



WORKING PAPER

WORLDWIDE AIR TRANSPORT CONFERENCE (ATCONF)

SIXTH MEETING

Montréal, 18 to 22 March 2013

Agenda Item 1: Global overview of trends and developments

Agenda Item 1.1: Industry and regulatory developments

STRATEGIC ALLIANCES IN THE LATIN AMERICAN REGION

(Presented by 22 Member States², Members of the
Latin American Civil Aviation Commission (LACAC))

EXECUTIVE SUMMARY

This working paper provides information about the growing trend towards the formation of groups of airlines as part of the air transport liberalization process. The advantages and disadvantages of these alliances are noted tangentially, and attention is drawn to certain regulatory issues, which arise as a result of these developments.

Action: The Conference is invited to:

- a) consider this information and the evaluations presented in this paper;
- b) endorse the conclusions presented in paragraph 5; and
- c) adopt the recommendations in paragraph 6.

References: ATConf/6 reference material is available at www.icao.int/meetings/atconf6.

1. INTRODUCTION

1.1 The so-called deregulation adopted by the United States in 1978 gave rise to a new trend in the international air transport market, which started to be governed by more open commercial air agreements with less intervention from the authorities, resulting in intense competition between airlines, where economies of scale are obviously a determining factor for competitiveness. Market size and the formation of ever more extensive networks have played a key role in this process as regards guaranteeing survival in a more open and more competitive international market. This is the reason why airline alliances feature on the agenda as a competitive strategy in the current global aviation market and are

¹ Spanish version provided by the Latin American Civil Aviation Commission (LACAC).

² Argentina, Aruba, Belize, Bolivia, Brazil, Chile, Colombia, Costa Rica, Cuba, Dominican Republic, Ecuador, El Salvador, Guatemala, Honduras, Jamaica, Mexico, Nicaragua, Panama, Paraguay, Peru, Uruguay and Venezuela.

playing an increasingly important role in the development of aviation in Latin America – an exceptional geographical area producing high growth rates.

2. ADVANTAGES AND DISADVANTAGES OF ALLIANCES

2.1 Advantages

2.1.1 Expansion of the network and supply is one of the main advantages, which has encouraged the development of alliances. These alliances represent benefits for users, and are a decisive factor for justifying integration, mergers and acquisitions, as long as there is a guarantee that this is being done in accordance with competition rules.

2.1.2 Apart from giving airlines a global presence, alliances also contribute to the production of a greater variety of services for customers such as: increased frequencies and routes; better connections; unified loyalty programmes for frequent passengers; joint use of VIP lounges; single billing for trips that involve flights with more than one company, etc. At the same time, they provide member airlines with more purchasing power and increased operational efficiencies such as: itinerary coordination, slot use, maintenance efficiencies, more efficient fleet programming and the creation of synergies, etc.

2.2 Disadvantages

2.2.1 Different business model approaches prior to the alliance and additional costs derived from the adjustments required during the alliance process, such as harmonization of fleets, processes and technology.

2.2.2 Possible objections or restrictions imposed by the authorities on the basis of competition rules, which may cause uncertainty around the alliance process. Lack of regulatory unity / harmonization.

2.2.3 Possible adverse effects on users if there are no appropriate control mechanisms in place to prevent unfair competition practices.

3. RECENT ALLIANCES IN LATIN AMERICA

3.1 Air transport has lived through various regulatory contexts during its commercial history, from more regulation (aviation protectionism) to more openness (liberalization and open skies). Agreements and alliances between airlines have always existed and prevailed, although with nuances in the scope, contents and the way in which they have been achieved. In this paper, reference will only be made to the most recent processes which have been observed in the Latin American region.

3.2 As of the 1990s, a much more flexible model for air traffic rights negotiations began to spread across Latin America, within the framework of international trends emerging in the United States and Europe towards the adoption of so-called open skies models. At least from a conceptual point of view, these models have turned out to be more compatible with alliances between operators, to the extent that they remove barriers to access to air routes. Within this new environment of more liberal air markets, the typical commercial alliance agreement between airlines has become code-sharing. This type of agreement has been repeated involving multiple operators, thereby opening the door to so-called Global Alliances. These Global Alliances consist of airline networks that follow a business model that seeks to standardize benefits for clients through frequent flyer programmes, with the subsequent accumulation of miles, standardized check-in procedures, VIP lounges, upgrades, etc.

3.3 Bearing in mind this brief description of the regulatory environment, the most recent experiences in terms of alliances between airlines in the Latin American region are given below and show that competitors align themselves in distinct airline groups- a phenomenon which may be considered as a distinctive feature of the current design of alliances in the region.

3.4 AviancaTaca Holding S.A. Group, consolidated in 2009, is composed of Aerovías del Continente Americano S.A. (Avianca), which includes Tampo Cargo S.A., as well as Aerolíneas Galápagos S.A. (Aerogal) and the airlines of the TACA GROUP: TACA International Airlines S.A., Líneas Aéreas Costarricenses S.A. (LACSA), Transamerican Airlines S.A. (TACA Peru), Servicios Aéreos Nacionales S.A. (SANSa), Aerotaxis La Costeña S.A. and Isleña de Inversiones C.A. de C.V. (ISLEÑA). The creation of this group has produced one of the largest air transport networks in Latin America, facilitating connectivity through its multiple system of connection centres in Bogota, El Salvador, San José (Costa Rica) and Lima.

3.5 COPA Airlines Group. Around the year 2000, COPA Airlines formed an alliance with the former Continental Airlines (today United Airlines), which involved becoming a majority shareholder, and primarily focused on updating its processes, certifying and modernizing its fleet and gaining access to more international destinations through a code-sharing agreement, which all served to strengthen the Panamanian airline. Through this process, at the start of 2005 Copa Holdings acquired the Colombian company Aero Republica, and went on to form a strategic alliance with the Panamanian airline COPA Airlines, with the aim of complementing its operations and air connectivity, in particular through the Panama Hub. COPA Airlines offers more than one hundred daily flights and covers around 60 destinations with some 30 countries on the American continent, meaning that users can travel on direct routes to and from Panama. This operation is complemented by the flights and route network of Aero Republica (known today as COPA Airlines Colombia).

3.6 LAN Group. At the end of the 1990s, the Chilean airline LAN Airlines launched a process of expansion in the South American region, through a model of establishing airlines in different countries under the same LAN brand, with the aim of serving both the cabotage market and the main international routes. LAN Peru, LAN Ecuador and LAN Argentina emerged thanks to this concept and formed the LAN Group together with the Chilean head office airline. In 2010, the LAN group, attracted by the enormous growth in the Colombian cabotage market, acquired the majority shareholding stake in the Colombian company AIRES, and one year later it changed its brand to match the rest of the group, renaming it as LAN Colombia for commercial reasons. Almost in parallel with the AIRES acquisition process, the LAN group formed a strategic alliance with the major Brazilian air transport company, TAM, undoubtedly one of the largest in the region, thereby paving the way for the LATAM alliance.

4. LATIN AMERICAN AIRLINES' PARTICIPATION IN GLOBAL ALLIANCES

4.1 Three global alliances have been formed: Star Alliance, Oneworld and SkyTeam, and together they cover more than 60 per cent of world passenger transport. The recent entry of AVIANCA-TACA and COPA Airlines into Star Alliance, one of the biggest global alliances in the world, represents significant Latin American regional aviation presence in a truly global network within the international air transport market, which will mean better connectivity options for users and increased profits.

4.2 The LATAM Airlines Group is going through an evaluation process because it has to decide between the different global alliances to which its component airlines belong, since LAN is integrated into the One World Alliance, whereas TAM is part of Star Alliance.

4.3 The information displayed below was provided by the Latin American and Caribbean Air Transport Association, ALTA and shows the Global Alliances, which are represented in the region.

4.4 It also compares the total ASK (Available Seat Kilometre) in the region before and after alliances between local airlines. Clearly, this increase is not solely due to the fact that airlines have combined their sales and operations efforts but also because of the increase in passenger traffic due to the influence of local economies.

Alliance	Regional Destinations	Regional ASK's Market Share	World Destinations	World ASK's Market Share
One World	144	18.06%	754	14.51%
SkyTeam	134	16.95%	946	19.32%
Star Alliance	170	30.98%	1185	27.94%

Year	Total # of ASKs from Alliances
2002	28.00%
2012	65.99%

5. CONCLUSIONS

5.1 Expansion of these different types of airline alliances is part of the air transport market's unique trends and characteristics, especially in the international area. In certain cases, this is in response to market regulation restrictions (such as bilateral restrictions on access to routes), while in other cases, this occurs because of the need to cut costs to remain competitive and present on the market, or as a result of the need to restructure the largest networks in the most competitive markets to improve profitability.

5.2 Undoubtedly, it is very important in the air transport business to increase the scale of operation. Forming network routes in the domestic, international and regional sphere contributes in a powerful way to achieving greater scales of operation, lower costs and more competitiveness. Trends towards market liberalization have helped to overcome the traditional concept of the flagship airline, leading to a scheme based more on groups of airlines (alliances), which go beyond the borders of one single country and seek instead to serve wider geographical zones. Alliances play a key role within this environment in terms of improving competitiveness and guaranteeing market presence in the long term.

5.3 The air industry is no stranger to this alliances-based trend, but it is faced with the challenge of having to render this trend compatible with a more liberal regulatory framework, in which it is imperative to guarantee that competition develops in a fair and equitable way. Increased competition and consolidation has led to a higher risk of unfair competitive behaviour.

5.4 Finally, in the case of Latin America, there is a growing trend towards the formation of groups of airlines through alliances that are in the middle of a process of evolution. This can be seen from the different types of agreements between airlines such as: code-sharing; joint use of the technological platform for the passenger reservation and check-in systems (single code); the Aircraft Use Agreements, both in the chartering arrangements and the reciprocal interchange of aircraft, which seek to optimize fleet use and increase airlines' operational capacity; and various commercial accords, including agreements on the joint use of a common brand.

6. **RECOMMENDATIONS**

6.1 The following recommendations are proposed for consideration by the Conference:

- a) ICAO should continue to monitor new developments in this area and update its guidance in response to changes and States' needs; and
- b) ICAO should establish a set of basic principles on fair competition in international air transport, given that competition not only occurs between airlines but increasingly between global alliances as well.

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