Chinese business & finance

Chinese airlines rush into Europe as western carriers retreat

Ability to keep flying over Russia helps three big state-owned carriers undercut European rivals

The number of Air China flights to the UK has risen sharply © Chris Ratcliffe/Bloomberg

Chan Ho-him in Hong Kong and **Philip Georgiadis** in London JANUARY 8 2025

China's three biggest state-owned airlines are rapidly expanding routes and capacity to Europe as their ability to fly over Russian airspace gives them a cost advantage over regional rivals.

Western carriers have slashed direct flights to China, with Scandinavian Airlines, Lufthansa, British Airways and Virgin Atlantic all suspending some routes to the mainland in 2024, citing cost pressures from avoiding Russia.

Moscow banned most European airlines from Russian airspace in 2022 in response to western sanctions imposed in the wake of President Vladimir Putin's full-scale invasion of Ukraine, adding hours to flights to Asian destinations, including China, and driving up fuel bills.

Chinese airlines, which are unaffected by the Russian airspace ban, have rushed to fill the gap, increasing capacity and offering cheaper tickets despite persistently reporting losses.

"European carriers are just not competitive," said David Yu, an aviation industry expert at New York University Shanghai.

Passenger seat capacity, measured in available seat kilometres, between China and western Europe by the three main Chinese intercontinental carriers — Air China, China Eastern and China Southern — were 18 per cent higher in October than in the same month in 2019, according to DBS equity research analyst Jason Sum.

The three airlines' scheduled flights to the UK, Spain and Italy have risen sharply, according to aviation consultancy Ishka, up between 25 per cent and 45 per cent in the first nine months of 2024 compared with 2019.

They are also able to offer more competitive prices given the cost advantage of flying over Russia. The big three airlines' fares are roughly 5 per cent to 35 per cent cheaper than those of European airlines for direct round-trip flights between China and western Europe, according to UBS analyst Eric Lin.

European airlines have complained that Chinese carriers have an unfair advantage and are establishing a stranglehold on routes between the two regions.

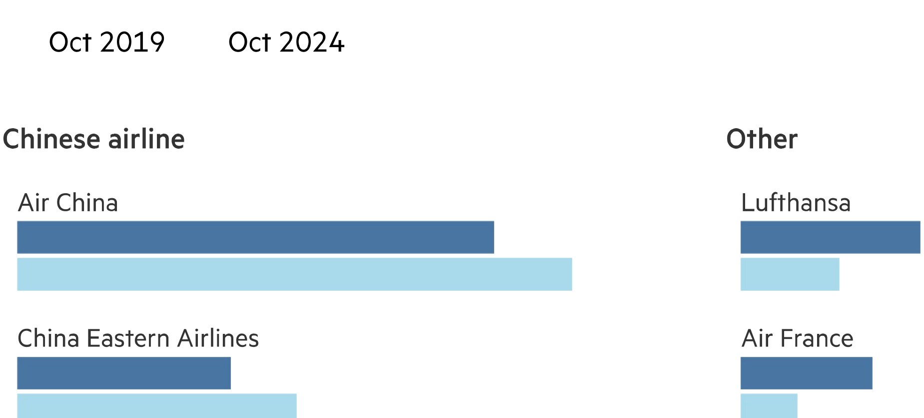
US airlines have successfully lobbied the US government to keep a tight cap on the number of direct round-trip flights to China to stop further inroads from the big Chinese carriers.

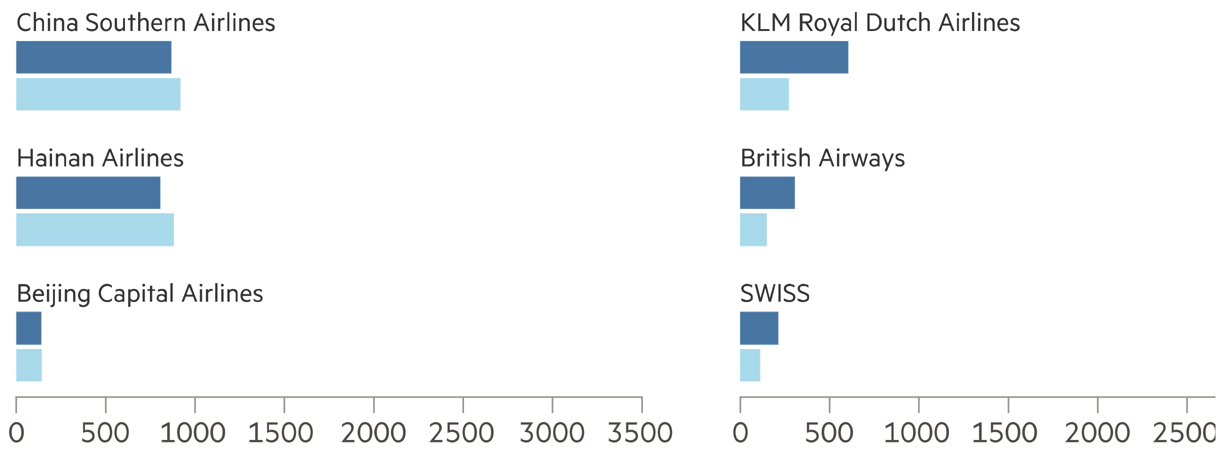
In a statement, Lufthansa said European airlines were "in an extremely unequal competitive position with China", where it said carriers benefited from lower costs and greater government support, as well as the ability to overfly Russia.

"The fact that Lufthansa now must remove one of its oldest routes, Frankfurt-Beijing, from its flight schedule shows how much the balance of international competition is shifting," the airline said.

Chinese airlines have increased capacity to western Europe

Available seat kilometers (mn) between western Europe and China





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Source: DBS

Western industry executives privately question the level of demand for the Chinese airlines' flights, which some say could be lossmaking. Analysts say political motivation is also at work as Beijing expands its visa-free plans to bring back tourists.

"The economy is coming down in China, tourism is not [fully] back yet and business is still recovering," said one China-based aviation industry executive. "You need to increase connectivity in order to increase the flow of people to China."

But while some western carriers have pointed to weak demand for flights out of China, UBS said international passenger demand for the big Chinese airlines was close to pre-pandemic levels.

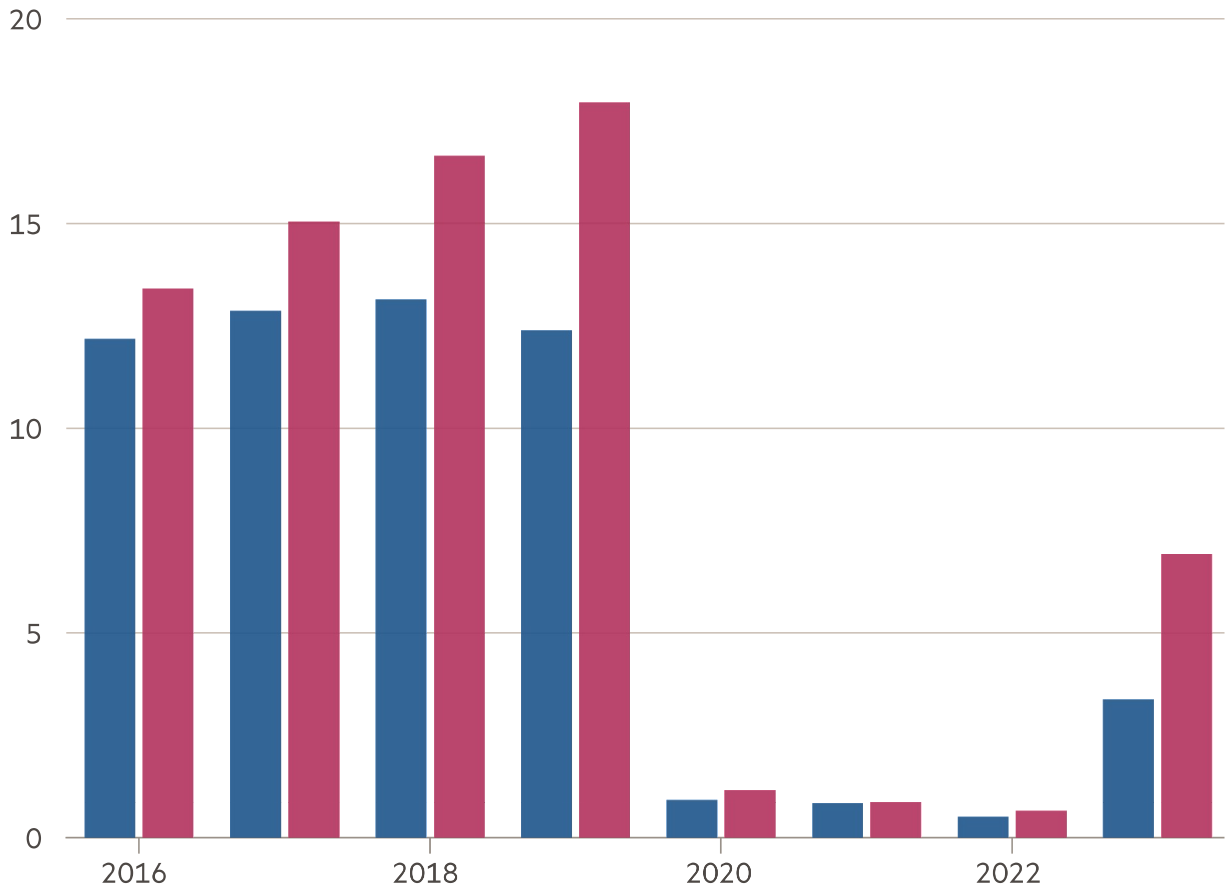
Large Chinese carriers have also boosted direct flights to the Middle East in recent months amid an expansion in business activity between Asia's biggest economy and the Gulf region as well as a deepening of economic ties, particularly between China and Saudi Arabia.

Scheduled flights in the first nine months of 2024 for the big three airlines to Saudi Arabia jumped more than seven-fold compared with the same period in 2019, according to Ishka, while flights to the United Arab Emirates rose 40 per cent.

International carriers have lost market share to Chinese rivals

Number of summer flights departing Europe and North America to China by carrier ('000)

International China



The big three carriers are important to the government in Beijing given aviation was "seen as a critical engine towards ongoing economic growth", said Ishka's analysts, adding that the carriers were helped by route subsidies and that state ownership meant they had significant credit facilities available.

Beijing-based Air China, Shanghai's China Eastern and Guangzhou's China Southern came into existence in the 1980s when the state airline monopoly was broken up and the industry underwent consolidation. All three are dual listed in Hong Kong and in mainland China.

While the Chinese airlines are taking advantage of their cost advantage over European rivals, the country's mixed economic recovery from the Covid-19 pandemic means they are still losing money overall.

In stark contrast to the booming profits reported in 2023 by flagship carriers in Europe and in other Asian nations, China's three big airlines recorded combined losses of Rmb13.3bn ($1.8bn). HSBC and DBS believe Air China and China Eastern could report losses again in 2024.

Analysts said the top Chinese carriers had taken a particular hit from slowing consumption in China as well as growing competition from low-cost carriers on domestic routes. Fares in 2024 for flights departing from Chinese airports are down more than 20 per cent from 2023 for domestic and international flights, according to aviation data provider ForwardKeys.

The big Chinese airlines' outlook for 2025 "continues to be dim", according to Sum at DBS, who said domestic competition would continue to exert "strong pressure" on profits per passenger while China's economic slowdown was likely to weigh on premium travel demand.

A subdued recovery in flights to the airlines' crucial market of North America will also add to profitability pressures, according to Lin at UBS. While Canada in October lifted restrictions on flights to China, flights in early November between China and the US only reached about 30 per cent of 2019 levels, compared with more than 90 per cent for China-Europe flights, according to UBS.

Additional reporting by Haohsiang Ko in Hong Kong