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THE DEVELOPMENT OF THE GERMAN DOMESTIC AVIATION MARKET UNDER LIBERALIZATION

(Submitted by Germany)

1. German aviation policy as well as the national aviation industry have dealt with the question of what impacts liberalization, globalization and privatization might have on the development of German civil aviation.

2. Against this background Germany had very early decided to play an active role in liberalization in Europe and has consequently taken a positive approach towards the opening up of the internal aviation market in Europe within the framework of the various EU Liberalization Packages. Germany is maintaining this strategy as it has proven to be right for the development of the national aviation market as a whole.

3. However, it has to be born in mind that the liberalization of a market so specialized as civil aviation cannot take place over night simply as a result of changing the basic framework. In fact, liberalization is a long -lasting process with no expectation of immediate results, as replacing governmental decisions by those of an entrepreneurial nature is a relatively cumbersome way of opening-up a market. Even if the legal framework for this change has already been set up, it takes a while for the market participants to cope with the new freedom and to benefit to the maximum from the changed environment. Only then will the political aim of intensifying the competition in the interests of consumers and a stimulation of the market be achieved.

4. The development of the German civil aviation market since the introduction of the European Liberalization Packages may serve as an example of how difficult such a process can be.

5. On the eve of the introduction of the Third Package in 1992, the German market was dominated by the flag carrier Lufthansa. Although there were two more German airlines providing scheduled services to national and international destinations, as well as some smaller regional airlines, there was no real competitor to Lufthansa.

6. For the German aviation market serious competition arose only when Deutsche British Airways (DBA) entered the market in 1992, taking over some internal German services (services that had been reserved before Germany's reunification for the airlines of the UK, US and France) to and from Berlin and competing with Lufthansa. In 1994, DBA set up its head office and main base at Munich and started scheduled services between Munich and Düsseldorf, and later on as well to more important German routes from Munich to (*inter alia*) Hamburg and Cologne. These routes had up to then been exclusively served by Lufthansa and the direct competition partly led to a very aggressive "price war" between the two carriers. This again resulted in fluctuations of tariffs in a tariff-system that up to then had been relatively fixed. For consumers, this development had the effect that they benefited not only from having the choice between two different carriers on those routes; in addition fares dropped and the tariff conditions became more consumer friendly (eg. off-peak prices, easier rebooking). The competition between the two carriers became even more aggressive when DBA finally pushed into Lufthansa's home base at Frankfurt and started a scheduled service Munich / Frankfurt. As an outcome of the situation, fares on that route dropped sharply between October 1997 and February 1998, by

a third for the business fare and by nearly a half for the fully flexible economy fare. Although DBA finally withdraw from that route in March 1998 and concentrated on other routes, the benefits of the price competition for consumers remained.

7. In the meantime, a number of other air carriers such as Eurowings, had successfully entered the German market and a considerable growth of routes and frequencies had taken place. Affected by that development were important routes like Frankfurt / Berlin on which Lufthansa in the beginning had had a virtual monopoly. This monopoly was now broken. This was for the first time a real market situation for civil aviation in Germany. The overall competition situation and the new awareness of air carriers of the market forces resulted in ever better conditions for consumers, as air carriers now had to compete for the consumer's favour. From time to time state authorities had to give advice to the participants of the newly developing market to keep things going in a fair and transparent way.

8. At present, the German aviation market is again being stimulated, as more and more Low Cost Carriers enter the market. In the beginning these carriers had only been active in profitable niches in the German market but with the growing success of the low cost concept they are now keen to expand their activities even to main routes that have up to now been the preserve of the established air carriers.

9. In principle, Germany welcomes this new competition in the aviation market, as long as it can be guaranteed by air carriers, that more and more reduced fares will not interfere with safety and security requirements.

10. From Germany's experiences with liberalization the following conclusions can be drawn:

a) Noticeable effects of liberalization for the German aviation market have occurred gradually; and

b) Possibly liberalization shows its most significant effects only now following the entry into the market of the Low Cost Carriers.

The emphasis on competition that arose with the liberalization of the aviation market had up to now mostly positive effects in Germany. Accordingly, Germany will continue to promote the liberalization of civil aviation.

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