

**Aviation Intelligence Reporter  
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It was Warren Buffett who noted that it is only when the tide goes out that we discover who is swimming naked. There is now an unholy scramble back to the dressing rooms from the edge of the fast receding surf. A lot of business models seem to have been caught out with no back-up and no support.

As befits a dash to modesty, it is each to their own. There is no thought of coordination or politeness – it is every industry sector, and indeed every industry model, for itself.

And it is clear that some parts of the industry are broken. Long haul legacy carriers have undergone considerable commendable change and development in the last few years, only to discover that it might not be enough. The one ray of hope for the legacy carriers is that finally, months after them, the low cost carriers too seem to be suffering.

For a long time, the LCCs showed remarkable growth in the teeth of a raging storm. At the start of this year, it is clear that this run was coming to an end. With their simplified operations, benefit of scale and nose for finding attractive sectors and market pockets they had for some time been able to slow down the rate of decrease. Now, even the LCCs are showing a fall in passenger numbers.

That, in turn, is bad news for the small and regional airports. When the LCCs sneeze, the regional airports catch a cold. The hunt is on for new markets and new ways of attracting the LCCs and their passengers. Text books on what is and is not State Aid are being dusted off. Likewise, the major hub airports, tied more closely to the legacy interlining carriers, have been declining for several months.

Eurocontrol also reports that business aviation is down by something like 20% in Europe. Overall, Eurocontrol predicts seeing a 5% reduction in traffic. Across the world ANSPs are reporting decreases in traffic of at least 5%, and in some cases much more. And that is blips on a screen that they are measuring, not the passengers inside the aircraft.

The situation is dire in all the areas of the world. IATA is using words like 'grim' to highlight what the situation is like. Europe is down, Asia is down, the US is down; even the Middle East is showing signs of strain. So what to do about it?

This, you might think, would be a perfect time for the industry to come together. Right. Dream on. There are a lot of things that might be done; could be done; should be done. But it is true that for any of those things to happen we will need, as an industry, to reshape and rebuild the entire industry and the way that it interacts – so there is no hope of that happening.

No, instead, we are seeing the distinctly unedifying sight of knives being sharpened and positions being staked out. From discussions about the ownership and control rules to infrastructure reform to airport competition and arguments about slots the industry is turning on itself. This edition of the Aviation Intelligence Reporter looks at each of these.

Remember, one of the golden rules is that in any fight between principle and self interest, back self interest – you can be sure that it is fighting to win. As they say in boxing: seconds, out of the ring.

## Ownership and Control: Rep Oberstar sets the scene

You might have thought that one of the easiest issues to address was that of liberalising investment rules to allow airlines to access capital markets like any other company. Few things would seem easier, and more logical. IATA has been pushing modest, step-wise proposals for some time, under the unfortunate name of the Agenda for Freedom. There is much to commend about the approach that IATA is putting forward.

At the same time, the European Commission was hoping that the second round of negotiations on the EU-US Open Skies bilateral agreement, which have already started, would also bring this issue to conclusion, allowing European airlines to invest in US airlines (and vice versa) and give European carriers access to the US capital markets.

But, no. In a speech that pundits are already calling the 'Hell no' speech, the influential Chairman of the US House Transport and Infrastructure Committee, Rep Oberstar set out what he considers are fundamental elements to recovery and growth of the US air transport industry. And hell, no, it does not include anything that might risk being construed as foreign interference with the running of US airlines. Far from loosening the current constraints, Rep Oberstar would tighten them. In his line of fire are alliances; non-US employees in positions of authority; and anti-trust immunity for mergers with foreigners. So don't even think about asking for changes to the punitive restrictions on ownership and control: hell no.

So that is that for the Agenda for Freedom. And any extension to the EU-US Open Skies deal. For IATA that is unfortunate, but it is in a position to push forward without direct US participation. But it will be much harder for the European Commission. If this view becomes doctrine (Rep Oberstar is influential, but not definitive – other views may still prevail now that finally an FAA Administrator has been nominated) that will put the acid back on the Europeans. How are they going to react to that?

In the past, well placed sources have been quoted saying that failure to open up the ownership and control discussion will see Europe repudiate the EU-US Open Skies agreement. Those are fighting words. It might be true that such things were being said when the European side did not think that its bluff was going to be called. If so it might be wise to wait and see.

However, there might be a canary in a coal mine on this one, giving us an early indication of what might happen. There has been considerable behind the scenes lobbying done by Europe and European airlines over an early Rep Oberstar contribution to the debate. He has inserted a requirement that all non-US repair stations that work on US registered aircraft must be certified pursuant to Part 145 of the US legislation, and to be inspected twice a year. Drug and alcohol tests are also required.

This is a real issue for Rep Oberstar and the US union movement which has long supported him. The amount of heavy maintenance work that has been outsourced in the USA has grown from 34% in 2003 to 71% last year.

The fear has been that this legislation will bring retaliation from the European side. After all, there is a trigger that the Europeans could use. As part of the EU-US Open Skies

package there was also an EU-US Safety Agreement, concluded in June 2008. The European side could delay implementing that. Bring it on says the good Congressman, bring it on. He is sure that the Europeans will not retaliate.

He notes, with some force, that the foreign repair station inspection provisions were already on the books when the Safety Agreement was signed. In his own words:

I think that the argument that this provision will somehow be the downfall of the U.S.-EU Safety agreement is unfounded. I have had this discussion with the EU Transport Ministry, in Brussels, Slovenia and here 2 weeks ago and with Paolo Costa, Chair of the EU Parliament Committee on Transportation and his colleagues – in French, in Italian, and in English. They understand – they do not like it – but they understand.

The fact is that the provision will simply ensure that foreign entities conducting repair work on U.S. aircraft adhere to U.S. safety standards and regulations. I welcome the same scrutiny by the EU of U.S. repair stations; the United States and the EU should be working together to harmonize standards and to make the system safer, rather than decreasing oversight and accountability. Alarmism about retaliation is premature and speculative at best.

The comment about working together to harmonise standards is important for another reason too. Working together is exactly what Rep Oberstar wants in the environment area. And in the same vein too. By “working together” he means our way; or not at all. At least he is consistent.

Even though officially, the US position on the European ETS is not settled, if Rep Oberstar has any say, it might as well be. He rejects out of hand any hint of working together with Europe within the Copenhagen process, and supports strongly working together with Europe within ICAO. The fact that Europe has threatened to abandon the ICAO track is irrelevant. The US is very much looking forward to working together with Europe in ICAO. Take it or leave it. Or, as Rep Oberstar said:

While I am a strong supporter of responsible action to deal with global climate change, I do not like the EU's unilateral decision to impose a solution on the United States. The EU emissions trading scheme violates international aviation law, offers no protection to U.S. airlines from multiple charges, and diverts revenue to subsidize EU industry and governments. The EU plan unilaterally mandates a single solution rather than negotiating with the United States and other countries to develop a performance based approach. How does that view square with our safety provisions? Safety is not negotiable – just as I said that the United States and the EU should harmonize safety standards, so shall we cooperate on emissions.

So there you have it – when the US acts unilaterally, it is in the interest of everyone because it is about safety, not US jobs, and when Europe acts unilaterally, it is outrageous perfidious foreign behaviour. What Europe needs to do is learn to act like us. But hell, no, not if that actually means behaving like us.

## Infrastructure: What about opening that to competition?

So if we cannot be sure that the airlines will be able to access capital like real companies any time soon, what about the rest of the industry? Is there any way that we can bring competition into other parts of the industry? Surely, it is competition that sorts the broken from the operative models, ensuring the survival of the fittest.

Everyone hates a monopoly, except of course, those that have one. So when faced with the opportunity to break up a monopoly, most regulators are only keen to be seen to do so. Monopoly suppliers are very much in the news in air transport at the moment, so it might be time to stop and reflect.

Depending on who you talk to, the two most well known natural monopolies in air transport are said to be airports and air traffic control. If that is true, discussions about competition are irrelevant. A natural monopoly is not capable of being 'fixed' by being broken up, or by having competitors introduced. All that can happen is that they be appropriately regulated.

Finding suitable regulations for these entities is perhaps best described as a work in progress. That might be because there is still dispute that they are in fact natural monopolies in the first place.

The legacy airlines are repeatedly in print (in ICAO submissions and elsewhere) noting that all airports are natural monopolies – a view, not surprisingly, the airports dispute. So, clearly, does the UK Competition Authority. In March it ordered that BAA, the owner of several airports in the UK, including three in London and three in Scotland, dispose of two London airports (Gatwick and Stansted) and one of Glasgow or Edinburgh.

If the airports were actually natural monopolies, ownership would be irrelevant. What would need to be regulated would be behaviour. The Competition Authority in fact decided that by changing ownership and pitting different operators against each other competitive forces will be brought into play. In coming to this conclusion they have further isolated the IATA position.

The usual argument against this proposed remedy is that each airport caters to a different mix of airlines and passengers and complex issues such as the interplay between slot restrictions and interline passenger flows mean that airlines have little choice about where to fly. On this analysis, little can be done to make each airport competitive with the others.

Therefore, it is hard to overestimate the importance of the second arm of what was obviously a coordinated pincer movement. For some reason, it was less heralded and commented on, but it was equally important. The UK government announced a change of policy on the supervision and regulation of airports.

From now on, all regulation must be focused on the experience of the passengers, rather than the airports' direct and actual customers, the airlines. This must be seen as a naked grab to go over the heads of the traditional airline argument and to shake up these allegedly natural monopolies.

NetJets Europe also has its own self help approach – they have purchased an entire airport near Frankfurt to ensure that they have the slots and the customer service facilities that they need to run their operations. AirAsia considered the same thing in Kuala Lumpur. Which part of airport competition don't the legacy airlines get?

There would have been another way for the Competition Authority to do this – break down ownership at each airport at the terminal level. That would have sidestepped the interline/slot argument. It would have then allowed each airport to focus on the infrastructure that its airline customers need, but each terminal to focus on the passenger experience.

Such a move would bring the privatisation of aviation infrastructure in line with the privatisation of most other public infrastructure entities, such as rail and power – by considering the customer service issues apart from the provision of the underlying infrastructure. Currently in both airports and air navigation service provision that is not the case.

In the rail industry, whilst the train services are often privatised, the tracks themselves are usually State owned, or at least, owned by a different entity to the train service providers. The same is true in the power industry with the power lines. It may be that this is what is required in aviation too.

It may also help to think about options like this in the other infrastructure monopoly area, air traffic management provision. What is increasingly clear in the ATM arena is that the European model is broken. When it was decided to separate regulation and provision of air traffic control services it was seen as a very good first step towards widespread rationalisation of the fragmented and dysfunctional air traffic control system for Europe.

Sadly, what it actually meant was the creation of 37 different profit and loss accounts. And 37 regulators. Making it worse was the fact that the model called for strict control over charges. And, it was designed on the assumption of unending growth.

Maybe what was needed, given the courage that the decision to create commercial entities must have taken, was the courage to go all the way, and create one commercial air navigation service provider. Not that that would have made the system more competitive of course.

At least not at the moment. The European Low Fare Carriers Association advocates using the new technologies to create, in effect, a common infrastructure provider, and then a choice of service suppliers. This is clearly innovative for the ATM industry – which of itself makes it problematic.

But, it has to be said that the failure of the current regulatory structure is becoming apparent. The ATM industry is currently designed to be “cost plus.” With a sudden decrease in traffic, the cost per transaction must go up. Airlines are screaming with the pain, but the ANSPs can do little about it. If there is what is euphemistically called an ‘under-recovery’ it must be recouped within two years.

The problem was conceded by CANSO at the end of March, with an open letter on behalf of its members to its airline customers. ANSPs share the airlines' pain, and they are doing what they can. But that there is a limit to what can be done in the short term.

Equally importantly, this means that there is no way to fund development of new systems and capacity enhancements. That is a fundamental point given that we are at the particular crossroads we are at: the corner of Slump-in-Traffic and New-Systems.

## **ANSPs: At the crossroads – where to from here?**

This is not a service issue; it is a service model issue. At the recent ATC Global conference in Amsterdam, Boeing ATM's Neil Planzer put the cat amongst the ideological pigeons by noting that at best, the corporatised ANSPs could do tactical things. And, he noted, they had lost the right to run to the State for bail out funds the day they elected to become corporatised monopolies.

Airlines are protesting loudly at the pain of the costs; ANSPs are trying to run businesses that respond to their customers but which do not go bankrupt in the process. What can be done? The answer everyone is clinging to is new technology.

Eamonn Brennan, the CEO of the Irish ANSP, put that idea into context in his presentation. Again. To make his point he gave the same presentation that he gave 5 years ago. ANSPs are starting to look like performers in the world's longest running production of *Waiting for Godot*. His point then, and his point now, is that we can waste significant amounts of time writing reports, commissioning studies and creating committees, but all that will do is waste money.

The fact is that the aircraft today have significantly more technology on-board than is used to execute the air traffic control services that they receive. A modern aircraft can land completely automatically with only a third of its avionic equipment switched on. We control aircraft built and equipped in the 21<sup>st</sup> century with rules and processes developed half way through the 20<sup>th</sup>.

So how do we fix it? Does this mean that we need to spend more on SESAR? Brennan's answer to that is not until we have started to use what we have. Aircraft can already do tailored arrivals, but to do so will need to use new, different, procedures. And so will the controllers. That is proving a sticking point.

Airlines keen to use tailored arrivals where available, in Melbourne for example, are finding that the controllers are having trouble giving up their authority to the aircraft. They are the ones that want to tell the aircraft what to do. They are the controllers after all.

The recent trail environment flights, AIRE and ASPIRE, across the North Atlantic and Pacific respectively, are also examples of what can be done, and the savings in fuel and CO<sub>2</sub> that can be made, using the existing technology. In addition to tailored departures and arrivals the aircraft taking part in those trials were fed dynamic weather information, allowing them to alter their route to avoid bad weather and take advantage of winds.

What is remarkable about that is the realisation that this is not the case for all aircraft today. At the moment, aircraft routinely fly for 14 hours with more than 350 lives at stake with exactly the same weather information that you and I use to decide whether or not to take an umbrella when we go to work. And the information is about as up-to-date. But as the test flights have shown, that need not be the case. And it can be done today.

Adopting these sorts of changes will also have capacity implications. There is no reason to continue to use minima and separation standards from 1950. If we updated the standards to what the aircraft can do now, we could significantly increase airport throughput.

That might mean that the current pinch point that is slots is less contentious. That, in turn, might throw the airport debate into a spin. Would the airlines that currently make the occasional windfall gain from the sale of slots be prepared to share that gain with the builders of the slots, in return for guaranteed capacity increases and service improvements?

## **Slots: Time to use or lose the 'Use it or Lose it' rule**

Remember the full service long haul airlines? Whatever happened to them? They used to be everywhere: taking control, dictating terms, running the industry. Now, they just seem to be running scared. Haven't times changed for those once proud titans of the skies?

Whatever happened to their aura of invincibility, their sheer arrogance? Turns out they weren't all knowing, all powerful predators astride the world; the big kid in the playground, afraid of no-one. No, turned out they were bullies. And what was the kryptonite that brought these supermen to the level of Clark Kent? Slots!

Who would have seen that coming? The 'elephant in the room' we called it just last month, and right on schedule the legacy carriers went whimpering around to their parents for protection when the rest of the class fought back. Yes, slots and slot regulation: it's tough out there.

For those with short memories: airline executives perhaps, staff of the European Commission, that sort of person; you might like to go back and check your notes. Just a couple of months ago they were demanding that they be treated like any other industry; that they, and they alone amongst the various parts of the air transport industry, were the truly competitive players. Remember all that?

That would be the same full service legacy carriers that this month petitioned the European Commission to give them relief from the use it or lose rule in slot regulation. Poor loves. Turns out, the rules that they worked so hard to preserve, that they wanted concreted in, need some special tweaking. Not a full change, not a chance for the market to have a real, full blooded attempt to work out what might be the best thing, mind. Just a little tweak.

Not, for example, an opportunity for others to try and open up airports, to try their hand at offering services. In other circumstances, you might be excused for calling that giving the market a chance to work. Granted, suggesting that market forces be allowed to take their course is not popular at the moment, but even so. Unrestrained, unmitigated capitalism is out of favour, sure, but since when has it been agreed that all forms of competition must be taken out the back and put to sleep?

The legacy airlines successfully requested that the current use it or lose it rule (the 80% rule as it is sometimes known – allocated slots must be used 80% of the time or returned to the slot pool) be suspended for two seasons. The Commission agreed.

The reaction has been swift and vocal. The European Parliament was outraged that there was no consultation, to which the airlines replied that the situation was urgent as the planning process was about to commence. That would be a planning process that was foreshadowed about 24 months ago, so that is not a compelling argument.

The second argument that was used was that the world needs long haul, network airlines – there are only so many locations that LCCs can take you to, apparently – and thus it was for Your Own Good. The world does need long haul carriers, and to date, only a widespread network has shown the robustness to generate the traffic required to provide the service economically, but so what?

It is not like the long haul carriers were being told to hand back all their slots, just risk having those that they cannot make economic put back in the pool so that someone else can try to find an innovative way to use it. Who knows, maybe by providing a long haul service? Policies that have as their aim saving any current legacy procedures from the perils of innovation are rarely good policies.

The LCCs were also outraged. Ryanair was so outraged that Michael O’Leary, Ryanair’s motor-mouth CEO, actually went to talk to the Commission about aviation policy. That was a first. Normally he just shouts at them. It was a very cordial meeting apparently. EasyJet was incensed, too, but they are on better terms with the Commission so did not need to smoke a peace pipe to make their point.

It is easy to see why the LCCs were so concerned. When you think about airline models, and which ones are working, there is only so much more scope for the LCCs to fly to regional airports and ignore potential customers. A growing percentage of their passengers are in fact on business. The next move for the LCCs is to take at least a part of their operation into the mainstream. EasyJet already uses Gatwick for example.

That means access to mainstream airports – the very thing that the freeze will not allow. So we are seeing the struggling carriers barring the growing and cashed up carriers from some of the best bits of the playground. In the schoolyard it seems that there is still some work to do to make the sandpit level.

This neatly highlights why the airports are outraged, too. They need passengers to come through their facilities to make money. A freeze on the slot rule stops others from using the capacity that we already have to do exactly that. It also shows the contempt with which the airlines regard the airports.

If you think that this might be somewhat esoteric, think about Rome Fiumicino. The new look Alitalia is only intending to use 400 of the 500 or so slots that it has this summer – and summer is the busy time for Rome. Might others fly in during that period and open up what has been one of the least open and competitive airports in Europe? We will never know.

## **Environment: GIACC soldiers on**

The great and the good again meet at the very start of April in a basement – OK, yes, at a summit, to discuss the industry's approach to the environment debate. The good old 'ICAO, only ICAO and nothing but ICAO' line is looking thinner by the day, but no doubt that will remain the party line.

Unfortunately for the interests of solidarity, a number of players are falling off the band wagon – and starting to argue that it is better to be inside the Copenhagen tent than outside it. BA, Virgin and Cathay signed a pledge to work to that end last month.

Undeterred, ICAO's Group on International Aviation and Climate Change (GIACC) continue to work on. There are a number of issues that need to be resolved, including the fundamental difference of approach between ICAO, where all parties are equal, and the Kyoto Protocol, which recognises the 'common but differentiated' approach. Plus of course, there is the need to square the circle of Europe (and other States') emission trading schemes, with the ICAO principle of unanimous, coordinated action.

The easy thing to do is nothing – exactly what the environmentalists fear. So GIACC is working hard to find middle ground. To do that, they have created three working groups and a meeting schedule that by normal ICAO standards is lightning fast. But, there is only one meeting now left. 'Cautious optimism' is the on-message text that came out of the last round of meetings, in the middle of March. The last meeting is in May.

The timeline for global, aspirational, but non-binding, goals have been agreed – but not the goals themselves. In the drafts, the actual aspirational targets currently remain "X", "Y" and "XX". It has also been accepted, probably, that each State will need to find its own measures to meet international targets – like Europe is doing with the ETS for example – and so much for universal action. That was off-message, so work continues there. The third group, looking at means to monitor performance towards the aspirational goals seems stuck in a logical flaw – how does one measure aspirations? Is that like measuring the ground speed of joy, or the specific gravity of duty? They are standing by to find an appropriate scale for X, Y and XX.

The cautiously optimistic continue to hope for absolute emission reductions from an agreed baseline year, a timetable and binding targets for the sector as a whole before the end of the year.

**For further advice or information on any of these issues please do not hesitate to contact us at [info@aviationadvocacy.areo](mailto:info@aviationadvocacy.areo)**

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