                            | 3,713,819   | 4,244,443   | 4,313,658   | 4,208,822   | 4,653,592   |

*Source: Malta International Airport*

Aggregate results emanating from the Caruana report indicate a strong relationship between the number of available seats and the number of tourist arrivals for each change in seat capacity, in the winter, shoulder and summer months respectively.

The results continue to support the industry concerns in the event of a drop in seat capacity. For instance, if Air Malta were to revise downwards the number of winter passenger seats for the UK by 1,000, the number of British passengers visiting Malta would drop by 750. However, if the revised passenger seats (1,000) for the UK were held during shoulder months, the number of passengers would drop by a higher extent of 820. Moreover, the number of passengers during the summer months would drop by 860 in the eventuality of a downward revision in the number of passenger seats of 1,000 during this period. Indeed, this implies that if Air Malta were, say, to implement the reduced passenger seats strategy either on the UK or Germany, this would maximize the negative impact on tourists exports in Malta.

This economic study using 2010 data, also quantified the estimated loss in Total Value Added (direct and indirect) and Government Revenue following a reduction in the number of passenger seats by an extent of 1,000. These estimates are based on the total value added per night (amounting to EUR 127.59) and the tax per EUR 1 (amounting to EUR 0.15) of total value added. The following tables represent estimated losses per 1,000 passengers.

|                        | Loss in TVA for the Economy (EUR) |                |                |
|------------------------|-----------------------------------|----------------|----------------|
|                        | Winter                            | Shoulder       | Summer         |
| Russia                 | 1,045,008                         | 1,078,718      | 1,247,268      |
| United Kingdom         | 879,428                           | 961,508        | 1,008,411      |
| Germany                | 741,212                           | 818,652        | 885,029        |
| Netherlands            | 721,589                           | 753,424        | 838,317        |
| Scandinavia            | 720,120                           | 808,901        | 828,631        |
| Spain                  | 617,444                           | 606,799        | 787,774        |
| France                 | 651,595                           | 641,722        | 730,576        |
| Italy                  | 418,591                           | 463,440        | 538,189        |
| <b>Total (average)</b> | <b>671,088</b>                    | <b>745,653</b> | <b>820,219</b> |

|                        | TAX Revenue Losses due to drop of 1,000 passenger seats |                |                |
|------------------------|---|----------------|----------------|
|                        | Winter  | Shoulder       | Summer         |
| Russia                 | 156,751   | 161,808        | 187,090        |
| United Kingdom         | 131,914   | 144,226        | 151,262        |
| Germany                | 111,182   | 122,798        | 132,754        |
| Netherlands            | 108,238   | 113,014        | 125,748        |
| Scandinavia            | 108,018   | 121,335        | 124,295        |
| Spain                  | 92,617  | 91,020         | 118,166        |
| France                 | 97,739  | 96,258         | 109,586        |
| Italy                  | 62,789  | 69,516         | 80,728         |
| <b>Total (average)</b> | <b>100,663</b>  | <b>111,848</b> | <b>123,033</b> |

## 7.0 Impact of drop in seat capacity on Hotels' GOP

Our study also shows that hotels are most vulnerable to seat volatility. A drop in seat capacity would influence profitability levels differently across the seasons.

In recent years, overall profitability for the Hotels industry has been mainly driven by improvements in the number of nights spent by an extent of 59 per cent. Out of the total profitability, the higher charges for room rates contributed by an extent of 41 per cent. It's worth noting that the local hotel and restaurant industry gross operating profit expressed in terms of output is considered to be low compared to that of competing EU Member States, which makes it more susceptible to any fluctuation in tourist arrivals, even if small.

2009 proved to be a very bleak year for the tourism sector of Malta. In particular hotels underwent substantial setbacks to their revenues as the global recession adversely affected tourist demand for Malta,

whilst the surge in utility prices contributed to the rising operating costs of hotels. The double plunge incurred by hoteliers led to lower profits and consequently to a drop in employment.

As we have demonstrated to Government on several occasions, the hotels and restaurant sector had to a large extent, absorbed the rise in costs since the recession, as can be corroborated by the declining profits shown in official statistics. Profits in 2011 are still marginally below the levels registered in 2008, when costs were significantly lower. Despite the improvement in arrivals since, profitability remains a major concern. If tourist arrivals drop below 2011 levels, this will have devastating affects worse than those registered in 2009, given the substantial increases in costs since. Only through further growth can Malta realistically expect to push rates up and counter the pressures caused by a steadily declining average length of stay.

## **8.0 The Accommodation sector & Air Malta**

The accommodation sector in the Maltese Islands is made up of around forty five thousand beds spread over different category hotels and similar tourist accommodation establishments. Despite the success registered over recent years, the sustainability of the industry mainly hinges on maintaining the numbers of tourist arrivals to Malta.

Demand for Malta as a holiday destination, is measured by the number of tourist arrivals, which has increased by 235,259 over a span of eight years (2002-2010). This has been painstakingly achieved though various initiatives, but mainly through the increase of seat capacity and introduction of new routes. In order that Malta consolidates this effort we need to ensure that the number of seats to Malta are maintained. The manifestation of promising targets can only be assured through the preservation of seats and routes to Malta and possibly through further increases. Anything less will have a very negative effect on the economy, and indeed on the local investors and employment across the country.

## **9.0 Air Malta - Tourism and economy**

The MHRA sees growth in tourist numbers as a very positive solution for the Maltese Government to raise tax revenue and continue lowering the national deficit. The MHRA therefore underlines that tourism is considered as one of the six pillars for economic growth. Recognising the importance of tourism to the nation, both the public and private sectors have invested heavily in tourism over time, and this investment will only bear its full fruit if Air Malta's continued existence is guaranteed.

## 10.0 Conclusion

The above arguments demonstrate the high dependence the Maltese economy has on tourism. Air Malta remains a key to the sustainability of the industry and the MHRA advocates against the European Commission being the direct cause of further risks or shocks being applied to the fragile tourism industry at a stage when the Maltese economy is on the path to recovery after the effects of the recent economic recession. The recession has put immense pressure on the level of profitability of hotels and other catering establishments, which would only be further exacerbated by any negative Commission decision on the Air Malta case.

In our view the continued survival of Air Malta does not pose any risks to competition in the European air transport market. This should be clear from the relatively minute size of the airline when compared to its European peers. Furthermore, the MHRA strongly believes that the tourism industry can be part of a solution to restore pre-recession economic growth rates, so fundamental for the continued well-being of the Maltese people and islands given the lack of natural resources on the island. It is empirically proven that the tourism industry benefits the economy with the highest multiplier which in turn increases gross value added by substantial amounts and consequently any imposed measures that risk a drop in numbers can have very drastic results.

In the end what makes the tourism industry predominant amongst other sectors are the thousands of jobs directly and indirectly associated with this sector. Although there are other sectors that contribute heftily to the state coffers, none of them are directly or indirectly liable to the livelihood of so many families. Besides, tourism is one of the few remaining sectors in Malta that offers employment opportunities for those unskilled labourers. Prospective slowdown within the tourism industry would automatically give rise to structural unemployment.

As we have underlined, the correlation between tourist arrivals and passenger seats is indisputable. Consequently it remains predominantly important to work towards increasing tourist arrivals. Indeed, it must be ensured that the restructuring of Air Malta and the prospective establishment of new routes are set to continue to sustain tourism industry as a minimum to those registered in 2011 levels, and aim for further growth to make up for the drop in the average length of stay. We believe that Air Malta is too small a player in the air transport market in Europe to impact in a real way the competitive aspect of this sector.

MHRA strongly recommends to the Commission to take these factors into serious consideration in its deliberations, as they impact heavily on the economic and social fabric of Malta and on the general well-being and standard of living of the Maltese people.

**Tony Zahra,**  
**President,**  
**Malta Hotels & Restaurants Association**

*Sources: National Statistics Office*

*Malta International Airport*

*Malta Tourism Authority*

*Draft Tourism Policy for the Maltese Islands (2012-2016)*

*Malta Hotels & Restaurants Economic report- Deloitte & Touche -2009*

*Malta Hotels & Restaurants Economic report- Clyde Caruana -2011*