Alliances, Mergers, and Airline Consolidation

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- Airline consolidation has reached a new pinnacle.
- The main partners in the 3 global alliances now enjoy antitrust immunity.
- The DL/NW and UA/CO mergers have raised concentration in the US industry (along with Southwest/AirTran).

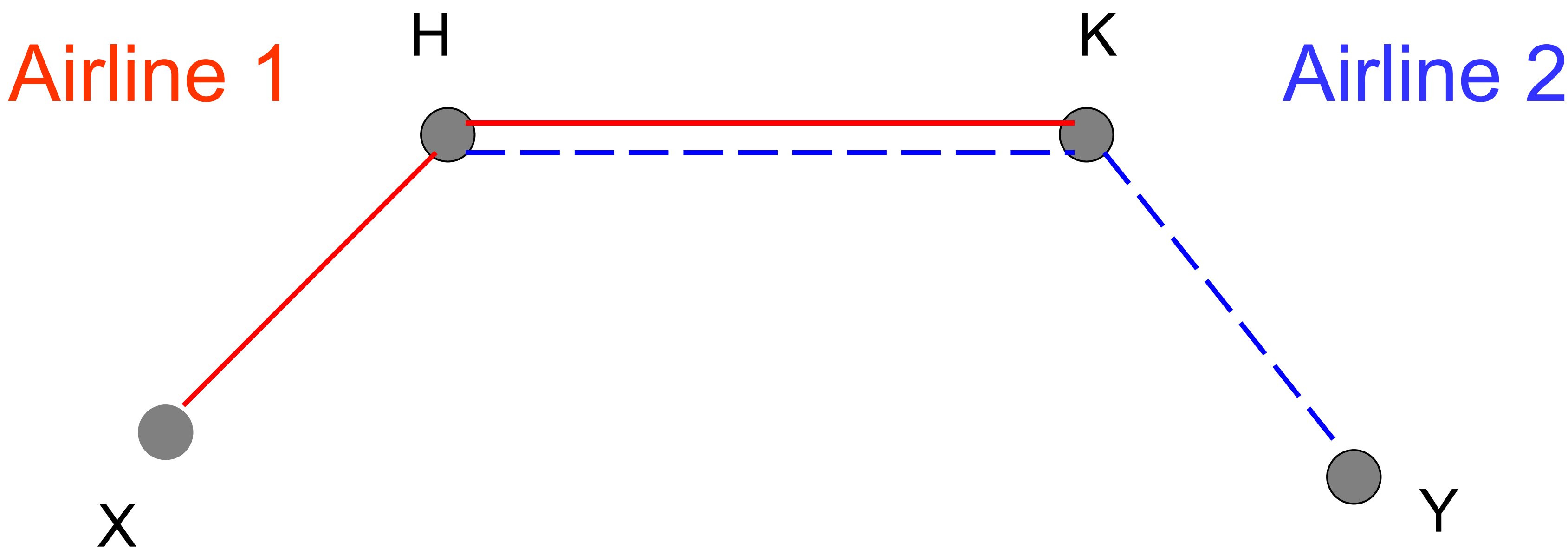
- Good or bad for consumers?
- Consider alliances, then mergers.

Alliances

- It's now recognized that alliances are good for passengers traveling across two networks ("interline passengers").

- Less known about impacts for passengers on hub-to-hub overlap routes.

XY pax get lower fare with alliance (double marginalization gone).



HK pax could see less competition and higher fares (e.g., JFK/LHR with AA/BA).

- With an immunized alliance, reduction in interline fares was as large as 27% in the late 1990s (relative to nonaligned, IATA fares).

- Over the 2000-08 period, reduction is smaller, at 11%.

- Possible reason is that IATA fares have become more competitive (closer to online fares).

- So interline passengers still benefit a lot from alliances.

- Hub-to-hub passengers may see less competition, but they also benefit from offsetting cost synergies from alliance JV's.

- These cost synergies are a possible reason for not imposing competition-enhancing carve-outs on hub-to-hub routes.

Mergers

- Mergers can be anticompetitive.

- But they also generate cost synergies and offer passengers larger networks with more destinations.

- How serious are any anticompetitive effects?

- Since fares don’t respond much to legacy competition, lost competition from a legacy merger doesn’t hurt much.

- Recent work shows that fares on a nonstop route rise by at most 5% when a legacy competitor is lost (LCC effect is much larger!)

- Fares on a connecting route rise by at most 3% when a legacy competitor is lost.

- Using these numbers, predicted aggregate fare increase from UA/CO merger is less than $40 million per year.

- Loss is almost surely offset by merger benefits (cost synergies, network benefits).

- Actual (rather than predicted) fare effects of DL/NW merger are also small.

- Controlling for other changes, recent study shows no measurable fare effect of merger on NW/DL nonstop overlap routes (small number of routes may preclude good estimate).

- NW/DL connecting routes show 5% fare increase from merger, controlling for other changes.

- Bottom line same as in UA/CO case: merger benefits probably dominate.

Conclusions

- Consolidation from mergers and greater integration of alliances generates various benefits.

- Downside of consolidation appears not sufficiently large to offset them.