

THE POLICY OF OPEN SKIES IN CHILE

1. Background

At the end of the 1970s, Chile started to make profound changes to its economic structure, promoting a social market economy system based on private ownership of the means of production, private initiative and social harmony, as elements necessary for the economic development of the country. In this context, Executive Order 2.564 was issued in 1979, confirming the so-called **open skies policy** in our country. This policy is based on the following fundamental principles:

a) Free entry into markets

The power to grant commercial air permits was repealed, since it was considered that these are granted directly by the act that establishes that both Chilean and foreign airlines can operate freely in the country, provided that they comply with insurance requirements and technical/operational safety requirements. As an exception, the Junta de Aeronáutica Civil de Chile (JAC) may restrict foreign airlines in the following cases:

- i) if their country of origin applies restrictions to Chilean airlines (bilateral reciprocity); and
- ii) if the foreign airline operates on a route which is restricted by another country for Chilean airlines and it is considered that such restrictions are significantly affecting Chilean airlines (optional power and at the judgement of the authority).

b) Freedom of prices

Airlines are permitted to freely establish the tariffs that they will apply. They only have to register them with the JAC. The authority does not have powers to set and object to prices. As an exception, tariffs can be set if the authority of the other country does not accept the freedom of tariffs; this situation has never occurred in practice. Within Chile, there is a totally open system in operation in this matter. When all the tariffs were set by the authority, lower tariffs were not achieved and only competition was avoided because the tariff levels were proposed by the same airlines and were generally accepted by the authority since it did not have access to the actual cost basis of the airlines.

c) Minimum intervention by the authority

This is reflected in:

- a) the markets are competitive, with the advantages of quality and prices that this implies;
- b) air transport services moved totally to the private sector;
- c) the authority was debureaucratized when irrelevant procedures and controls were removed. It was thus possible for airlines to quickly modify their operations whenever they needed to and only the technical implications were checked.

2. Liberalization of the regulatory framework

The harmony between Article 1, paragraph 1, of Executive Order 2.564 and Articles 4, 5 and 10 of the same Executive Order ensures adherence to the principle of **free entry into the market**: Chilean and foreign airlines will be able to establish domestic or international scheduled or non-scheduled passenger or cargo air transport services and specialized aerial work services, without limitations with respect to aircraft, title held on it, capacity offered, places of operation, frequency of services, itineraries and tariffs and without the need for any more approval by the commercial air authority other than the approval of the insurance requirements and the technical/operational safety requirements.

Furthermore, **freedom of tariffs** is one of the basic assumptions of the social market economy and it is thus being applied in air transport. Executive Order 2.564 repealed the powers of the JAC to set tariffs and these were left to be set freely by each airlines. At first, tariffs rose, but then they were quickly stabilized with competition until they stayed at normal levels. Nevertheless, Article 2, paragraph 4, of Executive Order 2.564 establishes that in cases where the JAC has not set tariffs, the airlines will have to register with that authority the tariffs that they will apply. The purpose is to give transparency to the market by keeping a public record of tariffs.

Finally, **minimum intervention** by the authority is reflected by the fact that Executive Order 2.564 did not grant the JAC extensive powers to intervene in markets, except on an ad hoc and specific basis: to check insurance and to negotiate reciprocity. If the international air traffic rights are restricted by another country and if there is more than one Chilean airline interested in exercising the same rights, Executive Order 2.564 establishes that there should be a call for tenders for these rights on the basis only of money tenders, without any other consideration by the JAC. The objective is to avoid subjective evaluations in assigning routes.

3. Effects and evolution

In order to see what the effects have been of the open skies policy applied by Chile, it is useful to differentiate what has occurred domestically from what has occurred internationally.

A. Domestic

Domestically, the policy of absolute freedom to enter into markets and set prices has been maintained. This has made it possible to expand domestic traffic from 800 000 passengers in 1989 to 2 900 000 passengers in 2002, with an increase of 255% and with an annual average growth rate of 11%. For its part, air cargo increased by 225% in the same period, with an annual average growth rate of 10%. The number of services departing from Santiago increased from 100 per week in 1989 to around 364 per week at the end of the last century. This means that it more than tripled in this period.

B. International

Internationally, in all bilateral negotiations, the Chilean aeronautical authority offers and promotes extensive and unrestricted openness which is not always shared by other countries. Since 1989, the government has been intensifying government efforts to obtain greater openness with other countries in order to create greater opportunities for Chilean airlines through negotiations between aeronautical authorities, on the basis on some occasions of economic complementation agreements signed by Chile. This has helped to increase Chile's international traffic from 957 000 passengers in 1989 to 3 066 000 in 2002, that is a 221% increase with an annual average growth rate of 10%. International air cargo measured in tonnes has increased in the same period by 207%, with an annual average growth rate of 9%. The number of international services increased from 104 in 1989 to 329 at the end of the last century. This means that supply tripled. In spite of the strong competition that has existed between Chilean and foreign airlines on Chile's international routes, Chilean airlines increased their international passenger traffic and their participation, also measured in terms of passengers, increased too. Furthermore, there are presently 15 foreign airlines with 134 services per week competing in Chile's market. Chilean airlines presently have 148 international services per week, in comparison with the 47 that they had in 1989. International cargo traffic (tonnes) of Chilean airlines increased by 162%, with an annual growth rate of 8%.