ATConf/5
2003

Aviation in Transition:

Challenges & Opportunities of Liberalization

Session 2: Industry Challenges for the Regulator

Seeking a New Way

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Speech at the ICAO Pre-Conference Seminar
Montreal, 22 March 2003

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"Seeking a New Way"

I think it is extremely positive that this panel focuses on the role of regulators. Regulation is indeed the core of the problem and also part of the solution to the liberalization issue.

Liberalization provides great challenges to regulators.

CThe first one is: what to regulate.
CThe second one: how to regulate better.

The paradox is that effective liberalization needs effective regulation. I will try in this short statement to begin sorting out these issues.

CRISIS

The air transport industry is going through its worst crisis since the Wright Brothers flew one hundred years ago. All continents are affected in one way or another by this crisis.

Asia-Pacific does better than the other regions because some of the structural problems there are hidden by spectacular market growth.

North America, still the number one aviation market in the world, is in ruins. Two major US carriers are in bankruptcy protection. The top six US airlines have one hundred billion dollars of debt but a market capitalization of only 2.5 billion dollars. Most observers point to a broken business model and the need for change.

In Europe, on the other hand, the top airlines are still performing well thanks to a decade of massive restructuring. Drastic cost reductions and flexible fleets, combined with a new approach to distribution are all part of this success. However, with over one hundred airlines, the European aviation market is still far too fragmented. In Europe, like in North America, change is needed.

But nowhere is change more needed than in West Africa and in Latin America. There, the industry is practically in its final stages. A third of the Latin American airlines are technically bankrupt.

Famous names such as Swissair, Air Afrique, Ansett, Sabena and TWA are gone. In the last two years, the industry has lost 31 billion dollars.

Given the current crisis over Iraq, 2003 could well be another year of heavy losses. Clearly this cannot continue.

THE LAST CHANCE

Our industry needs change. Government regulation keeps our industry from changing. This ICAO conference may well represent the last chance to set our industry on the right regulatory track.

THE THREE PILLARS OF STAGNATION

The obstacles to change are:

Cthe bilateral system,
Cnational ownership rules
Cand the attitude of competition authorities.

The three pillars of stagnation! We don't want to bring the system down. We want to modernize it to meet the economic reality of the 21st century.

Governments must continue to strictly regulate safety and security. Governments must keep on controlling the licensing process. Let me be clear, IATA firmly opposes any "flags of convenience" idea. But key parts of commercial regulation are outdated.

We need government leadership to initiate the process of change. I am here to say it loud and clear:

we must seek a new way!
We must modernize the three pillars of stagnation and
build a framework relevant to the reality of today and tomorrow.

THE BILATERAL SYSTEM

In the 1970s came market liberalization through domestic de-regulation. The next step was liberal bilaterals, the so-called "open skies" agreements.

We now need regional liberalization. In East and Southern Africa, and in parts of Latin America, developing states have already taken pragmatic steps towards regional liberalization. The Yamoussoukro Declaration is in itself a step in the right direction.

Liberalization can even take place between regions. The Transatlantic Common Aviation Area (TCAA) proposal represents progress in this direction. The North Atlantic could be a starting point in seeking a new way.

But remember, our industry is global. It relies on worldwide standards and rules. Other players from other regions must also be involved in the change process.

And this is why this conference is crucial. Change begins here at ICAO.

NATIONAL OWNERSHIP LIMITS

The recent ruling of the European Court of Justice goes in the right direction. It effectively abolished nationality clauses between EU member states. It's a good start. One pillar is chipped.

Airlines should be free to merge and approach the international financial markets for capital. The wave of globalization must eliminate national ownership limits wherever they represent an obstacle to development. These limits are denying airlines the freedom of action given to all other businesses. Some states may wish to keep a "golden share" to make sure their national interests are taken into account. Fine! We simply ask these states not to create obstacles for those who wish to liberalize further. They can decide their own timing but they should not be allowed to stop the process. Freedom is really what our industry needs the most.

COMPETITION POLICIES

Dogmatic competition policies also restrict our freedom.

Competition is tough in our industry. Some of it comes from the so-called "low cost" carriers. They do represent healthy competition and genuine change in the US, in Europe and even now in Asia. They also operate in single markets, free from the limitations imposed by the three pillars of stagnation!

The "network" carriers have been pushed to rethink their distributions systems. They are also drastically reducing their costs. Many airlines are also restructuring their fares to make them more attractive to new customer segments. Many are re-inventing their product. In spite of all that, competition authorities, all over the world seem to be over cautious with air transport.

What other global business is more fragmented than air transport? Where are the multi-national players, the Daimler-Chrysler's or the Pharmacia-Upjohn's of air transport? Some industries requiring large investments are fiercely competitive even with just a few very large players.

In spite of that, most airline alliance projects, or the few merger attempts face long delays.

Alliances are all geared at making our industry more efficient in the interest of our customers. We need the economies of scales that mergers or acquisitions can provide with the proper competition supervision. Here again, the regulators must take up the challenge of change!

But, as we prepare to modernise the three pillars of stagnation, governments must also take a hard look at the whole civil aviation sector.

LEVEL PLAYING FIELD

The airlines are vigorously competing with each other. While this battle continues, they are also the victims of monopoly operators of aviation infrastructure: airports and air traffic management companies.

The liberalization process has failed to provide a level playing field for all parties in the civil aviation sector. Regulators have not protected the airlines and their passengers from the monopoly infrastructure providers.

The marketplace discipline is not there to force airports and ATM companies to be efficient. Some may be tempted to take it easy. They are charging the cost of their inefficiency to the airlines and their customers. And this must end.

Airlines can no longer pay for their inefficiency. As monopolies, and often, private monopolies, they can easily abuse that position. To be fair, they don't always do so, there are exceptions. In Singapore and in a number of cases in the US and in Europe, national or local authorities have been wise. They treat aviation infrastructure as an asset in order to foster economic and social development. But this approach does not keep them from being profitable.

In a few cases, infrastructure providers are kept from abusing their position by effective economic regulation. But even where that regulation is in place, like in the UK, the airlines still face great problems in trying to keep charges in line with real costs.

Our industry needs an effective economic regulation of infrastructure providers. It cannot survive without it!

THE IMPACT OF WAR

As we gather here in Montreal, to consider the future of our industry, war goes on in the Middle East. According to our estimates, the war is likely to reduce traffic worldwide by 10% for the duration of the conflict. This would mean a loss of 10 billion dollars on international traffic only between now and the summer. This had to be said, our industry needs urgent relief and liberalization could be part of that relief.

In summary, there are four challenges for regulators: the three pillars of stagnation and the economic regulation of monopoly service providers.

I believe that they have enough to deal with! It is time to get going.

Thank you.