

# Chief Executive's review

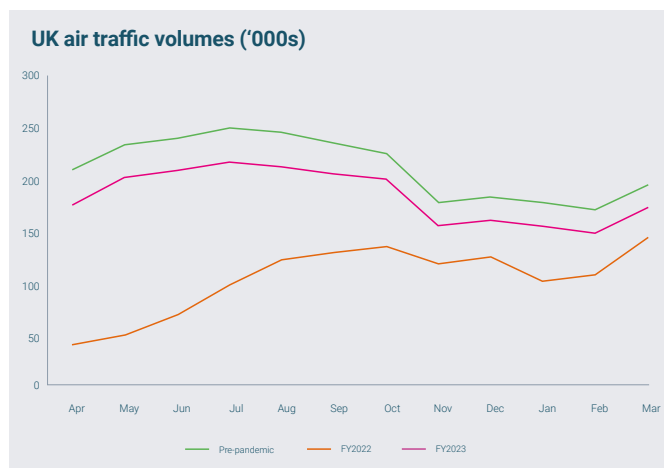
## A safe but at times turbulent recovery

It was a welcome relief to see air traffic volumes recover strongly last summer following the lifting of Covid travel restrictions in March 2022. Over the course of the year, we handled 2.24m flights in the year or 87% of pre-pandemic levels (2022: 1.29m flights). It became clear early last summer that pent-up demand after two years of lockdowns would buoy the industry's recovery, despite inflationary pressures and geopolitical risks.

Our overriding priority, unsurprisingly, was to ensure that we enabled a safe recovery of air traffic. We had made a conscious decision during the pandemic to retain the essential skills to support the recovery, not least because it takes up to three years to train an air traffic controller. In addition, before restrictions lifted, we had supported operational employees with simulation programmes to maintain skills on higher levels of traffic. This meant we were able to ramp our operation back up very quickly and safely support the level of demand. This was achieved in spite of one of the most challenging operational environments we have seen.

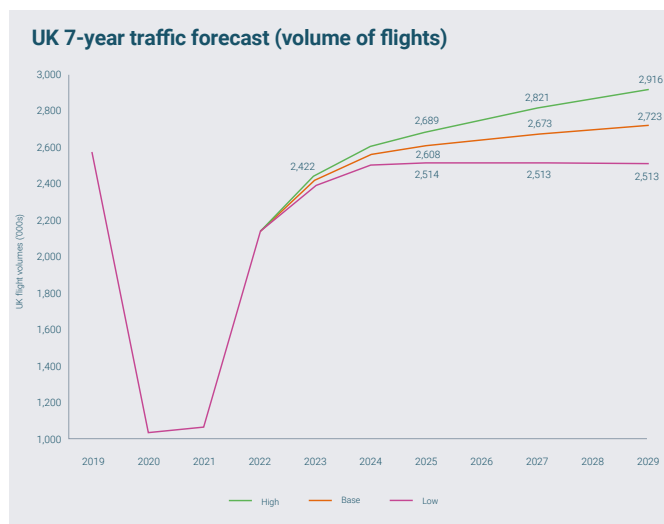
The aviation sector in the UK and much of Europe continued to contend with the after-effects of the pandemic - labour shortages and the struggle to rebuild operational capacity to keep pace with consumer demand. This presented us with a number of operational challenges in the first half of the year.

We plan our operational resourcing tactically according to the level of demand we anticipate and based on published flight schedules. As airlines and airports responded to the strength of consumer demand for travel last summer, traffic growth was not uniform across the airspace network and the daily flight schedule was much more volatile than expected. In peak periods and at certain times of day, volumes often exceeded 90% of pre-pandemic levels. Certain sectors of airspace were unexpectedly busier than others, varying materially from filed schedules, and at times our resources could not match unplanned hourly variations in those airline schedules. To ensure a safe service we consequently had to regulate traffic flows, resulting in some air traffic delay. The level of traffic volatility abated from mid-summer 2022, as airlines aligned their schedules with their abilities to meet demand alongside Heathrow and Gatwick airports' capacity restrictions to manage airline demand at their operations. With a more orderly network subsequently, our service performance improved to levels consistent with or better than 2019 and remained at a low level through the second half of the year.



## Outlook for air traffic volumes

Demand for air travel is generally linked to the strength of the economy. The challenging economic environment and cost of living pressures on consumers, alongside upward pressures on airline ticket prices from higher jet fuel costs remain headwinds for growth over the next few years.



Eurocontrol, Europe's network manager, recently published its March 2023 seven-year forecast together with a high and low case range which reflect assumptions on the strength of the UK's economy, to which air travel demand is generally linked. Its base case scenario assumes a contraction in UK GDP in 2023 and then for modest growth. Eurocontrol is projecting a continuation of the recovery in air traffic volumes we have seen this year with expectations of a return to pre-pandemic levels in 2025. However, this is followed by growth of just 1% per annum reflecting challenges such as inflation, pressure on oil prices and environmental concerns. In the low case, flight volume growth stagnates from 2024 onwards. In its high case, Eurocontrol project recovery in 2024, with average growth of 5% per annum thereafter.

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## Outlook for air traffic volumes (continued)

Given the degree of uncertainty in the outlook, we will be looking to the CAA to ensure that its traffic forecast for NERL's NR23 price control reflects the most up to date developments, including on the macro economy when making its final decision. This is vital to ensure that resourcing and service performance outcomes are appropriately calibrated to projected traffic levels.

## Regulatory developments

In the previous financial year, we consulted customers and submitted to the CAA a plan for the five-year NR23 period (2023-2027) which delivers a safe air traffic system under any recovery scenario, an efficient service performance level underpinned by operational and technical resilience and at cost effective prices to support the recovery of the aviation sector. The plan accommodates capacity increases to support 2027 traffic growth of up to 15% higher than 2019 volumes, enhanced environmental and fuel benefits consistent with achieving UK aviation's target of net zero carbon emissions by 2050 and meeting increased societal expectations of aviation, and the financial resilience against a possible slower recovery, which is essential for maintaining the critical national infrastructure we manage.

In October 2022, the CAA published its initial proposals for NERL's next price control as well as its views on the recovery of the income shortfall during Covid (years 2020 to 2022). In many ways, the CAA's initial proposals recognise the challenges that the company faced during Covid. While there are differences and issues to resolve across many elements of what has been proposed, many of these remain within the normal bounds of the regulatory discourse. However, we were concerned about the CAA's approach to pension costs and inflation, where we believe the balance has skewed well away from regulatory best practice and which present us with some fundamental challenges. These risk undermining much of the effort we made in mitigating the impact of Covid by placing new, unmanageable and unexpected burdens on the company. We are in no doubt that these would both significantly impede the delivery of our primary role, as well as run counter to the CAA's stated objectives for consumers. If left unaddressed, these cuts are of such severity that they would make our plan unworkable.

We currently expect the CAA's final decision later this summer. To achieve our plan's objectives we will require the appropriate resources and risk mitigations from the CAA's price control decisions to enable us to continue to develop and train the next generation of air traffic controllers to meet projected demand safely and provide further operational resilience, and to progress our technology transformation programme while sustaining our legacy technical equipment and advancing airspace modernisation to improve environmental performance and accommodate future traffic growth.

## Employee relations

The impacts of Covid and the uncertain economic environment made for a challenging period for industrial relations. However, engagement and effort by both the company and trades unions enabled us to work through some difficult situations and come to agreements on pay settlements, which recognised the contribution our employees continue to make, cost of living pressures and the wider challenges facing the aviation sector as it recovers from Covid.

Engagement with trades union colleagues is constructive as we work through areas of importance to both of us, including resourcing through NR23.

We reduced our workforce during Covid and since the start of the financial year have been hiring again across targeted areas of the business though, like many companies, we are finding recruitment challenging in key areas. The pandemic accelerated trends in remote working and career flexibility and, alongside employers' demand for well qualified employees, these are making for a competitive labour market, particularly in relation to the engineering skills we require.

During Covid, we retained our skilled air traffic controllers to support the recovery but we were unable to train new controllers due to the risk of spreading the virus within our operation as well as effective training in a live environment being unfeasible with such low flight volumes. In addition to providing the tactical service day to day, outside of the summer peak, we rely on operational staff to train new controllers and to support the development of new technology and changes to the airspace network. While we have sufficient resources today to meet our regulatory commitments, we are now training more new recruits than ever before to meet all of our operational and training needs in future, as the pipeline of newly trained controllers and less certain rates of staff retirements work through the system. We are striving to manage this with a key factor being the NR23 settlement providing an adequate financial envelope, robust to changes in inflation, and sufficient flexibility to respond to changing levels of traffic.

We are clear that building an inclusive culture and making the most of the talent in a diverse workforce are essential if we aspire to be a top 25 company in the UK to work for. Our employee networks continue to expand and propose positive changes that continue to make our workplace an ever more fair, equitable and enjoyable place for everyone. We joined National Inclusion Week again this year, building on the success of our first participation in the prior year. Alongside relevant experts, employee network representatives and senior leaders, Executive colleagues and I hosted a number of live panel discussions and presentations. These covered a range of topics including diversity in recruitment, inclusive processes, and the barriers to disability inclusion. Additionally, we heard from key partners on their approaches to equality, diversity and inclusion. While this is an annual event our focus is not just on the week itself, but on how it can be an extension of our everyday commitment to inclusion across the company for the long-term.

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## Employee relations (continued)

For the first time in four years, we asked our employees how they feel about working at NATS. The survey was conducted by Best Companies, employee engagement specialists, which enables our internal progress to be benchmarked and measured against their accreditation standards. Overall, 62% of employees responded. Based on their feedback, Best Companies rated us as a one-star organisation, one which is very good to work for. This is very encouraging and a high standard that we must maintain and improve on if we are to meet our long-term strategic objective.

With the help of colleagues from across the business, we will use the feedback from the survey to shape and deliver improvement plans particularly in areas of leadership, personal growth and giving something back. We will measure our progress through future surveys and through our ability to attract and retain talent.

## Our role in a sustainable future

We are committed to a net zero estate by 2035 and last summer our greenhouse gas emissions (GHG) reduction targets were independently validated by the SBTi (see page 29) as consistent with meeting the goals of the Paris Agreement, limiting the global temperature rise to 1.5°C. Our strategic objective is for our estate to be carbon negative by 2040.

In 2020, the UK aviation industry, including NATS, made a commitment to net zero emissions by 2050 and we are working with our customers, partners and suppliers to support this. Our plan for NR23 set an ambitious target to reduce carbon emissions from flights under our air traffic control by 4.4% between 2020 and 2035. This is in line with independent assessments of the contribution air traffic control can make to overall aviation emissions reduction, through measures such as optimising flight paths and airspace changes. This is represented in our plan by a sustainable reduction in the 3Di score in the face of traffic growth, which is enabled by airspace modernisation, the biggest contribution we can make to reducing the carbon footprint of flying.

Our airspace modernisation plan is a major component of the UK's overall Airspace Modernisation Strategy that will systemise UK terminal airspace, enhance the way we manage flows of traffic and deliver Free Route Airspace for flights in upper airspace (FRA enables pilots to choose their most direct flight path). The Airspace Change Organising Group (ACOG), which though under NATS' auspices is independent of NERL, leads the coordination of this programme. Synchronised airspace change on this scale requires the commitment of all industry stakeholders, the Department for Transport and the CAA.

As part of our ongoing focus on airspace, in March we modernised the airspace route network above 7,000 feet over South West England and Wales. This was one of the biggest and most complex changes we have made to UK airspace and includes some of the busiest air intersections for international flights. The change introduced a systemised route network from 7,000 feet to 24,500 feet as well as FRA above 24,500 feet, which should deliver an annual saving of over 12,000 tonnes of CO<sub>2</sub> emissions in UK airspace. FRA over Scotland was implemented in the prior year and is now aligned with Northern Europe, which will enable cross-border free routing in future as well as flexible and more efficient flight planning.

We also coordinated with Maastricht air traffic control on changes to airspace in the Humber region, which optimises flight trajectories across the North Sea and will enable annual savings of up to 18,000 tonnes of CO<sub>2</sub> across the UK and European network. Finally, we made changes to London City departure routes, enabling annual savings of 3,300 tonnes of CO<sub>2</sub>.

Aside from changes to airspace structures, our tools such as Arrival Manager and Intelligent Approach have the potential to support lower emissions.

As operator of the UK's critical airspace infrastructure, we are also acting to ensure that our infrastructure is more resilient to extreme weather events such as storms and extremes of temperature, which have had impacts in the last two years, including as recently as last summer, but without leading to service disruption. This includes building higher tolerance levels into the specification of new assets, scenario testing the resilience of airport and en route surveillance systems and enhancing protection of our assets and service during extreme events.

## Commercial developments

In October 2022, we regained the provision of air traffic control and engineering services at Gatwick Airport, the UK's second busiest airport, following a smooth transition from the previous provider. We are delighted to be working with the airport again. Our immediate focus has been on improving service resilience, which is necessary to support the airport with its business ambitions. An important first step was a plan to train and recruit new and experienced controllers which is well underway.

We recently contracted with Heathrow Airport for the delivery of the various equipment and systems required to support a new Virtual Contingency Control Tower (VCF), which is to act as a back-up to the existing airport control tower. This represents a major investment for Heathrow Airport and will provide resilience and help protect the nation's aviation infrastructure.

Other commercial contract successes in the period included a six-year extension of the contract to provide range air traffic control services to the MOD at Aberporth, West Freugh and the Outer Hebrides. Air traffic controllers ensure that fast jets and military drones operate in a safe and controlled environment.

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## Commercial developments (continued)

We also successfully deployed our Intelligent Approach system at Toronto Pearson International and at Amsterdam Airport Schiphol. This provides additional tactical capacity across these multi-runway airports and helps reduce delays, fuel burn and CO<sub>2</sub> emissions, particularly in high wind conditions.

Expanding our international presence, our Indian subsidiary opened an office in Delhi in October 2022, establishing a new team there to support the growth in aviation that the country is experiencing. We look forward to building on our already strong local reputation in the country, and thereby continuing to expand our international presence beyond our existing activities across the Middle East and Asia Pacific.

We remain cognisant of the complexity and the increasing pace of development of new technologies in our marketplace. It demonstrates the importance of working with key partners that are aligned to our strategic intent. Our existing investments in Aireon and Searidge Technologies form the foundation to our partnership aspirations and we continue to develop the technology-led offerings available from these investments while simultaneously investigating future venture possibilities with other key industry stakeholders.

Conversely, after more than a decade, we have concluded that market factors indicated that the time was right to sell our stake in FerroNATS, our air traffic control towers partnership in Spain. We are proud to leave a thriving, well-established and independent operation.

Linking directly to our strategic objective of delivering services for all airspace users, we are playing an active role in the development of electronic and autonomous flight technologies under the government's "Future Flight Challenge" programme. One project aims to demonstrate the feasibility of a UK Advanced Air Mobility ecosystem using Electric Vertical Take-Off & Landing (eVTOL) aircraft; the other is to trial what will be the UK's first distribution network to use drones to transport essential medical supplies and clinical samples throughout Scotland. We will be developing solutions to address the airspace integration challenge – how to integrate safely new types of aircraft with those already there to create a sustainable, modernised, and integrated airspace that is fit for the future. This is an important commercial opportunity for the UK and we have a key role to play as the network operator. It is essential that the operating model set up enables this industry to develop and does not overly constrain it with regulation.

## Executive team changes

Both Juliet Kennedy (Operations Director) and Rob Watkins (Technical Services Director) will be retiring during the next few months after many years of service with the company. They have both made fantastic contributions to NATS and I am very grateful for all they have achieved.

After a rigorous recruitment process, I am delighted that Kathryn Leahy, currently Director Team Heathrow and a former NATS Board member, will succeed Juliet in the role of Chief Operations Officer and that Kuldeep Gharatya, currently Head of Engineering, Major Projects Directorate at Transport for London, succeeds Rob. Both Kathryn and Kuldeep bring excellent experience and track records that will benefit NATS enormously. They are both committed to the objectives we have set and will bring their own determination and energy to seeing us succeed with our 2040 strategy.

## Concluding remarks

Later this summer, after publication of this report, we expect the CAA to make its final decision on the NR23 price control. Our immediate focus is on ensuring that we continue to play our part in working with the rest of the aviation sector to deliver a safe and smooth summer 2023 for the travelling public. We have prepared together for this to ensure a more coordinated management of the demand for air travel.



**Martin Rolfe, FRAeS**  
Chief Executive

