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for better DECISIONS



Transition to Normality

COVID may no longer be the biggest concern

T2RL's Outlook

April 2022



INTRODUCTION

This is the seventh edition of T2RL's analysis of the market recovery for the airline industry during and after the COVID-19 pandemic. T2RL will update this document on a periodic basis as new information and developments become apparent.

T2RL's View

As the Covid-19 pandemic enters its third year it is clear that fatigue is setting in. Despite case rates that are as high as any seen so far, many national governments are relaxing restrictions both domestically and with regard to international travel. This is justified by the assertion that Covid-19 is becoming a manageable, endemic infection and that the economic impact of restrictions cannot be sustained any longer. To the extent that the ratio of hospitalisations and deaths to reported cases is much smaller now than in the initial waves there may be some justification for that assertion. However it is important to note that this reduction in severe impacts is mainly due to large-scale vaccination programs that have been rolled out in most developed countries. The situation in poorer regions is not so positive.

Omicron remains the dominant virus variant throughout the world although we are beginning to see reports of one or more sub-variants, such as BA.2, which have been reported in China and other places.¹ All the indications so far are that Omicron and its sub-variants are producing less severe illness than previous strains. This may be due to a fundamental difference in the virus or to the increasing proportion of the population that is vaccinated. In all probability both factors are in play. In the absence of further new strains that increase the severity of the infection most governments are adopting the view that Covid-19 is becoming part of the environment to be managed rather than a unique hazard to be fought as an existential crisis.

Most of the travel restrictions that were imposed in response to the emergence of Omicron have now been lifted. Many experts doubted whether they were ever justified but they were a reminder that, in liberal democracies at least, governments feel obliged to be seen to take action, citing "the precautionary principle". In this case it is almost certain that the Omicron variant was already widely distributed before the travel restrictions were put in place and that those restrictions were ineffective in slowing its spread.

¹ <https://www.cnbc.com/2022/03/24/omicron-stealth-variant-ba2-is-spreading-rapidly-in-china.html>
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Whether it was the additional restrictions imposed because of Omicron or simply a reduction in demand due to increased case rates it is clear that the pace of recovery slowed at the end of 2021 and into the first quarter of the current year. T2RL's projected passenger numbers for the world's top 5 airlines in 1Q22 show a fall of around 60 million compared with the final quarter of 2021. This is disappointing after the strong recovery through the first half of last year was followed by a levelling out at around 65% of 2019 numbers in the fourth quarter.

North America continues to lead the way back to normality. Passenger boardings there more than doubled between 2020 and 2021 and although 1Q22 projections reflect the global setback, traffic should still be around 76% of the equivalent period in 2019. By contrast European traffic is currently running at around 56% of 2019 levels. The Chinese market has been the most volatile with early strong recovery followed by declines as new virus variants added their impact to economic downturn. Current projections show Chinese airlines boarding around 50% of their 1Q19 numbers in the most recent quarter. Asia Pacific outside China remains the most severely affected of all regions with only 38% of 2019's numbers expected in the first quarter of 2022.

T2RL subscribers can follow the development of traffic recovery at our dedicated COVID-19 pages. <https://www.t2rl.net/airline/covid19traffic>

The further outlook for the airline industry and its technology providers remains highly uncertain. Change and volatility will be the key factors in 2022 and beyond. The airline industry has demonstrated many times that it is able to adapt to a changed environment but widespread inconsistency between different regulatory regimes will be very challenging. There will be more variants of the virus and more responses from governments. Many now want to lift restrictions but others like China continue to impose lockdowns. IATA has been obliged to shift its AGM from Shanghai to Doha due to an upturn in Covid cases and consequent responses by China². Variations in border controls, vaccination certification and quarantine requirements will probably be with us for at least several more years.

National Market Responses

At the start of the pandemic T2RL defined four categories of national approaches to its management. As time has passed the distinctions between these four approaches have

² <https://travelweekly.co.uk/news/air/china-covid-travel-curbs-force-iata-to-switch-agm-to-qatar>
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become increasingly blurred and to a large extent they are only of historical interest. At the time of writing it appears that more or less all governments are adopting similar – though crucially not identical – approaches, with the main distinction now being the availability and acceptance of vaccines.

Vaccination Uptake

Since the first vaccines were deployed at the end of 2020 they have been rolled out around the world. In developed countries it is generally true to say that vaccination is available to everyone who is prepared to accept it. Most of the available vaccines require two doses to deliver protection but many countries are now providing a third, booster, dose. Some have even begun to recommend a fourth dose to those at particular risk.

Take-up rates have varied significantly with resistance to vaccination becoming a political issue in some countries, most notably the USA. As reported by the Financial Times³ 36 countries have delivered more than two vaccine doses per head of population with the leading position taken by Cuba where 87.5% of the population is fully vaccinated and 55% have received a booster. In contrast to that number, three countries in sub-Saharan Africa have vaccinated fewer than 1% of their population while many still have single-digit totals. Among rich countries the USA is an outlier with only two thirds of the population fully vaccinated despite the vaccine being free of charge in a country with otherwise high health care costs.

Particularly since the establishment of Omicron as the dominant strain it has become clear that the main value of vaccination has been to prevent Covid-19 infections developing into serious illness or death. Case rates have continued at a high level while rates of hospitalisation and death have been much lower than in earlier waves of the pandemic. Despite this even mild Covid cases are causing economic disruption as absence rates in essential industries climb to unprecedented levels.

Border Controls

At the beginning of the pandemic some countries adopted a very hard line on border controls and quarantine. In the case of nations like Australia and New Zealand that are separated by oceans from even their nearest neighbours this strategy was viable as a

³ All vaccination data is from The Financial Times Covid Tracker pages
<https://ig.ft.com/coronavirus-vaccine-tracker>
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means of buying time until vaccines were available but it came with large economic and social costs. By mid-2021 it was clear that it was not a workable long-term solution and countries that had implemented it began to loosen their restrictions.

In other countries where neighbours were closer, and especially where land borders existed, the controls that were put in place served to assist national health organisations to track and manage the flow of possibly infected travellers. In the early stages the controls were largely based on testing and a variety of regimes were adopted for pre-travel tests, post-travel tests and in some cases both. As vaccines became widely available testing regimes were relaxed for vaccinated travellers.

At the beginning of 2022 there is a mixed approach of documentation on vaccination and testing and this is likely to remain in place for some time. The biggest challenge for travel providers is the lack of consistency across markets. In general the current trend is for a relaxation of controls but many border crossings still require proof of vaccination or a negative test. These are new requirements that the pandemic has brought to the industry and experience after 9/11 suggests that once in place it will be very difficult to remove them. This in turn will place a burden and subsequent cost on airlines, PSSs, travel agents and GDSs to enable vaccine and testing data to be collected and certified at the time of booking and/or boarding.

T2RL continues to believe there will be little international business travel in the next year, even in markets where travel restrictions have been relaxed. The issues of duty of care and insurance will cause hesitation in corporate travel offices although that position is gradually softening.

Social Controls

Social controls are the classic infection control measures that have been used to a greater or lesser extent since the Black Death ravaged Europe in the 14th century. They include isolation and quarantine of infected persons, restrictions on the assembly of people, hand hygiene⁴ and the use of face masks. At the beginning of 2020 such methods were the only available means of combatting the virus and they were introduced in practically every country on earth. In the most extreme cases entire populations were confined to their homes for periods of several weeks. As vaccines became available many countries, especially in the English-speaking world, relaxed the restrictions and some

⁴ Unlike the other measures here the promotion of hand hygiene is a relatively recent phenomenon, dating only from the 20th century
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have now abandoned them altogether. This is not the case in other regions and in Asia especially social controls are still widespread. The use of face masks has been common in countries that were affected by the SARS epidemic in 2002-3 and it is likely to continue indefinitely. Most developed countries have avoided the use of lockdowns in the last year although it is still a tool used in China where at the time of writing the city of Shanghai is entering a complete lock-down.⁵

Summary

In summary the world is a completely heterogeneous environment when it comes to managing the Covid-19 pandemic. Although all governments are selecting from the same menu of responses the packages of measures that they are putting in place vary greatly. Vaccination though is a common factor. For the time being the highest priority of international organisations like the WHO is to dramatically improve the supply of vaccines to less developed countries that have so far lagged a long way behind their richer neighbours.⁶

A side issue to the availability of vaccines is the reluctance of some groups to accept them. Although this is most prominent in the USA there is a measure of vaccine resistance in most regions which sometimes spills over into social unrest.

Border controls and social measures are being applied quite differently in different locations. This will present challenges to international carriers which must stay on top of legal requirements in origin and destination countries. In some cases they will be subject to financial penalties if they carry passengers who are subsequently denied entry on arrival. There may also be issues around compliance with social measures like the use of face masks when this is mandated by regulators but resisted by passengers and even by staff.

Beyond The Pandemic

While the Covid-19 pandemic is far from done it is not the only major external event that is impacting the airline industry. The Russian invasion of Ukraine in February 2022 has created large-scale disruption that extends beyond the borders of the countries most

⁵ <https://www.theguardian.com/world/2022/mar/28/shanghai-to-lock-down-millions-for-mass-testing-as-chinas-covid-cases-surge>

⁶ <https://news.un.org/en/story/2022/03/1113672>

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directly affected. Severe economic sanctions imposed by most western countries have led to a near complete shutdown of flights between Russia and the rest of the world, the closure of Russian airspace to foreign airlines and a spike in the price of oil. Of these effects the oil price rise has the most widespread impact although the closure of routes across Russia has a severe impact on long haul flights to and from Asia Pacific.

RECOMMENDATIONS

Contracting

In the absence of significantly more deadly new variants, especially any that are vaccine-resistant, we are probably moving towards the endgame of the pandemic. Covid-19 is not going away but it is no longer the overwhelmingly highest priority for many airlines and vendors. Despite this its impact is still evident and airlines need to be vigilant in ensuring that their new and renewed contracts are optimised for a period of slow recovery.

A new feature in 2022 is the rise in global inflation. Many older contracts contain escalation clauses that automatically raise prices in line with consumer price indices. Where these are still in place they are liable to cause some pain. Wherever possible airlines should seek to negotiate these clauses away on contract renewal and should certainly not accept them in new contracts.

Vendors need to understand that airlines are not crying wolf. The financial pressures they face are real and if anything have become worse over the last few months as government support to business in general and airlines in particular has been reduced while costs across the board are rising. Rising energy costs will be problematic for hosting vendors whether in conventional data centres or in the cloud. The largest vendors should be investigating the possibility of hedging energy costs in the way that airlines have long hedged fuel prices.

We expect continued pressure for consolidation among airlines and technology providers alike. Both sides need to understand clearly the impact of mergers, acquisitions and company failures on their contractual commitments.

Distribution

Although business travel remains depressed GDS bookings showed a slight recovery towards the end of 2021. There is some anecdotal evidence that customers are turning to travel agents to help them negotiate the complexities of travel restrictions. This may

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be offsetting the pull to direct sales that are perceived to make changes and refunds easier.

Growth continues in API-mediated connectivity, primarily using the NDC standard. All three western GDSs are now pushing hard to get more airlines connected via NDC. This raises questions about the future shape of the market for NDC. The acquisition of a controlling interest in TP Connects by Flight Centre in March suggests that there may be a reconfiguration among the market intermediaries. We explored this in the FirstView “Is there a Future for Standalone NDC Aggregators?”⁷.

One of the drivers for distribution channels with greater capability to supply rich content is the need to provide much more information in the booking flow about current and potential restrictions on travel. There is very little standardisation in these requirements and it is critically important to provide reliable information at the time of booking and to update it as required until after travel is complete.

IT Capabilities

The most critical requirement for airlines and their distribution partners as they attempt to recover from the effects of Covid19 is the ability to manage the increasingly complex regulatory environment. Regulations around border controls, vaccination certification and quarantine are hard to manage and likely to become more so. Governments are already placing increased burdens on airlines with penalties for transporting passengers without the requisite documentation.

Companies offering products that assist airlines in managing these requirements include Amadeus, Daon Inc, Mindtree and IATA Timatic. These solutions were described in previous editions of this report.

Possibly the most important objective of all these technology solutions is the simplification of the process around validating authority to travel and the documentation needed. Any approach that involves a centralised database of passenger vaccination and testing results risks falling foul of data protection regulation such as the European Union’s GDPR. An ideal solution would leave data stored on the passenger’s own device that could be queried at the time of booking and check-in. This is a prime opportunity for serverless technology where processing takes place in the cloud but data remains separate. At least one vendor is working on such a solution.

⁷ <https://www.t2rl.net/insight/display.asp?ID=690>

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In addition to the new burdens brought by the pandemic, staff absences caused by high Covid case rates are causing bottlenecks at many airports. Airlines and airports must work together to accelerate the use of self-service and other tools that ameliorate these pressures.

Please see previous editions of this report for commentary on the opportunities and threats the pandemic has generated in the areas of demand forecasting, dynamic scheduling, cargo, loyalty and interlining.



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