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AIRLINES' COMPETITION ON THE NORTH ATLANTIC ROUTES 1970-1980


by

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A thesis submitted in fulfilment of the requirements for the award of the degree of Master of Philosophy.

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DEDICATION

To my parents
ACKNOWLEDGEMENT

While only one name is shown on the cover of this thesis, one has not to forget that its contents have been formed with much consideration to those who previously contributed to the subject.

My greatest debt is to my research supervisor Mr. A.J. Burkart for his constructive criticism throughout the work and continuous counsel, advise and encouragement. The development of the work owes a great deal to his support, knowledge and experience.

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SUMMARY

In the North Atlantic market, with carriers supplying far more seats than required by the passengers, a situation of over-capacity has been created. This made many international airlines to compete vigorously among themselves to get good share of the market by attracting the maximum number of passengers to fill as many of the empty seats as possible in a desperate move to receive new revenues; but that resulted in a deterioration in their financial results due to low yields and higher costs.

The major aim of the work is to examine the state of competition occurring between international airlines, with many carriers coming to the market bringing or introducing innovative low fares, and to ascertain whether this competition has had any role in causing the over-capacity in the supply of seats and the overall influence on the industry.

The work suggests formulating a remedial action of co-ordination between all those parties associated with the industry to reach a better multilateral understanding build on the optimal balance to serve the interests of all for the best of the whole air transport industry.

The performance of the airlines and their financial stability need some form of regulation in offsetting the results of deregulation and to refrain from extreme system of either way as the unilateral action by one party to impose its own views and practices can prove very difficult for others.
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LIST OF ABBREVIATIONS

ABC - Advanced Booking Charter
AEA - Association of European Airlines, Brussels
APEX - Advance Purchase Excursion
ASM - Available Seat-Miles
ATK - Average Tonne-Km
CAA - Civil Aviation Authority, UK
CAB - Civil Aeronautics Board, USA
ECAC - European Civil Aviation Conference
IATA - International Air Transport Association
ICAO - International Civil Aviation Organisation
ITA - Institut du Transport Aérien, Paris
ITC - Inclusive Tour Charter
OCED - Organisation for Economic Co-operation and Development
OTC - One-stop inclusive Tour Charter
RPM - Revenue Passenger-Miles
TGC - Travel Group Charter
CHAPTER ONE

INTRODUCTION
CHAPTER 1

INTRODUCTION

1.1. AIMS:

The main objectives of this study can be outlined in the following points:

A- To look into one of the most important sectors of the international air transport market that of the North Atlantic.

B- To investigate the state of competition occurring between the international carriers and the unhealthy state of air transport where many airlines are suffering severe financial setbacks especially in the end of seventies and up to this date.

C- To examine and analyze this market by studying all the areas affecting the operation of the participating air carriers and to ascertain whether competition had any significant role in causing the overcapacity and the overall influence of this competition on the industry.

D- To formulate a remedial action which takes into consideration the different objectives of airlines.

1.2. HYPOTHESIS:

Because the interests of the public and private sectors sometimes conflict, there is no one system of airline operation which is applicable to all carriers in the North Atlantic market and this need for an optimal balance which influences the degree of competition between airlines. This is so due to the fact that some carriers are privately owned and the others are partially or wholly controlled by
governments and that international airlines tend to belong to two main streams of thinking one aiming to achieve financial profitability and the other to operate as a public service and to benefit the economy.

1.3. METHODOLOGY:
The work has been progressed by focusing on the theoretical side of the subject, the collection, collection and analysis of the relevant data and last the extraction of the findings, conclusions and recommendations.

The theoretical work is based on giving the reader a complete picture to what the air transport industry, especially that of the North Atlantic, is all about by looking at those areas that constitute and play the major role in determining its shape of existence and its continuity.

The collection of data concerning the operating traffic results for the period 1970-1980 were drawn mainly from the International Air Transport Association (IATA)'s publications, being the most reliable and official source of information in the industry, Institut du Transport Aerien (ITA) an international association that is concerned with all aspects of air transport, and data published by Civil Aeronautics Board (CAB) which relate to the economic regulation and promotion of commercial air transportation within as well as to and from the US. The CAB's main publications include Air Carrier Traffic Statistics and Air Carrier Financial Statistics. The financial data is one source of data by which it enables CAB more
accurate assessment of the economic performance of airlines and in understanding the market environment in which carriers are operating and competing in.

The main journals and trade magazines that were used in the desk research beside the major literatures were:
- Journal of Air Law and Commerce.
- The Aeronautical Journal.
- ITA Study and Bulletins.
- Aviation Week and Space Technology.
- Flight magazine.
- Tourism International Air-Letter.
- Air transport world.
- International Tourism Quarterly.
- Interavia.
- ICAO publications.

A ten years period, 1970-1980, was chosen for investigation and analysis in this study as the airlines in the last quarter of the seventies have experienced some financial difficulties contrary to the early years of the period when the industry was experiencing a considerable growth in passenger traffic and airlines were achieving sound financial results making it very lucrative for new international carriers to join the market.

Also in this period the controversial deregulation approach was introduced in the market following the American Deregulation Act of 1978.
From the initial reading a draft material was prepared on each suggested chapter, then came the stage of collecting the data that concerned the chosen period in which they were tabulated to serve the study. From the analysis of these different tables together with the suggested material of the chapters, the writer was able to reach certain findings, conclusions and recommendations which focused and built to reflect the following:
- The effect of competition.
- The economic difficulties facing the industry.
- The issue of fares.
- The costs factor.
- The political significance of the industry.

1.4. BACKGROUND TO THE MARKET:

The North Atlantic market, connecting North America and Canada with Europe, Middle East and North Africa, which represents approximately one third of the world's international passenger traffic, is such an interesting market that has attracted over forty scheduled international airlines beside many charter air carriers. With this number of competing carriers, the market is having a supply of aircraft's seats much more than required by the passenger demand and so a situation of extra capacity is created. Also it is necessary to mention that some airlines tend to depart the market as they go bankrupt while others come in because they see a potential for profit, therefore we have seen significant entry and exit of carriers. The international air transport industry is going through
severe financial crisis leading in some cases to the withdrawl and ceasing of operation and Laker Airways is only one example of this. The general reasons behind this international confusion and complexity can be attributed to the followings which are interrelated with each other:

1- The existence of large number of airlines.
2- Fluctuating and unstable growth of demand.
3- Intense competition within the scheduled airlines and between the scheduled and charter carriers leading to the availability of extra capacity.
4- The general world economic recession.

The introduction of deregulation and the emergence of many non-scheduled carriers offering low cost fares to the public forced the scheduled airlines with no choice but to compete vigorously to retain their share of the market by introducing their own low promotional fares attracting passengers to fill as many empty seats as possible in desperate move to get new revenues. This lead to a deterioration in the financial situation with less and less profits due to low yields and at the same time higher cost factors.

With the jury's still out, where airlines still face bankruptcy or the threats of bankruptcy taking place, can air carriers survive deregulation, as it exists today, is the biggest concern facing the industry, and there is that question whether governments should have more say in the airlines' affairs and to have some potential regulation.

Facing such a situation, the industry still lacks an important
ingredient in formulating its remedial action that would suit all the participating parties for the benefit and the survival of efficient industry.

1.5. LITERATURE REVIEW:

As the study is looking into such an important issue that has a big role in effecting and shaping the results of air transport industry on such vital and large market that of the North Atlantic, the writer has built his review of the main literature on this subject on the following areas which most of the discussion in the chapters to follow will focus on.

1- The role of the International Air Transport Association in fixing rates and the criticism to this activity mainly by the Civil Aeronautics Board of the United States of America.

2- The issue whether competition and freedom of skies is serving for the benefit of the industry or is it playing part in the deterioration of the financial position of airlines.

3- How crucial is the issue of extra capacity in discussing the above.

On the role of IATA, Richard Chuang and J. Brancker were two main sources who focused in detail on the activity of the Association.

Chuang in his book "A case study of a Quasi-Government Organisation" which is a revised version of his doctoral thesis submitted in 1970 referred to IATA as Quasi-government organisation and explored on the following issues:

A- Delegation of functions to a non governmental organisation on the basis of many bilateral air service agreements and not on the multilateral convention system.
B- The scope of IATA traffic conferences' activities and the politics of government reservations.

C- The nature of IATA resolutions.

D- The impact of a nation's economic philosophy on IATA and the relationship between aviation policy and the overall foreign policy.

Chuang referred to the existence of an inverse relationship between the degree of effective government control over its carriers and the frequency of government disapproval and of government reservations to IATA resolutions and that countries tend to have a negative or unfavourable attitude toward IATA when they support and approve the free enterprise economic policy.

At the same time Chuang refers to the criticism toward IATA by CAB in focusing on two issues one, where fares are high and second, the secrecy and the closed meetings of IATA.

J. Brancker, in his work "IATA and what it does" published in 1977 aimed to show that many activities of the Association achieve its objectives that of benefiting a regular and economic world air transport system by providing a high standard of air transport and making air services available to many people.

The work concentrated mainly on the IATA machinery and conferences and how the consumer benefit out of the facilities provided. Brancker justifies the role of IATA fare fixing and that fares' agreements are subject to government approval and that the actual cost of operation and market conditions are taken into consideration when building these fares.
The International Air Transport Association in a survey conducted by itself "IATA agreeing fares and rates", describes its conference machinery showing the way fare and rate agreements are reached and it explains the reasons behind the implementation of these procedures.

The Association made many interesting conclusions:

1- No single state or airline can enforce its philosophy on international level.

2- The provision of excess capacity has contributed to the financial difficulties of airlines' operations beside that of inflation and rising costs.

3- There is a greater understanding among governments for the need of an international and uniform policy for achieving a coordinated and economical civil air transport.

Mahlon Straszheim and Stephen Wheatcroft have been two main authors who contributed to the subject of criticism of IATA's role.

Straszheim in his book "The international airline industry" in 1969 refers to the Association fare setting process as a value of service pricing system due to the political influence and consideration that these play at time of establishing fares and advocates the introduction of rational pricing.

Straszheim believe that governments tend to give their approval to IATA's rates not because they meet the interest of the traveller and the airline but because the objective of most of these governments' is the interest of their airlines, so
he recommends the need for more government interference and supervision of IATA rates setting but at the same time aiming and asking for price competition.

Straszheim in his paper "The determination of airlines fares and load factors" believes that the ability of IATA to maintain prices well above competition levels for the more efficient carriers leaves the travelling public's interest for lower fares unrepresented.

Straszheim then focused on two main issues:
- Profits are excessive in some airline markets.
- Load factors are too low in some other markets.

He then argues the theoretical solution for the trade-off between scheduled frequency, fares and capacity, and goes to analyse the travel patterns and profit prospects.

Wheatcroft on the other hand has always been an IATA supporter to its fare setting role in being a compromise to achieve the benefit for both the private and the public.

Wheatcroft in his book "Air Transport Policy" published in 1964 has given considerable attention to the importance of IATA's role in stabilizing the market even that he does agree that some IATA fares tend to be build on higher rates due to lack of competition than those fares structured without the existence of its role fare fixing.

Wheatcroft have also examined the reasons for regulating air transport in which he identified the following:
1- The characteristic of the industry of being a Quasi public utility.
2- Free for all could harm the safety of operations.
3- Its importance for national prestige and defence activities.
4- Due to its national economic characteristics only few airlines can operate and that product differentiation is limited. Wheatcroft believes that due to the oligopolistic character of the available carriers it would be difficult to have a perfect competitive market and so unregulated competition is unlikely to achieve the type of air transport development that governments seek and that the scheduled international carriers would be satisfied with.

Wheatcroft then advocates the control of entry and tariffs as an essential framework for the industry but does not believe that market forces should be relied upon exclusively to control the development of the airline industry.

Wheatcroft in a paper "The changing economics of international air transport", presented to the Economics and Finance Council of Air Transport Association of America in USA in 1981, looked at those changes that happened in the international scene, their implications and then referred to the actions needed by airlines to overcome the problems facing the industry.

In this paper Wheatcroft reaffirms his believe in the necessity of some economic regulation in the international air service operations.

He stressed the fact that IATA's Conferences should be maintained when agreeing on fares and rates and at the same time he saw that some changes are needed in its machinery to enable it have a more workable system.
M. Straszheim in his paper "Airline Demand functions in the North Atlantic" examined the demand functions and the price and the income elasticity for the different classes of services in the North Atlantic. He then affirmed that prices play an important role in the development of traffic.

While in his work "The international airline industry", conducted in 1965 in which the data used were for the years 1962 and 1964, Straszheim examined the economic efficiency in evaluating the industry performance and considered the structural changes in the regulatory environment and recommended policies toward improving the performance of the industry.

He also looked at the characteristics of demand and focused on the North Atlantic as one market of case study when discussing the price elasticity within the First class and Economy class services.

A major work on the issue of price elasticity was conducted in 1978 by Wheatcroft "Price elasticity revisited" which examined the many studies made by different researchers on the North Atlantic.

Jesse Friedman prepared his report for British Airways and Pan American "A new air transport policy for the North Atlantic: Saving an endangered system" on the nature of the economic problems facing the world airlines particularly on the North Atlantic market and gave his solutions to these problems. He emphasized on the importance of blending control and competition and the need of accommodating the interests of the scheduled and non-scheduled airlines and the public.
Friedman advocated the reduction or elimination of flight frequencies provided by scheduled operations, the prevention of excess capacity by the non-scheduled operations and also the elimination of barriers to the mixing of both scheduled and non-scheduled passengers on the same flights.

Friedman favours the need for the intergovernmental machinery concerning capacity problems to be on multilateral basis.

On the subject of efficient pricing, Friedman calls for the scheduled carriers to respond to consumer demand and to competitive charter operations by offering discount promotional fares at any margin above the incremental cost, but due to the requirements of healthy competition, this will require fares to be not lower than that necessary to meet the charter competition at the equilibrium.

Friedman goes on to suggest the need that rates for both charter and scheduled services have to be controlled.

As excess regulation is politically out of question, Friedman concluded his work that the only choice is between effective or ineffective regulation and so the crucial fact is that capacity control is the key to remedy the situation on the North Atlantic.

Professor Rigas Doganis, in his article "Air transport — A case study in international regulation ", besides looking into the economic consequences resulting out of the type of regulation available in the international air transport arena, examined the arguments for and against regulation.

He went on to show that there are political constraints which
make it difficult to justify freedom of competition and recommends a revision in the bilateral air service agreements. Doganis in his study "Current trends in the international regulation of air transport" reviewed the existing trends for both deregulation and protectionism and then foresaw the following developments: first, charter services to be included in the bilateral air agreements where their capacity together with that of the scheduled operations will be more controlled and second to bring the tariff of the non-scheduled services within the control of these agreements.

Nawal Taneja in his book "US international aviation policy", published in 1980, examined the importance of IATA's multilateral system in the existing international bilateral regulatory system, the pros and cons of deregulation and the consequences of the US international aviation policy. He also reviewed and analysed the North Atlantic operations for the period 1968-1978 and assessed the results.

Taneja challenged the criticism and allegations against IATA of being anticonsumer and anticompetitive organisation and in contrary believes in the effectiveness of its machinery for the benefit of the consumer and find no alternative system to work much effectively in the public interest. Taneja does not appeal to the free market approach in the pricing structure and advocates the importance of having the international fares controlled by governments.
Richard Smithies in his article "The changing demand for air transport" summarises the international framework behind the changing mix of scheduled and charter service on the North Atlantic.

Smithies believes that the travellers' needs have changed from that of the 1940s and 1950s which made the North Atlantic a mass market in which both scheduled and charter air services are gearing their activities to meet this demand in a complementary shape. So he goes to suggest that regulations and legislations concerning the air policies should consider this change in demand. He has referred to the following as part of the problem existing on the North Atlantic:
- The excess of scheduled services.
- The complicated and unprofitable fare structure.
- The existence of different regulations governing the charter carriers.

Mutti and Murai in their paper "Airline travel on the North Atlantic" focused on the relationship between the passenger demand on the North Atlantic and the market shares. They referred to price levels and exchange rates as two important issues when considering demand on the market.

Cooper and Maynard in their paper "The price of air travel" suggest that there are no convincing evidence that open market and freedom of air will harm the passengers. They go on to recommend, as a reform action, the introduction of regulated competition together with the injection of subsidies by governments to safeguard the continuity of their airlines.
Two books published in early 1960s have given the basic theoretical understanding to the subject of competition and regulation in air transportation.

S. Richmond in 1961 in his work "Regulation and competition in air transportation" looked on the justification of the importance of regulatory air transport and viewed that "unregulated competitive market forces may have adverse consequences for the public at large".

While R. Caves in "Air transport and its regulation" in 1962 shed the light on the advantages of free competition on the US domestic air industry and looked into the policies of Civil Aeronautics Board.

Caves relates both the airline's market conduct and performance to the regulatory pattern and to the economic elements of market structure.

William O'connor in 1971 in his book "Economic regulation of the world's airlines" concentrated on the economic regulation that of the right of carriers to establish service to another country, the control of the frequency of flights and capacity of aircraft and the fares to be charged.

O'connor advocates the idea of having a multilateral system instead of the bilateral. He then looks into the national and international aviation interests and suggests that the best system is that which will promote lower fares, centralize and simplify economic regulation and that seeks the welfare and advancement of the less developed countries and the lessening of international political tensions.
O'connor believes regulated competition is the most desirable system from the standpoint of world public interest and the inevitable and the prevalent system from the political standpoint in the foreseeable future.

One of the genuine and detailed works in air transport conducted in the United Kingdom is the "British Air Transport in the seventies" prepared by the Committee of Inquiry into the civil air transport chaired by Professor Sir Ronald Edwards and presented to the parliament in May 1969.

The aim of this committee, as put by the report, was
"To inquire into the economic and financial situation and prospects of the British civil air transport industry and into the methods of regulating competition and of licensing currently employed, and to propose with due attention to other forms of transport in this country what changes may be desirable to enable the industry to make its full contribution to the development of the economy and to the service and safety of the travelling public".

The report recommended:
1- The establishment of Civil Aviation Authority under which the economic, technological and operational aspects of regulation be brought.
2- The encouragement in the creation of a second force airline.
3- To have a better organised public sector carriers concerned with British scheduled air services and also to involve in charter and inclusive tours.
The report favoured the protection of scheduled services due to their public service characteristic and which, because of its operation at low load factors, will be facing a severe competition from their non-scheduled rivals.

Beside the above three areas that we mentioned, one has to look to one other special subject that of data published by IATA on the different data of the traffic movement being the main source of data.

IATA's Industry Research Division publishes continued data on:
- Passenger numbers (scheduled, non-scheduled, IATA and non-IATA).
- Percentage of growth on previous years.
- Percentage share of the market.
- Seasonality.
- Load factors.
- Passengers carried by airlines.
- Seating capacity offered.
- Fare types.

The main publications on the North Atlantic are:

1- 1978 North Atlantic traffic Report:

The report in its three sections covered three major issues:


B) Analysis of the North Atlantic passenger traffic and capacity by quarter and by direction for the period 1972-1977.

C) Analysis of the North Atlantic passenger traffic by carrier and country for the period 1972-1977.
The main findings of this report were:
1- Seating capacity during the period 1972-1977 recorded a slower development than traffic and both capacity and traffic recorded marked differences in growth rates by quarter.
2- The introduction of non-IATA scheduled Laker Skytrain service at the end of 1977.
3- Both IATA non-scheduled and total charter traffic grew faster than IATA scheduled and the total scheduled traffic for the period 1968-1977.
4- IATA non-scheduled traffic grew at 13.8% per year slower than the traffic growth of the non-IATA non-scheduled of 15.8%.
5- First-class capacity for IATA scheduled services in the period 1968-1977 experienced a growth at an average rate of 3.1% per year while traffic grew at a faster rate of 5.9%. The Economy class capacity grew at the rate of 8.6% per year while traffic growth rate recorded a 7.9% per year.

2- North Atlantic Passenger Traffic Report 1975-1980:
This report monitored the following issues:
- The US deregulation.
- The worldwide economic recession.
- The promotion of low excursion fares.
- The introduction of new scheduled services.
The report recorded data on airlines's results on individual and group basis and on region basis, traffic, capacity and load factors.

3- Analysis of the US international air travel statistics with particular emphasis on the US-Europe markets:
This report published in February 1979 where the figures were based on data collected by the US immigration and Naturalization
service also comprised detailed statistics by US gateways for the different top fifteen European countries, covered the years 1977 and 1978 and made the following findings:
A- The new low fares introduced in 1977 on US-Europe had only a small impact on the scheduled and charter traffic.
B- The UK-US market had a growth rate greater than those of other US-European city pairs.
C- Non-scheduled performance declined in contrast to the scheduled traffic.
D- Non-US airlines reported better traffic share than that of the American carriers.

4- World air transport statistics:
These are annual reports published to cover performance of IATA member carriers. One of the sections that the report deal with and give special attention is the North Atlantic that gives detailed data on the previous years activity on monthly basis.
Starting May 1976 the reports included traffic carried by Concorde as part of the First class figures.
Also starting from 1978 Miami was included in the North Atlantic figures while before it was considered part of the Mid Atlantic operations.

There is one important remark that has to be made with regard the figures published by IATA, where during looking into the figures issued in the Review of the North Atlantic Passenger Traffic Capacity and Load Factors trends referred in (1), we found the average annual growth for the years 1973-1975 in most of the tables to be different than those calculated by us.
Take for example table 1 appearing on page 9 of the Development of total North Atlantic Passenger Traffic: the three IATA growth rates for scheduled, charter and total traffic for 1973-1975 were -6.3%, 16.4% and -6.4% respectively, while in our calculation using the same traffic figures of the same table gave a growth rates of -6.0%, -6.0% and -6.0%. The same can be said about the other tables appearing in the same report.

When contacting IATA- Industry Research Division to explain this difference in growth rates figures, it was understood that IATA growth rates were calculated on original traffic figures but at time of printing the report new traffic figures were recorded and printed instead of the original ones while keeping the growth rates figures without alteration.

Finally, the research will allow the writer first to develop a wider conception of the problems associated with the international air transport industry and principally that concerning the North Atlantic market and second to find relationships in the literature with the study's hypothesis upon which the research work is build on.

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CHAPTER TWO

THE ANGLO-AMERICAN AIR SERVICE AGREEMENTS
2. THE ANGLO-AMERICAN AIR SERVICE AGREEMENTS

2.1 HISTORICAL BACKGROUND:

At the end of the Second World War, in which had the effect of establishing the United States as the world leader in the civil aircraft manufacturing and airline industry with most of Europe having been laid waste, one of the reconstruction programmes was to reestablish a proper world airline system. This was primarily due to the fear of most countries that the USA due to its monopoly position would offer unlimited capacity and exert its powerful air transport strength to acquire world dominance in determining the future of the international air transportation system.

During these years, the USA developed an extensive network of international airline operations, with their carriers having special economic and technical advantages over foreign carriers and possessing equipment and experience far surpassing that of their strongest competitors with a dominant position on the most important of the international routes, the North Atlantic.

After having preliminary conversations bilaterally between the various nations of the world and the USA, the US government then agreed to host an international conference to establish a post-war civil air structure, and to make arrangements to allow international airlines to develop commercial air transportation services through the conclusion of multilateral agreements.
2.2. CHICAGO CONFERENCE:

This conference was held in Chicago on 1 November 1944, in which the representatives of 54 countries attended (table 2.1) with the aim to consider some form of multinational agreement, and where it was proposed that an international regulatory body should be established. Different opinions and interests existed between the strategies of the United Kingdom and the United States delegations. The British fearing a US monopoly stressed the need for regulation in routes, rates and frequencies and favouring an international body to organise control and order in the air; while the US proposed complete freedom in the air with equal opportunity in an open sky for all nations on international routes, where it presumed market forces will determine frequencies and fares.

The conference laid down 5 traffic categories to be considered for international air transport, and formulated the five international freedom rights of civil air transport:

1) The privilege to fly across its territory without landing;
2) The privilege to land for non-traffic purposes;
3) The privilege to put down passengers, mail, and cargo taken on in the territory of the state whose nationality the aircraft possesses;
4) The privilege to take on passengers, mail or cargo destined for the territory of the state whose nationality the aircraft possesses;
5) The privilege to take on passengers, mail and cargo destined for the territory of any other contracting state and the privilege to put down passengers, mail and cargo coming from any such territory. "(1)
Table (2.1)  
Participants at the ICAO Conference 
Chicago 1944

<table>
<thead>
<tr>
<th>Country</th>
<th>Country</th>
</tr>
</thead>
<tbody>
<tr>
<td>Afghanistan</td>
<td>Luxemburg</td>
</tr>
<tr>
<td>Australia</td>
<td>Mexico</td>
</tr>
<tr>
<td>Belgium</td>
<td>Netherlands</td>
</tr>
<tr>
<td>Bolivia</td>
<td>New Zealand</td>
</tr>
<tr>
<td>Brazil</td>
<td>Nicaragua</td>
</tr>
<tr>
<td>Canada</td>
<td>Norway</td>
</tr>
<tr>
<td>Chile</td>
<td>Panama</td>
</tr>
<tr>
<td>China</td>
<td>Paraquay</td>
</tr>
<tr>
<td>Colombia</td>
<td>Peru</td>
</tr>
<tr>
<td>Costa Rica</td>
<td>Philippine Commonwealth</td>
</tr>
<tr>
<td>Cuba</td>
<td>Poland</td>
</tr>
<tr>
<td>Czechoslovakia</td>
<td>Portugal</td>
</tr>
<tr>
<td>Denmark</td>
<td>Spain</td>
</tr>
<tr>
<td>Dominican Republic</td>
<td>Sweden</td>
</tr>
<tr>
<td>Ecuador</td>
<td>Switzerland</td>
</tr>
<tr>
<td>Egypt</td>
<td>Syria</td>
</tr>
<tr>
<td>El Salvador</td>
<td>Thailand</td>
</tr>
<tr>
<td>Ethiopia</td>
<td>Turkey</td>
</tr>
<tr>
<td>France</td>
<td>Union of South Africa</td>
</tr>
<tr>
<td>Greece</td>
<td>United Kingdom</td>
</tr>
<tr>
<td>Guatemala</td>
<td>United States</td>
</tr>
<tr>
<td>Haiti</td>
<td>Uruguay</td>
</tr>
<tr>
<td>Honduras</td>
<td>Venezuela</td>
</tr>
<tr>
<td>Iceland</td>
<td>Yugoslavia</td>
</tr>
<tr>
<td>India</td>
<td></td>
</tr>
<tr>
<td>Iran</td>
<td></td>
</tr>
<tr>
<td>Iraq</td>
<td></td>
</tr>
<tr>
<td>Ireland (Eire)</td>
<td></td>
</tr>
<tr>
<td>Lebanon</td>
<td></td>
</tr>
<tr>
<td>Liberia</td>
<td></td>
</tr>
</tbody>
</table>

The major concern and debate in the conference was on the acceptance of the fifth freedom right, proposing transport between two other countries, with the British leading most of the European nations in opposing it. The other four freedom rights were acceptable to most nations with the first two rights accepted by the majority. The first two rights, called the transit agreements, were thus agreed upon, while the establishment of the last three rights, called the transport agreements, being left for discussion on a bilateral basis as the attempts at a multilateral agreement had proved unsuccessful.

The fifth freedom right remain the only issue not solved and thus became " a stumbling block which finally resulted in the failure of the draft ". (2)

As the Chicago Conference failed to solve the issues of multilateral economic regulation, this left governments and their airlines to face a situation of unregulated international air transport, with differences remaining on international air policy between the Europeans, led by the United Kingdom, at one pole pressing for regulation, and the United States at the other pole asking for freedom of capacity, fare levels and carriage of fifth freedom traffic.

Bilateral negotiations thus became the only means by which commercial freedoms could be obtained.

Out of the Chicago Conference, the following articles should be noticed:

Article 1 retained and restated the 1919 Paris Convention in which " the contracting states recognise that every state has
complete and exclusive sovereignty over the airspace above its territory " (3), and it is this that gives the conference the importance it still holds in the industry even in our present days. It follows from the principle of airspace sovereignty that every state is entitled to regulate the entry of foreign aircraft into its territory and that persons within its territory are subject to its laws.

Article 6 indicates that the convention is concerned only with scheduled air services, this being the only type of service that would be made available to the public, no forecast was anticipated for the existence of charter services, and the article states that " no scheduled international air service may be operated over or into the territory of a contracting state without its previous consent " . (4)

While article 77 states " aircraft have the nationality of the state in which they are registered " except in case of aircraft operated by international operating agencies where joint operating organisations were permitted, and that no aircraft could be validly registered in more than one state. (5)

Following the Chicago Conference, air carriers from 31 countries agreed in Havana in 1945 to establish the International Air Transport Association. Its membership open to airlines operating scheduled air services, with main function to regulate international air transport concerning both rates and service conditions, and it was generally accepted that control of international fares was in the public interest, and also for the benefit of the airlines in protecting the industry from price-cutting warfare.
2.3. BERMUDA AIR SERVICE AGREEMENT 1:

In 1946, at the invitation of the United Kingdom government, U.K. and U.S.A. representatives met in Bermuda to negotiate all the disputed issues between the two countries following the failure of the multilateral approach.

At this stage the interests of the two nations differed considerably and the US carriers possessed far more equipment and experience in the international aviation scene than their competitors including the United Kingdom. At this meeting the two sides arrived at a compromise whereby each nation granted to the air carriers of the other the rights to operate through their own airspace and to land for non-traffic purpose.

The two nations also gave each other the right of entry and departure to embark and disembark traffic in the territory of other, but this was to be valid only for airports named, and routes generally indicated, with the restrictions that the government should approve rates and nominate adequate capacity.

The dominant features of the agreement was that airlines were left free to operate services at the frequency and capacity they considered justified and the parties remained free to designate more than one airline on any particular route, where fair and equal opportunities were given for carriers of the two countries to operate any route between their territories and to provide air transport facilities to match public needs.

The agreement introduced a system of controlled competition with airlines having a "fair and equal opportunity" to operate services with the primary objective of the contracting parties to provide capacity "adequate to the traffic demands between the country of which such airline is a national and the countries of ultimate destination of the traffic". (6)
By the agreement, following the failure of the countries present at the Chicago Convention to find a practical way in solving the issues of fares control, fares and rates were to be set by the airlines of the two countries through the machinery of the International Air Transport Association with the two governments having the final say as they have the power to reject any fare they disapprove before coming into force.

One important fact to be noted is that capacity and frequency principles agreed upon in Bermuda differed from what the UK had previously advocated at Chicago Convention of predetermination of capacity needed to meet the traffic demand, while the new agreement associated with principles of ex-post facto review provided that services especially primary traffic that of third and fourth traffic of one party do not affect the services of the other party.

The agreement served as model and pattern that proved of lasting significance to all air transport agreements subsequently to be concluded between the two countries, and even between other countries in the years to come, where many of the bilateral air agreements reached at the present time are either based on the Bermuda agreement provisions or are very similar in character.

2.4. BERMUDA AIR SERVICE AGREEMENT II:

In early seventies, with the emergence of excess capacity leading to a serious waste of resources resulted in higher passenger fares and damage to airlines, the United Kingdom
asked for both capacity control by governments and a reduction of fifth freedom rights of United States' carriers beyond London, while the United States remained in favour of Bermuda I principles and sought a better share of the market.

In June 1976, The British expressed their discontent with the Bermuda I agreement and the UK government gave one year notice to cease service unless a new agreement was reached. The UK objective behind this renegotiation of the Bermuda I agreement as put by the UK chief negotiator W. Shovelton focussed on the following:

" - to improve balance of the agreement, particularly by opening up new gateways for our own airlines in the States.
 - to set up a form of capacity rationalization across the North Atlantic which would help to save the waste of resources and fuel occasioned by the over-provision of seats on these routes and so help to maintain fares or, if possible, lower them.
 - to reduce and make more equal the fifth freedom opportunities available to each side.
 - to get a sizable share of services into Gatwick as well as Heathrow.
 - to improve the tariffs clauses.
 - to secure a clearer, more comprehensive and up-to-date agreement. " (7)

Also one has to refer to the imbalance in earnings between the airlines of both countries that existed at that time as a result of the first Bermuda agreement, where the British
carriers had an earning of £127 millions compared to £183 millions for the American carriers for services on the North Atlantic as per the figures released in 1976 by the United Kingdom Department of Trade (table 2.2).

In 1977 the governments of both United Kingdom and United States concluded the Second Bermuda air service agreement, which came into force on 23 July 1977 to replace the 31 years old Bermuda I agreement.

This new agreement provided a new and, complicated mechanism for certain routes especially the major transatlantic ones. A feature of the agreement was that twice a year each country's carrier would file its proposed scheduled services with the government of the other country, allowing, in the case of objection by one of the parties, for consultation to agree on frequencies. In other words the airlines were allowed to decide the capacity and the number of scheduled flights they wished to operate but the foreign government has to approve them before operation as has the right to challenge the submitted capacity and frequency, but neither government has the right of veto over capacity.

Another feature of the agreement was that a two year period was given to an airline entering certain permitted routes with no capacity or frequency controls allowing it to compete with the already existing airlines.

As the United States used to insist that bilateral agreements permit multiple designation without limitations on the number of airlines on any route, the second Bermuda agreement was
# Table (2.2)

## EARNINGS ON ROUTES BETWEEN UK & USA

<table>
<thead>
<tr>
<th>ROUTE (both ways)</th>
<th>ANNUAL EARNING (£ millions)</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>UK</td>
</tr>
<tr>
<td>North Atlantic (UK-USA)</td>
<td>127</td>
</tr>
<tr>
<td>Hong Kong to/ from USA</td>
<td>No service</td>
</tr>
<tr>
<td>Bermuda &amp; other dependent territories to/ from USA</td>
<td>3</td>
</tr>
<tr>
<td>Fifth freedom beyond USA</td>
<td>No service</td>
</tr>
<tr>
<td>Fifth freedom beyond UK</td>
<td>--</td>
</tr>
<tr>
<td>Fifth freedom beyond Hong Kong</td>
<td>--</td>
</tr>
<tr>
<td>Total Earnings</td>
<td>130</td>
</tr>
</tbody>
</table>

a departure from the idea of designating an airline to a specific route.
The only routes where the number of airlines was limited were the transatlantic services, where para 2 of article 3 of the agreement designated only one airline on each route except for two specified routes that of New York-London and Los Angeles-London. While other transatlantic routes would be served by one carrier from each country, a second airline may be added if the total traffic of both countries reaches more than 600,000 passengers one way per year for two years running, or if one airline's traffic on a route exceeds 450,000 passengers one way in a year for two consecutive years.

On the subject of the fifth freedom, the American gave up this right on 22 cities from Britain to Belgium and Austria in three years time and to Holland, Sweden and Norway in five years, none of which was served at that time, but the US gained unlimited rights beyond London into Europe (for details of these routes refer to Appendix II).

As a result of this agreement, the number of gateways available to airlines from each country were increased, where British Airways, Laker, British Caledonian, Delta, Northwest, TWA, Braniff and Pan American were having new opportunities of service, where four new cities in Britain being served by US airlines and British carriers having four new cities in the United States.

The airlines of both parties were given a fair and equal opportunity to compete with each other with tariffs to be set at a rate giving adequate return based on "the costs of
providing such service assuming reasonable load factors " (8) and required that tariff filings be submitted well in advance before coming into effect.

This agreement in summary achieved a certain amount of liberalization, but remained in general somewhat more restrictive than the old Bermuda agreement, and ultimately led to the availability of lower fares on the North Atlantic and more substantial change in how frequency and capacity were to be regulated on services between the two countries (Appendix III refers to Article 11 of the agreement on the subject of "Fair Competition ").

Even that Bermuda II agreement was considered by the Americans to be restrictive, particularly with the barriers to fifth freedom and capacity clause, it was considered the best reward for those advocating low fares and as Nawal Taneja phrased it "since Bermuda two agreement was responsible for bringing Laker in the market in the first place, much of the credit for lower fares should go to Bermuda II ". (9)

Finally one must remember that with the anti trust laws in America, the US bilateral air agreements concluded with other countries in the years to follow Bermuda II tended to be more liberal, table 2.3. refers to these new agreements signed by the US with few European countries.

2.5. BERMUDA AGREEMENT II REVISIONS:

In accordance with article 18 of Bermuda II agreement, the first revision came into force on 1 April 1978 to replace article 14 of the original agreement. This revised agreement
<table>
<thead>
<tr>
<th>Country</th>
<th>Date of Agreement</th>
<th>Liberalization of Airlines</th>
<th>Elimination of Restrictions</th>
<th>Liberalization of Charters</th>
<th>Foreign Competition</th>
<th>Additional US Gateways</th>
</tr>
</thead>
<tbody>
<tr>
<td>Belgium</td>
<td>31.3.1978</td>
<td>Yes</td>
<td>Yes</td>
<td>Yes</td>
<td>Yes</td>
<td>Yes</td>
</tr>
<tr>
<td>Germany</td>
<td>1.11.1978</td>
<td>Yes</td>
<td>Yes</td>
<td>Yes</td>
<td>Yes</td>
<td>Yes</td>
</tr>
<tr>
<td>Netherlands</td>
<td>1.11.1978</td>
<td>Yes</td>
<td>Yes</td>
<td>Yes</td>
<td>Yes</td>
<td>Yes</td>
</tr>
</tbody>
</table>
was concluded separately and focused on the issues of charter services; it was agreed that the country’s rules will be applicable with the control over the price of charter flights rested with the country in which the flights originates. This revision provided for each country to designate an unlimited number of charter carriers with fair and equal opportunity prevailing when competing between themselves. The second revision came when in Washington in March 1980 the negotiators of both countries agreed to revise the original agreement; this resulted in the British claiming to have successfully negotiated controlled liberalization in the face of strong US pressure to remove almost all controls from the North Atlantic. The new revisions gave reasonable satisfaction to both countries even though not all of their demands were accepted by the other side. The new changes created 12 new US gateways from London and allowed both countries to nominate six new US gateways each in the 1980-1985 period. The amendments allowed the country which nominates a new US point to protect its own airline for three years without any competition from the other country's carriers. Also in addition to the existing cities, New York and Los-Angeles, two new US gateways, Boston and Miami, were allowed a dual designation by each country that could be served by two carriers from each country on flights from or to London. The US also agreed to use Gatwick airport for all new US-London services.
No agreement was reached on charter flights and the United States was denied fifth freedom rights for services through United Kingdom to Europe and the far east except for Glasgow, Prestwick and Oslo, and the United Kingdom was not permitted fifth freedom (cabotage) rights within USA on some direct flights from or to London.

By the revision in agreement both countries agreed that the mutual policy of promoting low fares could be continued while at the same time allowing for the virtual deregulation of UK-USA air cargo by the year 1985.

Finally it is important to note that with the new Bermuda agreement and its revisions on routes between United Kingdom and United States there is, beside frequency of services, a high degree of product and pricing freedom.

2.6. INTERNATIONAL CIVIL AVIATION ORGANISATION (ICAO) :

The great achievement of the Chicago Conference was the establishment of the International Civil Aviation Organisation, which was later to become a specialized agency affiliated to the United Nations.

One of the most important functions of ICAO, formally established on 4 April 1947, is the preparation and the periodical revision of international standards and recommending practices relating to civil aviation. It does much to standardise aeronautical regulations throughout the world.

Article 44 of the Chicago Conference sets the objectives of the Organisation as follows:

1- to ensure the safe and orderly growth of international civil aviation throughout the world.
2- to encourage the arts of aircraft design and operation for peaceful purposes.
3- to encourage the development of airways, airports and air navigation facilities for international civil aviation.
4- to meet the needs of the peoples of the world for safe, regular, efficient and economical air transport.
5- to prevent economic waste caused by unreasonable competition.
6- to ensure that the rights of contracting states are fully respected and that every contracting state has a fair opportunity to operate international airlines.
7- to avoid discrimination between contracting states.
8- to promote safety of flight in international air navigation.
9- to promote generally the development of all aspects of international civil aeronautics. (10)

The Organisation has an Assembly, which is its sovereign body meeting every three years, while the Council is the governing body having judicial powers whereby it excercises a role of mandatory arbitration in disputes between member states which among other things adopts the annexes to the convention and have an Air Navigation Commission; an Air Transport Committee; and a legal committee. Each state member of the Organisation has only one vote even if it has more than one scheduled service carrier, and here the USA serves as a good example.
In 1947 there were 26 ICAO member states while 148 states, excluding the USSR and China, now are members of it and adhere to the Chicago Conference.
The Organisation has always shown its preference for multilateralism and support for the machinery of IATA.

In its Second Special Air Transport Conference, which took place in Montreal, the Organisation recommended that the worldwide multilateral machinery of the IATA traffic conferences be adopted as the first choice when establishing international fares.

To conclude this chapter, it is necessary to mention that in the US where less protective measures were taken by the CAB, liberalisation of air transport regulation began in 1977. Through its market power and via bilaterism, the United States attempts to achieve an international aviation free market. Turning away from protective approach, the US international aviation policy moved toward less restrictive and competitive environment. With the application of deregulation, airline management decisions on such matters as route entry and pricing were no more determined by the CAB where discounts up to 50% were allowed and even later airlines were given complete pricing freedom.

Deregulation place maximum reliance on the competitive forces of the airline market place and allows new and existing carriers to rapidly enter new markets beside sanctioning secondary airports to the major ones.

Finally, under the US deregulation policy, the US Administration has been trading new routes and gateways to foreign airlines in exchange for lower fares and a more competitive situation.
REFERENCES:


4- HMSO, ibid. PP. 7.

5- HMSO, ibid. PP. 24.


CHAPTER THREE

THE INTERNATIONAL AIR TRANSPORT ASSOCIATION
CHAPTER THREE :

3. THE INTERNATIONAL AIR TRANSPORT ASSOCIATION

3.1. INTRODUCTION:

In April 1945 after the Chicago Convention, 31 international carriers, whose countries were members of the International Civil Aviation Organisation, met in Havana and established the International Air Transport Association (IATA) and later in September 1945 the Association was incorporated by an Act of the Canadian Parliament. (1)

The Association had originally been formed in August 1919 in the Hague by airlines of six European countries: Holland, United Kingdom, West Germany, Sweden, Denmark and Norway under the name of the International Air Traffic Association with the objective of making air transport more convenient to the public together with the view of co-operating for mutual advantage to prepare and organise international air traffic, but at that time had nothing to do with fixing fares and rates. (2)

The new IATA was formed for controlling competition by regulating fares and tariffs of the international air transport activities, ensuring similarity of service standards, and having world wide machinery in promoting co-operation between the airlines in legal, traffic, financial and commercial fields. It was only when bilateral agreements became the norm, after signing Bermuda I agreement by the United Kingdom and United States in 1946, that the IATA machinery was given its role of fare fixing.
In the last decade the Association has been under lot of pressure from the new comers to the industry i.e. the non-scheduled operators who are making their way into the mass air service market, but has been successful in its attempts to control the development of these non-scheduled services by influencing governments' legislation, which have led to the classification of just four types of charter services, these being the Single Entity Charters, Affinity Group Charters, a separate fare carriers either to establish their own charter services outside the IATA machinery, or to implement special promotional fares to meet this competition from the charter carriers.

The IATA's member airlines have had a big share in carrying passengers, with the North Atlantic market being a good example where total number of passengers carried by IATA carriers for both scheduled and non-scheduled services in 1970 was 8 million reaching 15.4 million passengers in 1979 with the figures for 1980 being lower than those of 1979 mainly because Pan Am was classified as a non-IATA carrier due to the Show Cause Order of 1978 introduced in USA; chapter nine refers in detail to this subject.

3.2. IATA MEMBERSHIP:

The Association has a voluntary membership open only to airlines operating scheduled commercial services with two types of membership available: either as Active member or Associate member with the former applicable to airlines, whose country of registration is a member of ICAO, operating
international scheduled services with full membership's authorities and rights, while the latter type is open to domestic airlines operating scheduled services.

One important difference between the two types is that the Active members have voting rights in traffic conferences and other meetings of the Association while the Associate member has no right to vote.

Of the 110 Association's members in 1981, shown in table 3.1 there are two British carriers: British Airways and British Caledonian, and six American carriers: Braniff, Eastern, TWA, American, United and Pan American (National was merged with Pan Am) operating scheduled services on the North Atlantic between United Kingdom and United States.

Non-scheduled passengers are also carried by Pan Am, TWA and British Airways but at much lower rate.

One of the founders of IATA, Pan American resigned in March 1979 from its membership after the introduction of the Show Cause Order in 1978, mentioned earlier, where Pan Am was not prepared in participating in the rate and fare fixing activities of the Association conferences, but the carrier rejoined IATA on 1 April 1981.

Membership of any airline can be terminated by the Association when the airline breaches any article or fails to comply with the Association's procedures, or when the country's membership to which the airline belongs is terminated from ICAO.
### Table (3.1)
**IATA Membership as at 1 April 1981**

#### Active Members (93)
- Aer Lingus
- Aerolineas Argentinas
- AEROMEXICO
- AVIANCA
- Air Afrique
- Air Algeria
- Air Canada
- Air France
- Air Gabon
- Air Guinee
- Air India
- Air Malawi
- Air Mali
- Air Malta
- Air Mauritius *
- Air New Zealand
- Air Niugini
- Air Pacific *
- Air Tanzania Corp.
- Air UK *
- Air Zaire
- ALLA
- Alitalia
- American Airlines *
- Angola Airlines
- ARABIA *
- Ariana Afghan Airlines
- Austrian Airlines
- AVIANCA
- Braniff International *
- British Airways
- British Caledonian
- Cameroon Airlines
- CSA
- MEXICANA
- CP Air
- Cruzeiro do Sul S.A. *
- Cubana
- Cyprus Airways
- Deutsche Lufthansa
- Eastern Air Lines *
- Ecuatoriana
- Egyptair
- El Al
- Ethiopian Airlines
- Finnair
- Flying Tiger **
- P.N. Garuda Indonesian Airways
- Ghana Airways
- IBERIA
- Icelandair
- Indian Airlines
- Iran Air
- Iraqi Airways
- Japan Air Lines Co.
- JAT
- KENYA Airways
- KLM
- Kuwait Airways
- LADÉCO *
- LAN-CHILE
- LAB *
- Libyan Arab Airlines
- LOT
- Middle East Airlines
- Nigeria Airways
- Olympic Airways
- Pakistan International Airlines
- Pan American *
- Philippine Airlines
- LACASA *
- PLUNA *
- Qantas Airways
- Royal Swazi National Airways *
- SABENA
- Saudi Arabian Airlines
- SAS
- SOLAIR *
- South African Airways
- Sudan Airways
- SWISSAIR
- Syrian Arab Airlines
- TMA **
- Trans World Airlines *
- BWIA International *
- Tunis Air
- Turkish Airlines
- UTA
- United Airlines *
- VARIG
- VIASA
- Zambia Airways

#### Associate Members (17)
- AEROCOR
- Air Liberia
- Ansett
- VASP
- Quebecair
- Trans Brasil
- Namib Air
- TALAIR Pty. Ltd.
- IPEC Aviation
- Kendell Airlines
- Mount Cook
- Douglas Airways Pty. Ltd.
- Trans Australia
- Masling Commuter Services Pty. Ltd.
- Commercial Airways (Pty.) Ltd.
- Eastern Provincial Airways
- East-West Airlines
- * elected not to participate in Tariff Cord.
- ** Cargo Tariff Coordination.

Source: IATA Publication
3.3. IATA MACHINERY:

The Annual General Meeting (AGM) is the central decision making body and the overall authority of the Association in running its activities and formulating its structure that takes place in the late summer of each year. According to Article VIII of the Association, the AGM has the functions of electing the president and members of the Executive Committee who control and supervise the affairs of the Association, pass the accounts of the previous year and approve the next year's budget.

The Director General, together with the Secretary and the Treasurer who are elected by the Executive Committee, perform and exercise the daily activities of the Association.

The Executive Committee, which has 21 members elected by the AGM from the Active members, appoints five standing committees to which it delegates the power to help perform its duties and functions.

These committees are the Traffic Committee, which has close relationship with the traffic conferences, the legal, medical, financial and technical committees, with membership in these committees open only to Active members. (3)

3.3.1. IATA TRAFFIC CONFERENCES:

In December 1945 at the first Annual General Meeting, the Association adopted the resolutions of "Provisions for the Regulation and Conduct of the Traffic Conference" whereby the conference machinery was to be based on nine regions covering most areas of the world, but because it was difficult
to establish fares for all the areas at the same time, a
new arrangement of area divisions was reached that has
been maintained up to our present day.
These new area divisions, called Traffic Conference Areas
are as follows:
1) Traffic Conference Area I (TC1): which deals with the
western Hemisphere consisting mainly of North and South
America and nearby islands.
2) Traffic Conference Area 2 (TC2): which involves Europe,
the Middle East, and Africa.
3) Traffic Conference Area 3 (TC3): which deals with all the
remaining parts of Asia, Australia, New Zealand and the
Pacific Islands.
Beside these main conference areas there are few joint areas
which deal with international traffic between two or more
of these main areas:
- Joint Traffic Conference, dealing between area 1 and 2(JT12).
- Joint Traffic Conference, dealing between area 2 and 3(JT23).
- Joint Traffic Conference, dealing between area 3 and 1(JT31).
- Joint Traffic Conference that deals with routes all around
  the world (JT123).
Then these seven area traffic conferences are divided into
54 sub-areas to meet local market conditions in these small
areas; these sub-areas which are sometimes called negotiating
areas are as follows:
- Within TC1: 1) USA/Canada/Mexico
  2) North America-Caribbean
  3) North America/Caribbean-Central/South
   America and within America.
- Within TC2: 1) Within Europe.
   2) Europe-Middle East.
   3) Europe/Middle East-Africa.
   4) Within Middle East.
   5) Within Africa.
- Within TC3: 1) Indian Sub Continent.
   2) South East Asia.
   3) South West Pacific.
   4) Japan and Korea.

The traffic conference is the forum in which the industry's pricing decisions are made. The meetings of these traffic conferences usually take place annually in September-October for passenger traffic and in April-May for cargo traffic. Membership of the traffic conferences is compulsory for all Active members of the Association who operate international scheduled flights within a particular area or areas, but if a carrier operates international services in more than one area then it is allowed to participate in the traffic conferences of these other areas but only as a non-voting member, while has the right to one vote in its own area. Members are to adhere to the resolutions which must be agreed unanimously, and which are subject to their governments' approval. It is this unanimity factor which gives the right of veto to an individual member and so the interest of each carrier is thus safeguarded and no one is left outvoted. Beside catering and maintaining international tariff framework, the traffic conference develops documents and control air transport tickets, Airway Bills and unified reservation and handling procedures, with the aim of establishing quick
interline bookings and connections. The conferences also play a large role in connecting the domestic and international routes between different countries.

At the 1978 Annual General Meeting of the Association in Geneva, it was decided to implement a plan which had been developed by a specially formed task force, which allowed members of the Trade Association the option of participating in tariff coordination. The Trade Association attracts and appeals to the entire international air transport community. Following this, the Civil Aeronautics Board in USA decided in October 1979 to grant approval for its international carriers to participate as trade members.

The Trade Association is involved with the daily operations of an integrated world air transport network concerning technical, legal, industrial research, traffic services, governmental affairs and policy coordination, agency, financial and public information. While the Tariff Coordination of IATA deals with fares, rates and levels of commission on agency sales.

3.4. IATA AND THE CAB:

It was only at the Bermuda Conference that the US government changed its position from that of free fare fixing to that of allowing fares to be agreed and set internationally. The US government had to accept and approve the machinery of IATA mainly because it found that this was the best way in which international fares would be kept under its indirect control; while the CAB had authority only over US domestic
fares as any control over international air fares was excluded from its power according to the civil Aeronautic Act of 1938. The US government reluctantly accepted the UK proposal of indirect control of rates by IATA; there had been some division within the CAB itself on this issue and no alternative machinery of rate control was available to the CAB. So while accepting IATA's authority the CAB insisted on allowing itself room to retreat from this international machinery whenever alternative means might be found. The CAB's approval of IATA's machinery had to be renewed annually until 1955 when it gave IATA its permanent approval, but the CAB once again showed its reluctance when in June 1978 passed its Show Cause Order against the Traffic Conferences of IATA, in which the CAB announced that it would henceforth withhold approval from these traffic conferences and their related agreements as they were deemed not to be in the public interest. With this warning the CAB announced that it would withdraw immunity, required under the Anti Trust Laws, from any US carrier that might object to this order and insist on participating in the Traffic Conference. Then in September 1979 the CAB changed this position and decided to limit its warning to cover only tariff coordination on US-Europe operations. The CAB in April 1980 published a new document in which agreed to approve the Traffic Conference system and continued to exempt the conferences from Anti Trust legislation for a period of two years on these conditions:
1- That its own representatives were to attend, as observers, those conferences in which United States was involved.
2- The CAB prohibited participation by US airlines in the meetings of the Traffic Conferences that deal with traffic between Europe and USA.

As for IATA's position vis-a-vis these new developments, it continued to disapprove the CAB's arguments and justifications, especially its discrimination against the North Atlantic routes and the two years period to which CAB approval was subject to.

One of the possible reasons for the hostile position taken by the CAB toward IATA is to its lack of power to fix the fares of its international carriers especially as it disapproved the fares reached by IATA, even though the Bermuda I agreement in its Annex 2 gives a set of alternatives as substitute procedures to be used when there is disagreement to IATA's machinery. These procedures were designed for the event that the IATA's conference is unable to agree on a rate or, no IATA machinery is applicable or, if approval for IATA's decisions is either withdrawn by one party or not renewed.

The granting by many governments to IATA the power to fix fares did not give any guarantee that these governments accept or would continue to accept the rate agreement with the Miami and Chandler meetings being two well known occasions when American government did not accept the fares agreed by IATA.

**MIAMI MEETING:** Following the IATA meeting at Miami in 1955, where a 10% increase on First class fares was agreed instead
of the original proposed luxury surcharge to be effective from October 1956, the US government sought a reduction in Tourist fares and did not accept the agreed increase on First class fares; this led to the holding of a special conference to solve the problem, which at last resulted in a compromise by accepting the fares agreed at Miami to be effective but only valid up to the end of March 1958, while a reduction of 20% in Tourist fares was allowed.

**CHANDLER MEETING:** At the Chandler meeting in 1962 the IATA traffic conference decided to adjust the round trip discount from 10% to 5% on the North Atlantic services. This decision was rejected by the CAB and later by the Canadian Air Transport Board as well. The CAB asked US carriers not to implement this proposed fare increase but to continue charging the old fare. The European position clearly opposed the Americans and later the United Kingdom threatened to take action against US carriers by not granting them landing rights and to impose penalties, it even went so far as to threaten to detain aircraft if necessary. In the end after several unsuccessful discussions, and to avoid this critical international embarrassment, the US government reluctantly had to ask the CAB to accept the proposed increases and to allow as a compromise a 5% discount to be implemented for about one year up to 31 March 1964 and to arrange a further conference to take place in the fall of 1963 to review the entire fare structure commencing 1 April 1964. (4)
3.5. IATA'S CRITICS:

As each airline has its own policies, it is difficult for the Association to agree on a single policy that will suit them all without making some parties dissatisfied in one way or another. It is for this reason that IATA has come under much criticism.

One accusation against IATA has been that it eliminates competition between airlines because of its role in fixing tariffs, but IATA has never really fixed fares, it only recommends fares to governments to be implemented by airlines. The American Civil Aeronautics Board has been one of IATA's harshest and most intransigent critics. Secor Brown, CAB's chairman, addressing the Royal Aeronautical Society, described the Association as being "the vice of market containment rather market development". (5)

The CAB bases its accusation on the ground that rates are set at the high cost level of uneconomical or inefficient airlines. In response to this, one may look at IATA's figures (figure 3.1) where the average Economy fare for the period 1970-1980 has been increasing at a lower rate than that of the consumer prices calculated on the OCED weighted composite index for USA, Canada and Western Europe.

On this subject, Nawal Taneja has in fact shown that for the years 1968-1978 the average Normal fare increased by less than 40% compared to an increase in consumer price index of over 100%. (6)

Other arguments have been taking place concerning IATA's function as a carter organisation in which fares are set for
NORTH ATLANTIC FARES COMPARED TO THE CONSUMER PRICE INDEX
1970 - 1980

Note: An OECD weighted composite price index for the U.S., Canada and Western Europe.

the airlines' benefit.

Rigas Doganis has charged the Association with being a suppliers' cartel, with the aim to maximise its members' profits by fixing fares around the cost levels of its least efficient members by that protecting unsatisfactory performers and giving the greatest possible return to those doing well. On the other hand most carriers usually bargain for a fare based on their demand and cost curves. It appears furthermore that most governments concerned have insufficient information on which to question their airlines and IATA on these agreed fares, and are thus put into the position of having to approve IATA's fares automatically. (7)

On the secrecy aspect of the IATA conferences, Cooper & Maynard charge the Association with being a producers' cartel whose members meet secretly behind locked doors deciding fares in a unanimous way which all must agree; they then ask "what remains of competition" after all that? (8)

D. Corbett blames the unanimity rule of IATA because it gives the small and weak carriers the power to veto the larger and more efficient airlines' efforts to reduce fares. (9)

IATA however has never been short of advocates, Swissair's president Dr. Walter Berechtold, in a speech delivered in 1962, rebuffed the critics and asserted that even the efficient carriers could have done much better and achieved better financial results than were doing currently; he noted that IATA set the fares around the costs of the inefficient carriers, but felt the whole industry benefitted from that and then the situation spoke for itself. (10)
The International Organisation of Consumers Unions, representing consumers' interests, in its paper presented to the United Nations in June 1970, criticised IATA for being "a mechanism for the elimination of competition in air fares" while suggesting that the system of fixing fares should be "more responsive to the consumer interest". (11)

In contrast, Mahlon Straszheim (12) suggested that to accuse IATA of being a private cartel is not a valid criticism; he blamed governments for inadequately supervising their rate making operations.

These remarks were made in reply to the CAB chairman's speech, given to the International Club in Washington following Athens Meetings of IATA in 1965, in which the chairman criticised the Association of lacking persuasive power, for being ineffective, and for allowing prolonged fighting among its members.

Straszheim did however at the same time defend the CAB's role, as being a representative of government, charged with protecting public interest in the USA while airlines are private; he felt that this led inevitably to a conflict of interests; but airlines of other countries and their aviation authorities tend to have similar interests and objectives as they are usually both government controlled.

In reply to these allegations and other accusations of IATA's ineffectiveness, the Association's previous Director General Sir William Hildred (13) defended its machinery in his speech at the 12th Annual General Meeting in Edinburgh in 1956. Hildred drew a complete picture that left the critics with nothing on which to base their campaign to replace IATA with
some other system that would be more acceptable and workable for all parties, while at the same time giving the public what they wanted.

Sir Hildred puts the following points in defence of IATA:

"Whereas a cartel is designed for the benefit of a few, IATA has not limited its membership;

Whereas a cartel stifles competition, IATA members engage in a wide variety of competition, between themselves, with other scheduled operators who are not members of IATA, with non scheduled operators and surface carriers;

Whereas a cartel divides the market, IATA has nothing to say about the market, routes are designated by governments;

Whereas a cartel controls production, IATA can say nothing about frequencies or capacities or the type of aircraft to be used;

Whereas a cartel fixes prices, IATA can only make recommendations in respect of international fares and rates;

Whereas a cartel operates behind closed doors, IATA operates openly, its recommendations are formal and written and must be approved by governments."

The ICAO assembly in its support for IATA against the CAB Show Cause Order recommended:

"1- When establishing international fares and rates, the worldwide multilateral machinery of IATA should be adopted as a first choice and carriers should not be discouraged from participation.

2- The entire international aviation community should
participate in the examination of any system for the 
multilateral establishment of international tariffs.

3- Any unilateral action by governments which may have a 
negative effect on carriers' efforts toward reaching 
agreements should be avoided.

4- That international tariffs should be established 
   multilaterally and done so regionally, the worldwide 
   system should be considered. " (14)

Stephen Wheatcroft, advocates the importance of IATA machinery 
and argues that it is " a reasonable compromise between the 
interests of the travelling public and the economic health 
of airlines " and stresses that the IATA system does not allow 
prices to be fixed on a monopolist approach as its agreements 
do not restrict capacity, and its decisions are reached through 
a unanimity rule. (15)

The Edwards Report, issued in 1969 in the United Kingdom, 
reinforced the position of IATA, and felt that no workable 
alternative to the regulation of international fares and rates 
through the traffic conferences of IATA had yet been devised.(16)

In conclusion, with the heterogeneous type of market in which 
airlines are operating in, one can say that no one system would 
seem acceptable to all, and until more effective procedures 
or systems have been introduced or suggested to replace IATA, 
the international air community must adhere to it and enforce 
its regulations for the good of all its members.
REFERENCES:


3- Brancker, J.W. ibid. PP. 15.


11- Smithies, R. op. cit. PP. 233.

12- Brancker, J.W. op. cit. PP. 139-140.


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CHAPTER FOUR

THE CIVIL AVIATION REGULATORY BODIES IN UK & USA
CHAPTER FOUR

4. THE CIVIL AVIATION REGULATORY BODIES IN UK AND USA

4.1. INTRODUCTION TO CIVIL AIR TRANSPORT:

The civil air transport system makes a vital and irreplaceable contribution to the development of a country's economy because of its importance in such areas as employment, balance of payments, foreign trade, communication network and tourism.

The importance of air transport industry for each country could be derived from the objectives it sets out to achieve. In setting the objectives of air transport, the following issues and factors play a big role:

- Making profit.
- Achieving the public's interest in satisfying their travel requirements whether it is business or leisure.
- National prestige of the country.
- Economic issues e.g. tourism and foreign currency exchange.
- Political and defence policies.
- To develop and enhance the aircraft industry for those countries which are involved in such industry.

Much of the development of air transport will depend on the selling criteria of air travel and the amount of promotion contributing to it. There are many factors that will involve or affect the promotion or the growth of air travel; these being economical e.g. the GNP of the country, the personal disposable income and the currency exchange rates, political, fuel prices, air fares and the quality of service.

For various reasons it is supposed that civil air transport should have certain economic regulatory features where it serves the interests of the public.
These regulations should be effective and applicable to the interests of both the operators of air services and the public using them.
Wheatcroft has explicitly considered the reasons behind the importance of regulating air transport where beside the safety measures that would be effected due to the lack of government control, he refers to the industry as a quasi-public utility serving the objectives of national policy for defence purposes and of being a symbol of national prestige.
Wheatcroft has also referred to the economic characteristics of the industry, in advocating the importance of regulation, such as the limited effect of economies of scale, the lack of product differentiation and the oligopolistic nature of supply. (1)
On international routes and markets such as the North Atlantic with many airlines of different countries operating, it would seem more essential to emphasis on these factors and would be surprising to imagine how these countries would accept their air transport industry be liberalized of any regulation. Also to apply one country's regulatory machinery at international level needs certain principles and measures different than those when applied in its domestic operations. Here it is important to stress such factors as the sovereignty of each country over its air space, as emphasized in article 1 of the Chicago Conference in 1944 (2), and the acceptance by most countries of their international obligations e.g. in approving IATA's price fixing machinery, and in the existence of many formal civil bilateral agreements between countries,
With this in mind it would not be surprising to see each country building its regulatory system with much consideration to its own national interests first and the international interests second.

Therefore each country's political system and economic philosophy will play big role and would have great effect when formulating its regulatory machinery. So we cannot expect the basic principles to be considered in formulating a regulatory system in United States to be the same as those of the USSR, and if this is an extreme example, one may still observe the many different regulatory systems of the European countries.

The main issues to be dealt with in any regulatory system are:
Control of entry and exit, rates and tariffs and the competition involved.

The organisation to whom responsibility is given for implementing this machinery is another important issue. Some countries believe it is better to have the regulatory body within one of the government departments, while others feel more feasible and acceptable to have it outside the government but working closely with it.

Lord Boyd-Carpenter, CAA's chairman, delivering the thirty second Brancker Memorial Lecture on 3 February 1975, drew attention to this fact and enumerated the advantages and disadvantages of both systems; he felt that a regulatory body too closely associated with a government department would be unduly influenced by its ministry's politics. He suggested
a scheme where the regulatory body is placed "at least one remove from the world of politics and government" (3) in order to leave the body more free to enforce its principles away from the influence of politicians.

Lord Boyd-Carpenter concluded that the CAA of the United Kingdom and the CAB of the United States are the most reasonable of regulatory systems, but suggested certain changes to be necessary in the machinery and the organisation of these two bodies.

To give a picture of the regulatory machinery existing in the UK and the US, one should examine the background history and the creation of both CAA and CAB together with the many legal changes that have since taken place affecting the industry of both countries.

4.2 CIVIL AVIATION IN UNITED KINGDOM:

4.2.1. BACKGROUND:

A study of the background of British civil aviation must start with a look at the establishment of the Air Transport Licensing Authority in 1938 which aimed at, as the Edwards Report put it, "rationalising UK domestic air services following the Report of the Maybury Committee in 1937 referred with concern to the kaleidoscopic and financially unstable conditions of these operations". (4)

Following nationalisation of the air corporations which took place after the second world war, in which three public corporations were set up, the Civil Aviation Act of 1946 came into force in which granted exclusive rights to the British nationalised air corporations to fly scheduled air services,
leaving the private airlines the authority to operate only charter air services.

Three years later, under the Air Corporations Act of 1949, the Air Transport Advisory Council was created in order to give advice to the Ministry of Transport and Civil Aviation concerning the services which require permission to operate and on the many agreements already and subsequently concluded. (5)

In 1960 the Civil Aviation Licensing Act came into force and did away with the statutory monopoly of the nationalised corporations, and the Air Transport Licensing Board (ATLB) was formed to regulate a new licensing system in which both the nationalised and the private carriers were given equal opportunity to operate international and domestic services. At this time it was necessary for all commercial flights to have an air service licence to allow them to operate.

The ATLB had to look at the following matters as part of its duties:
1- The competence and fitness of the carrier to operate a proposed service.
2- To consult with regional advisory committees in considering such applications.
3- To consult with the Board of Trade about relations with other countries.
4- The general regulation of airline tariffs, and for prices and incomes policy. (6)

There has since been much criticism of the ATLB machinery; the Edwards Report issued in 1969 examined these criticisms.
very explicitly and focused mainly on two issues:
First, the appeal procedure and regulations allowed against the ATLB's decisions, where the Report recommended appeals to be taken to a judicial body not to the Minister, while the 1960 Act had given any party the right to appeal only to the Minister against the Board's decision.
Second, there had been no clear statements of policy, and the Edwards Report recommended that statements of policy be formulated by the government and published as a statutory instrument containing guidelines to follow. (7)

Stephen Wheatcroft, in his lecture given on 27 November 1963 before the Air Law Group of the Royal Aeronautical Society, referred to the role of the ATLB and criticized the general regulatory system of the Act of 1960; He emphasized the following issues:
1- Policy making, where he raised the question of "who makes policy and how is it promulgated ", and suggested that policy making should be left to the Minister. He criticized the appeal procedure as being only a rehearing of the original case, and thought it would have been more acceptable for the Minister to be given the authority to make policy.
2- On control of entry, capacity and tariffs, Wheatcroft called for a regulatory procedure to achieve unified control over the whole industry. He criticized the then regulatory system and then showed the division of control over three types of route: International, Domestic and Cabotage (table 4.1).
### Table (4.1)

**DIVERSITY OF AUTHORITY IN BRITISH AIR TRANSPORTATION REGULATION**

<table>
<thead>
<tr>
<th></th>
<th>CONTROL OF ENTRY AND CAPACITY</th>
<th>CONTROL OF TARIFFS</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>INTERNATIONAL</strong></td>
<td>1- ATLB licensing subject to appeal to Minister.</td>
<td>Ministry control as agreed in bilateral agreements normally by approval of IATA Traffic Conference Agreements.</td>
</tr>
<tr>
<td></td>
<td>2- Ministry negotiation of traffic rights under bilateral agreements.</td>
<td></td>
</tr>
<tr>
<td><strong>COLONIAL CABOTAGE</strong></td>
<td>1- ATLB licensing subject to appeal to Minister.</td>
<td>1- General-Ministry approval after consultation with Colonial Authorities.</td>
</tr>
<tr>
<td></td>
<td>2- Licence required from Colonial Licensing Authority (except specified Corporation routes).</td>
<td>2- Specified cases—ATLB approval subject to normal appeal procedure.</td>
</tr>
<tr>
<td><strong>DOMESTIC</strong></td>
<td>ATLB licensing subject to appeal to Minister.</td>
<td>ATLB approval subject to appeal to Minister.</td>
</tr>
</tbody>
</table>

3- On Inclusive Tour Charters, he analysed the situation in which an airline involved with a tour operation had to apply to the ATLB for a licence if it is a British carrier, and if the Board rejected its application the tour operator would search for a non-British airline to operate the same service without the need for such a licence. In this situation it would be difficult for the Board to refuse British applicants as by the end it would be effecting the position of the scheduled service operators. So Wheatcroft suggested instead that the tour operator himself should apply for the licence and specify the airline, whether British or Foreign, that would operate the route. (8)

The ATLB according to the Act is "to further the development of British civil aviation" but no positive guidance was given for the Board to follow on policy matters. As an independent licensing board it was responsible for regulating competition but had no responsibility for technical safety matters as these were the responsibility of the Air Registration Board and the Director of aviation safety. The Board had been given power to consider the financial resources, equipment, organisation and staffing of an applicant when granting a licence.

4.2.2. Edwards Report:

In July 1967 a committee chaired by Sir Ronald Edwards was appointed by the Board of Trade to look into the methods of regulating competition, the licensing procedures employed and the economical and financial position of the British civil air transport industry.
The Committee was to recommend any required changes in the industry that would serve the development of the economy, the safety of flights and the travellers' requirements. The Report was also to clarify the aims of civil aviation regulation generally.

The Edwards Report was subsequently regarded as a foundation of all civil aviation regulation policy in the United Kingdom; the 1971 Civil Aviation Act and the Civil Aviation Authority were in fact created upon the report's recommendation.

The report forwarded a multi-airline policy and to secure or achieve adequate level of service and airline efficiency it recommended the provision of a competitive environment and that a "second force airline" was needed to compete with the state air corporations. (9)

This second airline should come from the merger of the two main private air carriers British United Airways and Caledonian Airways.

Another important recommendation was the creation of British Airways Board to manage the public interests in the two state air corporations of BOAC and BEA.

4.2.3. CIVIL AVIATION AUTHORITY (CAA):

Air transport in most countries is regulated and protected by their governments and this responsibility in the United Kingdom has been delegated to a professional and a non governmentational organisation, the CAA, which acts as the government's expert adviser and has been the authorised representative of the UK government in most international aviation matters.
The Civil Aviation Authority, created on the recommendation of the Edwards Report, was formally brought into being on 22 December 1971 following the passage of Civil Aviation Act of 1971. It assumed full responsibilities on 1 April 1972 both as a public service and as a regulatory body.

Sir Ronald Edwards, in his speech presented in 1975 to the Air Law Group of the Royal Aeronautical Society, noted that the principle reason for recommending the creation of the CAA was that safety and financial strength were closely interlinked and should therefore be supervised by one body with special statutory authority.

This authority, although not a governmental department, has overall responsibility for such matters as safety, navigational services, airport planning, air travel organisers licensing, ownership and management of aerodrome, protection of consumer interests and price control.

The Authority refers to its responsibilities to be related with:

1- National air traffic services, air traffic control and telecommunications jointly with Ministry of Defence.

2- The economic regulation of the civil aviation industry, including air transport licensing and approval of air fares, and the licensing of air travel organisers.

3- Air safety, both airworthiness and operational safety, including the licensing of flight crew, aircraft engineers and aerodromes, and the certification of UK airlines and aircraft.

4- Advice to the government on domestic and international civil aviation matters.
5- Consumer interests; private aviation requirements, economic and scientific research; the collection and publication of statistical and economic data; and consultancy and training for overseas administrations.

6- The ownership and operation of the CAA aerodromes in the Scottish Highlands and Islands. " (10)

Three important functions of the CAA should be mentioned:
A- The Authority aims to see that demand is satisfied by the provision of services at the lowest possible rate but also with an economic return to efficient carriers.
B- In its approval of fares the Authority tries, beside considering many other factors, to relate the proposed air fares to costs.
C- It tries to balance the conflicting interests in civil air transport of the airline industry, air passengers and the nation as a whole. (11)

Figure 4.1 refers to the Authority's organisation chart, showing its departments: Economic, Safety, Finance and Planning, National Air Traffic and Personnel Services.

It was the Civil Aviation Act of 1971, which set out the broad objectives of government policy for the civil air transport industry, that provided for the establishment of the Authority. The Act gave the CAA the duty of ensuring British airlines provide air transport services to satisfy all substantial categories of public demand (section 1-a). Then the Policy Guidance of 1972 declared that as " civil air transport exists by serving the public, the Authority
Fig. 4.1

Organisation of the Civil Aviation Authority
should inform itself of the public's needs and take full account of them". (12)

Section 22-5-b of the 1971 Act gave the Authority power to fix domestic fares; but the fares detailed in paragraph 22 of the 1972 Policy Guidance should be set at levels which allowed a sufficient return to efficient operators, and at levels relating to costs. (13)

The Authority was also given, according to section 21 of the Act, the power to issue air licences, and it prohibited any aircraft from carrying passengers or cargo without having obtained an air licence.

The CAA, according to sections 36 and 61 of Act 1971 and as restated in para 26 of the Policy Guidance of 1972, is required frequently to publish statistics and information about the industry and to undertake research and development in such matters as air safety, traffic control, navigation services and air transport economics. (14)

It was in 1972 that the Secretary of State for Trade delegated to the CAA the power to approve international fares which have been previously agreed by the airlines at IATA meetings. But the consent to operate services into the UK by airlines was withheld from the CAA and reserved for consideration by the Department of Trade.

This division in responsibility between the CAA and the Department of Trade was criticised by the Authority itself, and Lord Boyd-Carpenter, in the 23rd Brancker memorial speech in 1975, emphasised on this point and made the remark that the "line of demarcation of functions is drawn in the wrong place". (15)
R. Colegate, in a lecture given on 4 November 1980 to the Air Law Group of the Royal Aeronautical Society, sees the two main elements behind the CAA’s policies as:

"- To limit and in the long term, to reduce the discriminatory elements in airline fares.
- To contain and reduce again progressively over a period, the extent to which one segment of demand is systematically overcharged in order to enable another to be undercharged so as to take advantage of elasticity differentials. " (16)

Policy Guidance of 1972 laid down the air transport objectives:
1- To ensure that British airlines provide air transport services which satisfy all substantial categories of public demand, at the lowest charges consistent with a high standard of safety in operating the services, while providing an economic return to the efficient operators.
2- To ensure that at least one major British carrier, not being controlled by the British Airways Board, has opportunities to participate in providing charter and other terms of air transport services that satisfy the public.
3- To encourage the civil air transport industry to increase the contributions which it makes towards a favourable balance of payments for the UK, and towards the prosperity of the national economy.
4- To further the reasonable interests of users of air transport services. (17)

Certain modifications in the British air transport were decided following a new policy statement published on
February 1976; these changes may be summarised as follows:

1- Not to allow competition between British carriers, and therefore not to have more than one British airline operating the same long haul routes, except services to and from London where Heathrow and Gatwick airports were considered to form one destination.

2- A restructuring of the networks whereby both British Caledonian and British Airways routes and services should become complementary rather than competitive. The new modified route structures arranged for BCAL to extend its services in South America by taking Colombia, Venezuela and Peru from BA; also services to Singapore and Central Africa were also transferred to BCAL from BA, while East Africa and the Seychelles remained with BA.

As for North America routes, Houston and Atlanta remained part of BCAL's network, and it was going to be the sole British carrier designated to operate this route when it became available.

3- Emphasis was placed on the role of British Airways as the main provider of international scheduled services, while British Caledonian was seen as the major private carrier.

4- The proposed Skytrain service to be offered by Laker Airways on the London-New York route would be cancelled. (18)

Finally, the Authority has always been directly concerned with the negotiation of arrangements made with international and European regulatory bodies and organisations such as
the International Civil Aviation Organisation, the European Civil Aviation Conference and the International Air Transport Association.

The CAA has played a major role in the implementation of the Advanced Booking Charter (ABC) and the Advance Purchase Excursions (APEX) type of fares in the early seventies on the North Atlantic routes.

We can say of the CAA that it has been committed to a policy of reduced control and supervision of the airlines' commercial activities, thus leaving them open to compete more effectively.

4.2.4. THE CIVIL AVIATION ACT OF 1980:

The first major issue dealt in this new Act was that the power of the Secretary of State for Trade to give Policy Guidance to the CAA, in respect of how to perform its functions, was abolished, instead the CAA was required to formulate and publish a statement of the policies that it intended to adopt in the field of air transport licensing, after consultation with industry and the users of air services. The abolishing of governmental guidance has strengthened the CAA and gave it more of non-political continuity to the development of its regulatory policies. Under the new Act, however, the air carriers retained their right of appeal to the Secretary of State against the CAA's decisions. The Act also proposed that certain environmental factors should be considered by the CAA, both when performing its air transport licensing functions and in exercise of its functions regarding aerodrome licensing.
These environmental factors were to include noise, vibration, atmospheric pollution or any other cause attributable to the use of aircraft for the purpose of civil aviation.

On international matters, the 1980 Act added to section 23 of 1971 Act a new paragraph stating that the CAA was to "perform its air transport licensing functions in the manner it considers is best calculated to ensure that British airlines compete as effectively as possible with other airlines in providing air transport services on international routes, and in performing those functions the Authority shall also have regard".

The 1980 Act also proposed that in granting any air licence on existing air transport services provided by British carriers, the CAA should consider the effect of authorising any new services under their new licence; and they were also to consider the benefits that might arise out of having two or more airlines providing similar services.

4.3. CIVIL AVIATION IN UNITED STATES:

4.3.1. THE 1938 ACT AND THE CREATION OF CAB:

In United States public utility regulation began with the Civil Aeronautics Act of 1938, where the Congress recodified the economic regulation of commercial aviation completely with a system of federal licensing, rate regulation, subsidy and regulation of mergers and acquisitions.

Under this Act, the federal economic regulatory responsibility was vested in the Civil Aeronautics Board and that each air carrier requires a "Certificate of public Convenience and
Necessity "(19) issued by the Board before operating a particular commercial air route.

These certificates were to be granted only when carriers were found financially fit to operate a safe service meeting public demand. However, certain certificates called "grandfathers" were issued automatically to those carriers who had operated services during the three months preceding the Act's coming into force on 22 August 1938 unless the service rendered during this period had been considered inadequate or inefficient.

The Civil Aeronautics Act of 1938 did a great deal to stabilise the air transport industry, and required the CAB to consider first, the promotion of adequate, economical and efficient service by air carriers at reasonable charges without unjust discriminations, undue preferences or advantages or unfair or destructive competitive practices; and second, to encourage competition to the extent that it might be necessary to ensure the sound development of an air transportation system properly adapted to the needs of the foreign and domestic commerce of the United States, the postal service and of national defence.

In 1940 the Safety Board was abolished and its functions transferred to the CAB, together with responsibility for regulating the economic aspects of air carrier operations, issuance of civil air regulations and other safety rules, and investigating aircraft accidents.

The organisation of the CAB was then divided into four functional groups: Economics Bureau, Safety Bureau, General Council and a Secretariat.
The CAB functions as an advisor to the State Department on international aviation affairs, such as bilateral air negotiations, and in representing the United States in different international air transport meetings such as the First Bermuda Agreement of 1946 which was signed between the UK and the USA mentioned in chapter two. Bermuda I agreement in its para (b) of Annex II pointed out that the CAB acts as an approving body for the traffic conference rate agreements reached through IATA's machinery being subject to the approval of the CAB. (20)

The CAB could only refuse, or alter the rates for international routes submitted by the air carriers if they were found to be unjustly discriminatory.

According to the Act of 1938, which was later confirmed in the Federal Aviation Act of 1958, the CAB did not have the overall authority to set rates on international routes as it had on the domestic ones. Indirect authority or power to approve rates was however given to the CAB over the US international carriers if they went into agreements among themselves or with foreign carriers.

Under the 1938 Act the CAB is equipped with the following powers:

1- Entry power; to grant or deny a "Certificate of Public Conference and necessity" which an airline needs to fly interstate.

2- Rate power; the authority to suspend or set air fares.

3- Anti-trust power; to approve or disapprove agreements among airlines.
4. Power to authorise mergers.
5. Power to administer a subsidy.
6. Power to enforce its own regulations.
7. Power to regulate certain matters of airline service.

The 1938 Act is the most important piece of legislation in United States' aviation history, setting out national policy for developing and promoting the airlines.

Richard Caves refers to this Act as the "basic statute governing public control of civil aviation in USA". (21)

Finally, one has to say that, the US airline regulation has been governed by the 1938 Act with entry and fares under its control with the provision of frequency, capacity and on board services being the only factors for competition.

4.3.2. THE FEDERAL AVIATION ACT OF 1958 :

This new Act recodified the general economic regulatory authority of the Civil Aeronautics Act of 1938, and it established the Federal Aviation Administration to regulate safety and provide for safe and efficient use of air space by civil and military aircraft.

According to the Declaration Policy in the Federal Aviation Act, the CAB is concerned in the following functions:
1. The encouragement and development of an air transportation system properly adapted to the present and future needs of the foreign and domestic commerce of the United States, of the postal service and of national defence.
2. The encouragement of competition to the extent necessary to ensure the sound development of air transportation.
3- The regulation of air transportation in such a manner as to recognise and preserve its inherent advantages, ensure its highest degree of safety, foster its sound economic condition, improve the relations and coordinate transportation between the carriers.

4- The promotion of an adequate, economical and efficient service by air carriers at reasonable charges, without unjust discrimination, undue preference, or unfair and destructive competitive practices.

5- The promotion of safety in air commerce.

6- The promotion, encouragement and development of civil aeronautics.

The CAB can be said is responsible for seeing that rates are just, reasonable, and non discriminatory; it has the power to investigate rates and to establish them if it sees the rates filed by the carrier as being unlawful. Mahlon Straszheim notes that the CAB has power to prevent discriminatory rates and to approve or disapprove rates proposed either by US or by foreign carriers, but that it has no power to set rates. (22)

It is due to the CAB’s lack of authority to set rates that the US carriers face difficulty to bargain within IATA; the Chandler dispute referred in chapter three is the prime example on this.

In addition, the CAB has no punitive power concerning the fares charged by carriers operating international services, as these fares are set internationally through IATA.
machinery, as agreed between the US government and other nations in the bilateral agreements.
The CAB approval for these international fares will mean granting to the carriers the immunity from the Anti trust law; while its disapproval of them removes this immunity.

According to the CAB's chairman, in a speech presented on March 1967 to the US House of Representatives, the CAB economic regulatory activities are concerned with:
1- Awards of operating authority.
2- Regulation of rates and fares.
3- Regulation of agreements and interlocking relationships, among air carriers, and between air carriers and other aeronautical enterprises.
4- Support of air services through subsidy payments.
5- Regulation of the air carriers' accounting.
6- Enforcement of applicable laws and regulations.
The CAB, through its Economic Bureau, tries to maintain a competitive climate by protecting the industry from a monopolistic situation.
The international rate orders of the CAB have to pass through the White House, and the US President is empowered by the Federal Aviation Act to disapprove any such order when he feels that disapproval is required for reasons of national defence or because of US foreign policy. If the President does not act to disapprove an order within 10 days, the order is then issued by the CAB;
while for routes' certificates, the President must sign the certificates and thus he share with the CAB the responsibility for the wisdom of the decision.

The CAB in 1951 questioned the statutory position of the non-scheduled airlines, on whether there was a need for large irregular carriers offering services in addition to those performed by public carriers holding a certificate. While it was being determined that there was a need for such services, the CAB granted those carriers temporary certificates; but because of objection and appeal by the scheduled operators, the CAB requested Congress to redefine the role of the supplemental carriers and to clarify its powers of certification.

Therefore, in July 1962, section 401 of the Federal Aviation Act of 1958 was amended to authorise the CAB to grant certificates of public convenience and necessity to the supplementals on a geographical basis; and the CAB was given the power to determine which carriers might operate scheduled interstate services and on which routes they might operate.

Opponents of the 1958 Act claimed that CAB control over entry and exit would reduce the economic pressure to keep costs down, and that it would safeguard carriers operating inefficiently while blocking the way for efficient ones, and that it would enable carriers to establish an inefficient route structure, with inefficient utilisation of aircraft, and in the end produce higher air travel costs.
4.3.3. THE AIRLINE DEREGULATION ACT OF 1978:

Deregulation of air transport in United States took a long process where in July 1975 the CAB stated its intention to liberalise entry and exit issues in commercial aviation and to give freedom to carriers to set their own fare levels.

The Aviation Act of 1975 later allowed a wider operation of competitive forces within the airlines.

After lengthy discussions by all the parties concerned, the US Senate and the House of Representatives approved a new regulatory reform bill, and the Deregulation Act was later signed by President Carter on 24 October 1978.

Emphasis in the 1978 Act was placed on having a liberalised situation; allowing a more efficient industry to emerge from market forces rather than government regulations, so the Act provided the following:

1- Allowing airlines to cut domestic passenger and cargo fares up to 50% or raise them by 5% without CAB permission.
2- Giving freedom of entry and exit to carriers of both passengers and cargo.
3- Phasing out the CAB's authority by 1982, unless it can be shown to be worth retaining over fares and mergers.
4- Complete abolishing of the CAB in January 1985 with transfer of its activities to the Department of Transport.
5- Anti trust exemptions granted to carriers were limited from the CAB authority.
6- Ending federal and state economic regulation on all US interstate carriers.
Before the implementation of the Act, price competition was almost non-existent in the industry with rivalry being mainly in terms of service and the frequency and scheduling of flights.

The main idea behind the Deregulation Act was to have a long list of fares, with travellers choosing fares from among those available that would suit their requirements. The Act would also leave airlines free to serve or abandon routes, thus producing stiffer competition and leading automatically to lower fares.

This could mean the industry shifting from what is considered having a public utility form of regulation to one that permits competition.

The CAB followed a policy of promoting more price competition and lower rates on international routes, and in encouraging the carriers to develop innovative pricing systems and also of having less regulatory interference in the carriers' decision making.

The Deregulation Act in its section 102 refers to what constitute in the public interest and the public convenience and necessity for the CAB to consider when performing its duties and powers; Appendix IV quotes section 102 in detail.

Finally, the advocates of deregulation believe that free entry is the keystone to an efficient system, without having the CAB to control and shape the structure of the industry, but leaving market forces to play their roles; and on the other hand suggest that regulation results in inefficient air transportation.
E. Levitas, Chairman of the investigations and oversight Sub Committee of the House Public Works and Transportation Committee suggests that "As deregulation is becoming institutionalized, there is no need to continue the CAB" (23).

In conclusion, it is of great essence to mention that in formulating the regulatory policies, the regulatory body of any country has to consider the national policies together with the satisfaction of the legitimate requirements of both scheduled and charter air services. Also providing an efficient network of services is the corner stone for considering air transport a public utility where without regulation seems difficult to maintain.
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CHAPTER FIVE

SCHEDULED vs NON-SCHEDULED SERVICES
CHAPTER FIVE

5. SCHEDULED vs NON SCHEDULED SERVICES:

The first task of the airline industry, whether it is involved in scheduled or non-scheduled operations, is to meet the public's demand for air travel. With the air traveller being no longer an economic elite the new phase of mass travel of non-scheduled transport has very different characteristics from that of the more traditional scheduled market.

In the past ten years the more liberal policies of a number of countries have assisted non-scheduled transport to become a vital sector, growing at a remarkable rate particularly in the North Atlantic, where low-cost mass transport with high load factors and lower costs has been vigorously promoted at the expense of the rival scheduled carriers.

Freddy Laker, in a speech at the Conference of World Tourism and Travel in 1973, viewed the situation where "scheduled airlines can never meet the low fare requirements because of fixed heavy overheads, complicated distribution system and enormous capital investment". (1)

With the non-scheduled carriers having such a significant effect on traffic in mid sixties and during the seventies, fares were developed which were low enough to attract travellers whose demand for travel was price elastic and who had a less rigid demand for amenities.

Before studying the characteristics of the two modes of service, one must define and understand the two terms.
5.1. **DEFINITION OF SCHEDULED AND NON-SCHEDULED:**

The Chicago Convention of 1944 gave the first elucidation and distinction of the two types of service where Article 5 concerned with the non-scheduled services read:

"Aircraft of a contracting state not engaged in scheduled international air services may, subject to certain conditions, make flights into or across the territory of all other contracting states" (2); while Article 6 read: "No scheduled international air service may be operated over or into the territory of a contracting state, except with the special permission or other authorisation of the state, and in accordance with the terms of such permission or authorisation". (3)

The International Civil Aviation Organisation (ICAO) in 1952 sought to redefine the shape and characteristics of international scheduled air services, as a misunderstanding had risen over what article 5 meant by "not engaged in scheduled". So the scheduled service was then to be defined as a flight that:

1. Passes through the air space over the territory of more than one state;
2. Is performed by aircraft for the transport of passengers, mail or cargo for remuneration in such a manner that each flight is open to use by members of the public.
3. Is operated, so as to serve traffic between the same two or more points, either:
i) according to a published timetable or
ii) with flights so regular or frequent that they constitute a recognisably systematic series. " (4)

While those states who were members of the European Civil Aviation Conference (ECAC), an organisation composed of representatives of civil aviation authorities of the European countries, in their Paris Agreement of 1956 elaborated on the meaning of non-scheduled, and it was agreed that no requirements were needed prior to the authorisation for:

1- Flights of a humanitarian or emergency nature;
2- Occasional taxi class passenger flights, provided seating capacity did not exceed six passengers, the destination was chosen by the client, and no part of the aircraft's space was resold;
3- Flights on which the entire space is hired by a single person or party for the carriage of his or its staff or merchandise, and provided that no part of its space was resold;
4- Single flights, of which no operator or group of operators was entitled under this sub-paragraph, to more than one flight per month between the same two traffic centres for all aircraft available to him. (5)

On the other hand the International Air Transport Association (IATA) defines the two types of service with the scheduled services as those "flights performed according to a published timetable, or so regular or frequent as to constitute recognisably systematic services
which are open to use by the public, extra flights occasioned by overflow traffic from the scheduled flights, and preparatory flights on planned air services"; while non-scheduled services are "charter flights and special flights performed for remuneration on an irregular basis, including empty flights related thereto and inclusive tours other than those reported under scheduled services". (6)

In mid 1977 the Special Air Transport Conference meeting in Montreal gave to ICAO’s Air Transport Regulation Panel (ATRP) the task of looking into the difference between the two types of service as the ICAO’s definition mentioned earlier was no longer satisfactory and it had become difficult to differentiate between the two services on the basis of this definition. The amendments and clarifications proposed by the panel were, however, subsequently rejected at the Second Air Transport Conference of 1980.

The amendments emphasised that "A service may be regarded as open to the public, not withstanding certain restrictions, which relate for example, to the time of reservation, the minimum length of stay, or the obligation to deal with an intermediary. It will be incumbent on each contracting state, in respect of these restrictions and decide whether the restrictions are so substantial that the service should be considered as non-scheduled". (7)

The Association of European Airlines (AEA), with a membership of twenty major European airlines consisting of: Air Lingus, Air France, Austrian, British Airways, British Caledonian,
Finnair, Iberia, Icelandair, JAT, KLM, Luxair, Lufthansa, Olympic, Sabena, SAS, Swissair, Turkish, TAP and UTA; in defining scheduled services also refers to them of being "regular or frequent as to constitute a recognisably systematic service". (8)

Here it is essential to mention that by regularity of flights one is to understand that the scheduled carriers face an obligation to provide this type of service with no consideration of load factors, as insistence on maintaining high load factors would reduce the customer's chances of finding a flight when it suits him.

On this obligation, the Edwards Report refers to the necessity of retaining "some degree of protection for the scheduled operator". (9)

On regularity of service and load factor, A. Rosenberg makes his own distinction between scheduled and charter service and sees that charter services make load factor the prime consideration while for the scheduled services regularity is essential. (10)

C. Taylor has a very distinct concept of the contrast between scheduled and non-scheduled carriers that of market loyalty. He sees charter operators as having little loyalty to the market, with economic circumstances forcing them to remain very volatile, while the scheduled operator feels a commitment to the routes he is serving. (11)

However, loyalty to the market is not confined merely to providing service but in offering that service to the public
at reasonable and acceptable fares to meet the demand and desire of the passenger.

A crucial objective of the airline's marketing strategy is to obtain accurate information on how the passenger sees the product offered to him with regard to the type of services, level of fares, the restrictions attached to it and the satisfaction perceived out of the use of a particular service.

Philip Kotler sees the customer continue using one brand of product "as long as their brand provides the anticipated satisfaction" (12).

Achieving his anticipated satisfaction when using one type of air service, the passenger would continue his use of that service unless to his disappointment that service ceases operating or it changed in providing unacceptable set of conditions and requirements affecting the passenger preference for that particular service or he may find his satisfaction and demand preference changing toward another different type of air service.

Kotler in his explanation of market loyalty, advocates that the continuity in the purchase pattern of a customer for a particular brand of product "would seem to reflect the intrinsic preference for the product but may really reflect habit, indifference, a lower price or the non availability of substitutes". (13)

Loyalty, however, is a two sided pattern, first by the customer towards one or more of the following categories:

- Brand of product e.g. APEX, First class, etc.
- An organisation e.g. British Airways, Pan Am, etc.
- A destination e.g. New York, London, Paris, Los Angeles, etc.

Second by the provider of the product towards a particular segment or type of customers who form his market. So availability and continuity of a service at a reasonable rate of return are principle factors on which this loyalty may be found and built upon, but can air carriers meet these two obligations at the same time.

5.2. THE INTER-RELATIONSHIP BETWEEN SCHEDULED AND NON-SCHEDULED:

With an increased need for non-scheduled services, demand in North Atlantic became widely distributed between the inelastic demand of high fares e.g. First class and Economy class passengers, and the more elastic demands of promotional fare payers e.g. Advance Purchase Excursions and charter fares passengers.

The different needs constituting the traffic mix and the rights granted by the international regulatory framework in allowing the existence of both scheduled and non-scheduled services, require ways to satisfy the demands of both categories of passengers.

The idea has to be accepted that both types of service may exist in harmony with each other where the needs of both being satisfied without any cut throat competition.

However, few distinctions must be made between these two types of service:
1- The means of selling seats to the public are different, requiring in the case of non-scheduled carriers the services
of an intermediary channel capable of marketing seats in bulk, while scheduled carriers tend to sell directly to the public.

2- Scheduled services are subject to bilateral air service agreements, and their fares are set within the machinery of IATA, while the others have greater freedom of operation, needing only the permission of their countries where their fare levels being agreed by the governments concerned. Also the fact that not only fare levels but traffic rights of the scheduled services are covered by the operations of the bilateral agreements.

In its attempts to control the operations of non-scheduled carriers, IATA in its resolution 045, established that minimum charter fares should not be less than the lowest scheduled fare.

In September 1974, at IATA's 30th Annual General Meeting in Montreal, it was allowed that charter carrier might apply for the Association's membership, and that charter agreements should be developed within the IATA machinery.

But, in November 1976, the CAB voiced its disapproval of the participation of charter carriers in IATA's machinery. The CAB's chairman, Secor Browne, had previously, in speech to the Royal Aeronautical Society in 1972, emphasised the United States' objection to both the multilateral approach to the operation of charter services, and of bringing charter rates within the IATA fare machinery. (14)

The United States had been favouring the implementation of bilateral agreements on charter issues and a revision of Bermuda
Agreement II in 1978 mentioned in chapter three dealt with this; while the Europeans have tended to favour charter issues coming within multinational agreement.

The CAB's Chairman also pointed out that, according to the Statements of International Air Transportation Policy, the US bilateral approach to charter services would depend on the propositions that routes would be governed by formula similar to those used in its own bilateral agreements on scheduled services; that there would be no control on capacity; that bilateral machinery should be used to prevent substantial impairment of scheduled services, and that there needs to be a definitional agreement. (15)

In 1972, when the CAB refused to allow the use of the affinity group concept, the United States and European countries made non-scheduled services available to the public by offering Advanced Booking Charters (ABC) and Travel Group Charters (TGC). In the USA, the Civil Aeronautics Board on 7 August 1975 passed resolution ER-924 which authorised non-scheduled transport under a new charter formula called "One Stop Inclusive Tour Charter (OTC)" where one intermediate stop was allowed on a package travel formula.

One of the measures taken by the scheduled carriers to combat the threat of the charter operations was to form its own subsidiaries operating outside IATA. Complementing that, and as a result of the US Deregulation Act of 1978, dual certification was permitted whereby charter carriers were allowed to operate scheduled services.
Finally, one has to mention that disagreement between the Europeans and the American is with regard how to bring the services of the scheduled and the non-scheduled into a co-ordinated process where the Europeans are recommending a multilateral approach in contrast to the country of origin rule advocated by the United States where rules and regulations of the country in which traffic first take place will govern the non-scheduled services of the bilateral agreements.

Therefore, one could say, even with the existence of distinction between the two types of service and due to the importance of such services by the passenger, the solution would require governments and airlines to be aware that both scheduled and charter services have to be regulated to provide better service to the public.
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CHAPTER SIX

FARES
CHAPTER SIX
6. FARES
6.1. INTRODUCTION
When the first Bermuda air agreement was signed in 1946 between the United Kingdom and the United States, it was accepted that IATA would be the channel or the tool in setting the international scheduled fares, subject to the approval of both governments before implementation.

As the fares and rates of the scheduled services on international routes are in the end controlled by the governments of the individual countries which they serve and because thousands of routes exist which cover the inter-connecting services between areas so that virtually every fare is related and dependent on every other one; therefore it seems much appropriate to expect and require multilateral acceptance and IATA's fares being spread by such use of bilateral agreements.

The fare agreements, reached through IATA's three traffic conferences representing IATA's geographical areas of the world, need unanimous approval of all the members concerned. In setting fares on the North Atlantic a multilateral acceptance seems more needed because more than the usual two countries are involved where beside pairs of countries existing within this market i.e. USA-UK, USA-FRANCE and etc there are those involved in fifth freedom services.

Air fares are usually taken to mean tariffs available in the marketplace to members of the public wishing to use existing means of transport by air whether it is scheduled, charter or inclusive. In the first two cases the tariffs are
presented by the air carriers as individual fares while in the last case the air fares are part of an inclusive package deal sold through the tour operators or their agents. Here one has to remember that fares of all types excluding First class provide virtually the same product i.e. a seat but the difference lies to the conditions attached in providing these fares.

The following main types of fare have been made available on the North Atlantic:

1- Normal fares: These are the most expensive fares, with choice of either First or Economy class. They are available to all members of the public with no stay restrictions and no limitations to the alteration of the tickets.

2- Excursion fares: These are cheaper than the normal fares but generally at various restrictions to their validity in the time of purchase and length of stay with restricted stopovers or none at all.

3- Skytrain: A scheduled, no frills, service first introduced and operated by Laker Airways between London (Gatwick) and New York in 1977. Other skytrain services were later offered to Miami, Tampa and Los Angeles from Gatwick; to New York and Los Angeles from Manchester; and to Los-Angeles from Prestwick. The skytrain service ceased operation with the collapse of Laker Airways in February 1982. These skytrain services were the first to reduce scheduled transatlantic air fares.
4- Standby: These are the cheapest fares available with scheduled airlines on the North Atlantic and were introduced as a response to Laker's skytrain service. The standby fare is a one way fare and available to many US cities from Gatwick, Heathrow, Glasgow and Manchester.

5- Advance Purchase Excursion (APEX): These must be bought and paid 21 days to 3 months before departure with minimum and maximum stay requirements. Also available Super APEX fares which are the lowest advance purchase fares but with more restrictive conditions.

6- Advance Bookings Charter (ABC): These are charter fares purchased 21 days in advance with a minimum of 7 days but with no maximum stay. These fares were introduced on the North Atlantic from 1 April 1973 following the meeting of representatives of ECAC, US and Canada in Ottawa to replace the Travel Group Charter (TGC) for flights from USA. The ABC rules implemented by the European differed from the American TGC rules in that a fixed price were introduced by the ABC while a pro rata system of pricing where the cost of charter is shared equally by the passengers occurred with TGC. Table 6.1 refers to the regulations governing both types of fares.

7- Budget: These fares are similar to the standby where the passenger nominates the week in which he wishes to travel with payment and ticket bought 21 days before the first day of the week in which travel is required.
Table (6.1)

REGULATIONS GOVERNING ADVANCED BOOKING CHARTERS ON UNITED KINGDOM/UNITED STATES SERVICES

SUMMER 1977

<table>
<thead>
<tr>
<th></th>
<th>ABC (Westbound)</th>
<th>ABC (Eastbound)</th>
<th>OTC (Available eastbound only)</th>
<th>TGC (Available eastbound only)</th>
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<td>60 days</td>
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<tr>
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<td>Yes</td>
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<tr>
<td>Minimum stay</td>
<td>10/14 days</td>
<td>7 days</td>
<td>7 days</td>
<td>10 days</td>
</tr>
<tr>
<td>Is substitution possible ?</td>
<td>10% from waiting list filed 45 days advance</td>
<td>10% from waiting list plus 10% off street up to 7 days before flight</td>
<td>?</td>
<td>15% off street up 14 days before flight</td>
</tr>
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</table>

The scheduled airlines were prepared to promote the new APEX fares on a wider scale not only because of their competitive impact on charter services but also due to the need to remain competitive in a North Atlantic market deeply affected by Laker's rivalry.

The availability of these special promotional fares at lower than the normal Economy fares could mean that the low yield generated could only be accepted by high load factors with the revenues that would be derived from those passengers paying normal fares.

At the time these low scheduled fares were being introduced the American CAB was beginning to liberalize charter services at a time when their competition was already pronounced.

Table 6.1 mentioned earlier shows the regulations and restrictions applicable to the non-scheduled fares available between the United Kingdom and the United States in the summer of 1977 at time when these low fare structures were increasingly available in the market place.

Table 6.2 shows the different scheduled and charter fares available on the leading route London-New York.

It is essential to mention that the introduction of APEX and ABC types of fare on the North Atlantic at about the same time was a sign that competition was growing between scheduled and charter carriers.

It is due to the availability of all these low promotional and competitive fares that discounted bucket shop tickets have not been sold by the travel industry on the North Atlantic.
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Source: ITA Study, No. 7/1978. PP. 23

Return scheduled & charter fares London-New York

TABLE (6.2.7)
6.2. DEMAND AND FARES:

Most organisations, from the marketing point of view, tend to have multiple objectives where beside the satisfaction of consumer, aim for a market share where to achieve a sales volume at a profitable terms to meet its obligations and to continue functioning effectively and competitively. The satisfaction of consumer in such an industry as the air transport could take the shape of providing air service for the traveller either on wide market or few or single city pair route, or to meet the demands of one segment or particular sector or the whole demand of all the different types of passenger i.e. Business, leisure, visiting friends and relatives.

The marketing strategy needed for each of the above situation taking into consideration the economic and political factors implemented by the country concerned, the air carrier will either aim to provide the type of service and the quantities required by the public or simply market the types of service provided by it.

The nature of the industry requires from the airlines to fulfill the needs and satisfactions of all segments of demand by offering multi number of fares than only one single fare but here one has to be careful of the abuses that might occur where many undifferent type of fares are created by airlines.

The problem facing the air transport industry is finding ways of satisfying diverse passengers' needs by bringing quality and cost factors into meaningful and profitable relationship.
To look at such crucial and sensitive issue from the point of view of both parties concerned, the airlines and the passengers, one has to start by examining the demand of air travel.

In the conventional theory, price tend to be a dominant variable and the way demand reacts to it is determined by the degree of elasticity. So one parameter to determine a meaningful measure of the relationship between air fares and air travel is the price elasticity of demand.

As all air travellers have freedom of choice from what is available in the marketplace, some passengers seek low cost fares with less convenient services while others prefer to face the high cost of more convenient services. Not overlooking the importance of the passenger being the consumer, here one has to remember that there are many types of passenger each with different needs.

The demand for passenger seats is usually drawn from two main sectors of the travelling public that of businessmen and holidaymakers and visiting friends and relatives. Each section is differently sensitive to fares, with the latter category being more responsive to price and with demand for travel having high degree of price elasticity than the former. The nature and purpose of the travel of each of these categories plays an important role in the degree of its price elasticity with business travellers having less in advance flexible plans requiring scheduled services with no restrictions attached to its availability; while holidaymaking and visiting friends and relatives tend not to require such fixed itineraries.
The elasticity of demand forecasts the overall trend of demand under the combined influences of rates and other factors such as the passenger's income. This elasticity is the propensity of change in travel due to price changes where it measures the percentage change in quantity demanded at certain percentage change in price. Here prices will be adjusted to the optimum level and a set of rates will be introduced whereby to improve the operations of airlines and at the same time the passenger will be provided with the service to satisfy and meet their needs.

Mahlon Straszheim in his study sees the North Atlantic market comprising two main segments, a tourist market seeking low fares and low quality at a high load factor, and being greatly sensitive to price, and a second market of businessmen looking for greater scheduled frequency, lower load factor, higher quality and therefore facing a higher fare.

In using the period 1952-1973, Straszheim has estimated the price elasticity for First class fare at -0.649, while the Economy service tended to have a high price elasticity of -1.92 at peak period of travel and the year round price elasticity was estimated at -1.48.

Then Straszheim in analysing the demand for the submarkets of the Economy service for the period 1963-1973 has estimated the demand function for high Discount market having a price elasticity of -2.73. (1) Then Straszheim went on to stress on the importance of
developing more varied types of service, with both peak load and off peak pricing, and sees that the existence of charter and inclusive tour fares, as part of the regular fare structure, is necessary to meet this segmented demand. The situation is seen by Straszheim as a supermarket, where the consumer is offered different grades of product at various prices. (2)

Mutti and Murai using data for 1964-1974 have looked on the price elasticity issue but from the point of view of the travellers' origin, i.e. the Americans vs European, where they estimated a year round price elasticity of -0.99 for the US and -0.07 for Germany, -0.14 for France, -0.28 for the Netherlands, -0.40 for the United Kingdom and -0.75 for Italy. (3)

In 1978, Stephen Wheatcroft has examined in his study the various price elasticity studies for the previous years together with his first work done in 1964 on the elasticity of demand on the North Atlantic. The conclusions of these studies are shown in table 6.3. (4)

M.A.Abe, in his paper published by the Department of Economics at Marquette University, lists air fare and service quality as the determinants of demand volume, where one finds those who are willing to pay more for higher quality service and those content to pay less for lower quality of service. (5)

Abe believes that deregulation could accomplish both the
# Table (6.3.)

## CONCLUSIONS ON PRICE ELASTICITY

<table>
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<tr>
<th>Study</th>
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<td>Total Market</td>
<td>Year Round</td>
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**Source:** Wheatcroft, S. (1978), 'Price elasticity revisited'.

increase in the number of travellers and consumer satisfaction in meeting the desires of the diverse submarkets by the provision of services at different quality levels and fares. He concludes that price elasticity for a skytrain service, of low fares and no frills, is higher than for a Concord high quality service, and therefore that applying fare reductions on no-frills services and increases on services of high quality, means in the end higher revenue and benefits for both passengers and airlines. (6)

A. Rosenberg, in his North Atlantic study, sees that the reason for having a higher price elasticity on the North Atlantic than on most international European routes is the high ratio of pleasure passengers to business travellers in the North Atlantic and that those pleasure passengers tend to be more sensitive to price variation and therefore that leads to greater seasonal variations. (7) According to the 1968 data published by New York port Authority, referred by both R. Smithies (8) and A. Rosenberg (9), that out of the North Atlantic Eastbond passenger traffic 18% were US business passengers travelling to UK and the remaining being tourists and those visiting friends and relatives; on the other hand, out of the west bond traffic to USA business travellers accounted for 27% of the total. Rosenberg reckons business travellers form 24.5% of all scheduled North Atlantic traffic to and from New York.
While Stephen Wheatcroft had suggested that 75% of all traffic is leisure travel and foresaw this type of traffic reaching 90% of the total traffic by the end of the century. (10)

Due to the fact that the market has had continuing growth in the more elastic leisure sector compared with that of the relatively inelastic business traveller, with more passengers using lower yield promotional fares, it might be said that no fare increase would substantially change the profitability position, as any increase would mean losing a certain proportion of passengers.

Fare increases tend to be economically harmful if the variable cost factors cannot be reduced at the same time.

IATA's Director General, Knut Hammarskjold, in his speech to the 37th AGM of the Association, saw that the nature of passenger demand has changed from that of low volume and therefore that traffic is becoming more sensitive to price elasticity and disposable income factors than it has been in previous years.

Hammarskjold focused on two factors that affect the availability of the different levels of fares that are necessary to meet the varying requirements on any particular route, where beside demand for seats stressed on:

1- The perishability of the product, as the seat will no longer be saleable when the plane takes off; and for that reason we see airlines offering seats for late arriving passengers at specially reduced fares to enable fill up the empty seats.
2- The need to have seats available to the passenger at any time is the chief reason why scheduled services are flown, where seats are offered at frequent intervals and in accordance to an issued timetable, although this may mean the carrier have to take the risk of flying with empty seats.

It will therefore be seen that when passengers have differing needs, which need to be satisfied, the airlines tend to provide different fares for each category of passengers, while at the same time imposing various restrictions and conditions applicable at different periods of the year.

Owing to the United States' domestic deregulation with its open sky policy implemented in the new bilateral agreements and its increased criticism and use of pressure against IATA machinery, the North Atlantic has seen airlines under pressure to widen their range of fares and introduce more low fares to stimulate demand.

With demand on the North Atlantic often being highly peaked, by that allowing airlines an over provision of capacity at peak periods, and where unused seats are left wasted making carriers seek early and quick revenue then one may consider not allowing competition as this will be wasteful. Beside the regulatory policy, the future demand for international travel will be influenced by such factors as the exchange rate of currencies, the availability and price of fuel, the inflation and the different rates of economic growth for the various countries.
6.3. Pricing and fare setting:
The economists see that the basis of laying down a policy of minimum price require costs to be at their lowest level. In air transport this would suggest to mean the provision of air services by the most efficient airlines operating at low costs offering low fares.

One of the possible cost reduction measures at times of excessive capacity would be the better utilization and reduction in capacity if needed beside the conventional minimisation in operating costs such as labour and fuel. The different types of fare should be based on the demand factor relating to it but in no case to be lower than the cost especially if the airline is there to achieve profit only with no consideration to national or economical benefits when setting fares.

The margin of profit incurred over the cost could vary and this will be built in consideration of the demand elasticity of these different type of fares.

M. Straszheim refers to this subject and stresses on the importance of the relationship between capacity, fares and load factors. He advocates that a fare structure should be based on long run marginal costs and that it should retain peak and off-peak pricing, make several changes in scheduled fares to relate fares to route density, eliminate free stopovers, base discount fares on advance purchase or group size and allow an advance purchase discount on all tickets. (11)

In comparison, Dr. Rosenberg has seen the following essential criteria when setting fares:
a) class of travel;
b) time of the year;
c) length of stay;
d) individual or group trip and size of group;
e) day of the week;
f) time of commencement of the journey and
g) number of stopovers. (12)

Historically, it is on the North Atlantic market that most of the major fare innovations have been first introduced, but as the changes in fares and eligibility restrictions on different classes of service have often been introduced, it has not been easy to examine and determine the effect of each of these factors separately.

In addition it has become difficult to differentiate between charter flights and the scheduled services on which one may find both types of passengers on the same flight where different types of fare are offered which have relatively similar conditions, for example APEX scheduled fares and ABC a non-scheduled fares are offered daily and on regular timetables.

This complex situation on the North Atlantic with the availability of so many different and complicated fares has led to the fact that a large proportion of passengers are not aware of the fares they are paying, or of what other fares are available, nor do they understand the tariff structure involved.

Edward Spry, Director-Industry Research of IATA in his presentation to an IATA symposium held in Dublin in May
1978 suggested that "airlines must work efficiently in making fare structure more understandable to the public" as many travellers do not know what type of fares they are paying. (13)

With the volatility of the market and prices, many number of fare changes are taking place which makes airlines' management difficult to implement a long term pricing strategy. This is so because when air carriers introduce any new fare then the rival competitors tend to change their prices accordingly to be competitive.

As a general understanding, the pricing strategy taken by airlines, especially the scheduled operators, require to make available a product that would satisfy passengers who are looking for both flexible normal fares and low cost promotional fares.

The value of product offered by airlines is affected by the conditions and availability of travel.

In satisfying the passenger needs, ways have to be found by the airlines in bringing fares, quality and type of service and costs under a system or procedure of calculation to satisfy the airlines too.

The availability of two basic pricing strategies, in which one provides a high level of capacity at a price at which to maximize revenue, while the other finances a lower capacity with higher load factor together with reduced prices, the airlines' choice will depend largely on the type of demand's nature.

By implementing the deregulatory approach a differential
pricing will be created where airlines will be able to charge different fares for relatively same service.

The Civil Aviation Authority in United Kingdom in its study "European Air fares" conducted in London in November 1977 referred to the following criteria as part of its pricing policy:
- fares to be at lowest level to cover costs of efficient carriers, together with an adequate return on capital.
- fares to be related to costs, and
- fares to be rational and simple.

By its pricing policy on the North Atlantic, the United Kingdom introduced ABC fares in 1972 and in 1977 approved the Skytrain fares of Laker, also authorised competitive scheduled fares.

While the United States in its air transport pricing strategy, the CAB advocated a diversification of fare levels to replace the old system and favoured peak and off-peak pricing where it offers low fares for flights less in demand and higher fares for more convenient flights at peak time.

The pricing revolution resulting out of deregulation has brought a variation in fare levels with vast number of changes in the low promotional fares that benefited only the discretionary passenger while the business traveller, being unable to meet the conditions and restrictions applied on the low fares, is left to pay higher fare.
6.4. Fares outlook:

As a general practice and understanding it is no surprise to find passengers asking and preferring to pay less for the product they buy, but at the same time it is essential not to overlook the simple fact that every commercial enterprise is in business to make profit to enable to survive and continue operation.

So, despite the availability of cheap air fares, the travelling public should never expect fares that do not cover the costs of the operator to continue at such low levels in a competitive situation as there will be no economical justification for these airlines to exist and continue operating unless such action of offering low fares is a short term policy to stand and overcome the pressures of this fierce competitive situation where so many operators are allowed to enter and leave the market.

The Edwards Report has advocated that fares shall not be less than "the economic value of the resources which are absorbed in the provision of each service" (14) and to be "the minimum economic price which can be contrived" (15). The pressure to reduce or offer low fares, in order to generate new demand and fill those empty seats, has to be balanced by pressure to reduce the unit operating costs involved in carrying all those new passengers.

Therefore it cannot be enough to maintain low fares and high seating load factors without there being genuine cost reductions.

A need just to fill the aircraft for its own sake, and
therefore putting the emphasis on improving seating load factors, would not help the situation at all but, rather hamper it as pressure is then felt to adjust schedules and if passengers subsequently have difficulty in obtaining seats then the very basic meaning of "schedule services" will no longer stand.

The present situation is one in which airlines in their struggle to keep pace with each other are dumping onto the market extra and undemanded seating capacity, so that not to lose an imagined competitive edge, that they feel necessary to be competitive in getting their slice of the traffic.

The consequences that airlines will face, with the need to sell more and more seats at low yield promotional fares only to fill extra seats and to maintain cash flow, is that extra or excessive capacity shall be created who was not necessary and would have never been provided in the first place.

The relaxation in the regulatory controls on the North Atlantic in the previous years have brought much pressure on the level of fares and rates with the scheduled carriers charging their promotional fares at even lower than incremental cost making non-scheduled airlines difficult to compete, therefore it is essential that scheduled and charter fares of both IATA and non-IATA carriers should fall under one acceptable fare machinery, which should enforce effective pricing to serve the interests of carriers and passengers alike.
Not only that, but the fares of non-IATA airlines have also to be discussed and covered, as no machinery will be effective and practical when part of the industry is under the machinery of IATA and its regulatory pricing system, while leaving the other part on its own.

Here two set of problems could arise, first the non-IATA carriers in introducing their own low fares they will jeopardize the IATA airlines' position in leaving them in continuance difficulty in reaching agreement on an acceptable and profitable fare, second the possibility that IATA airlines will reach a situation where they will match the low fares of the non-IATA even at an uneconomical levels just to stay competitive in the market.

Finally, widespread differences between international airlines as to what may constitute reasonable passenger fare levels are likely to lead to an open rate situation. The price war's dangers could effect consumers in the long run where if nothing is reached multilaterally between the parties concerned, the market will see carriers collapsing and forced out of business and so harming the interests of passengers.

Here we have to note that some of the airlines operating on the market have very low costs that make the other carriers not possible to cut their costs to match these airlines, so the present situation calls for airlines to start cutting their overhead costs and to look for more reasonable pricing for their amenities provided free of charge to customers, as it will not be enough to reduce
fares without reducing costs at the same time. We need better way of offering low fares while still producing revenue enough to meet the operating costs, and the need also remains to find better harmonisation between promotional scheduled fares and charter fares.
REFERENCES:


2- Straszheim, M.R. ibid. PP. 193.


6- Abe, M.R. ibid. PP. 47.


9- Rosenberg, A. op. cit. PP. 15.


12- Rosenberg, A. op. cit. PP. 30.


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CHAPTER SEVEN

COMPETITION AND REGULATION
CHAPTER SEVEN

7. COMPETITION AND REGULATION:

7.1. INTRODUCTION

Since early seventies the air transport industry in the North Atlantic has been passing through its worst ever economic crisis, facing tremendous pressure not only due to difficulties of the high cost of operation i.e. fuel and labour, but also from the intense competition that has surrounded its services.

On international routes, such as those of the North Atlantic, and as fares are set by the machinery of IATA, the area most left for competition is airlines' increase in capacity, with higher flight frequencies in an attempt to gain a greater share of the market; although this has in turn led to further complications.

The other areas left for competition were in offering a product of differentiated characteristics such as schedule pattern, safety record, passenger services, type of aircraft and reputation of the carrier.

The nature of the air transport industry producing a product different in kind from most other products or services offered to the consumer has played a significant role in generating this competition.

The uniqueness of air transport, mainly that of the scheduled services, is derived from its striking characteristic of offering such a perishable type of product where if the aircraft seats are not sold at the day of the flight then it would not be possible to store them or keep them for
next day's flight, and it seems no commodity is as perishable as an empty and unsold airline seat.

This waste or non-use of passenger seats is not similar to products of other industries where they could be stored for next day sale.

The other interesting criterion of the passenger seat is the control of supply per flight where the carrier's total supply is not controlled in the same manner as the production volume for most other products. Airlines tend to provide the same number of seats on a particular flight no matter how small or large is the demand for them and also the fact that the total capacity offered by the carrier cannot be changed easily to satisfy or to meet the change in demand.

Competition in international air transportation may occur at various levels and North Atlantic is no exception if not the most vulnerable market to such kinds of competition, and these being:

1- Between the scheduled carriers themselves.
2- Between the scheduled and the non-scheduled carriers.
3- Between IATA and Non-IATA carriers.
4- Between the public/state controlled and the private.
5- Between the airlines and other means of transport.

As mentioned in previous chapter, the North Atlantic is an air dominant market where competition from surface and sea transport is nominal that needs no mentioning and which give no worry for the airlines when formulating their policies contrary to what most other airlines would
face on their routes. Therefore our interest will focus on the first four levels of competition, beside understanding competition and how it works, and shall look first on what competition means.

7.2. DEFINITION OF COMPETITION:

Competition in business is generally a situation where two or more commercial establishments, involved in one line of activity, strive among themselves for certain advantages. Competition in the economic sense, foresee to maximise profit for the provider of goods or services and benefit the buyers of these goods and the users of these services, but where prices are controlled by the issue and the understanding of supply and demand.

In air transportation, Samuel Richmond refers to competition as that situation in which two or more carriers are authorised to perform essentially the same service. (1) Ross Rizley, ex-chairman of CAB, states that competition is the situation when two or more airlines contend between themselves for access to the available traffic, in approximately even terms and to get a better share of it. (2) Gill & Bates define air transportation competition as that situation existing when two or more airlines each carry more than 10% of the traffic between a particular pair of cities. (3)

Freedom of capacity, freedom to change prices and the ability of new firms to enter the market are necessary factors considered by Stephen Wheatcroft in his definition of competition. (4)
In speaking of competition, the Edwards Report refers to it as "regulated competition within a system of licensed entry and its consequential controls". (5)

S. Wheatcroft classifies the restrictions and controls over competition in air transportation as capacity and tariff regulation. The first includes controls over entry and licensing of routes, investment, innovations and control of scheduled; while tariff regulation means control over fares, rates, and quality of service. (6)

William O'Connor sees the removal of regulation on the international scene an impractical suggestion as no government will be willing to leave its air transport industry to the mercy of the market place, and he advocates the American system of regulated competition as most desirable. (7)

The Edwards Report has clearly recommended that regulated competition is the system best workable for the benefit of the customers in which "they will get comfortable and efficient service, that there will be enough capacity, that they will gain the advantages of technological advances and also enjoy the satisfaction of being able to choose between alternative carriers". (8)

The Edwards report sees competition existing only in such areas as quality of service and sales promotion, and stresses that no price competition exists in international airline operations.

But airlines on international routes especially the North Atlantic have always been involved in tremendous and continuous price manoeuvring, where different fares are
introduced with different conditions under various names and classifications to match fares of other carriers. If Laker's skytrain fare is not an example of such price competition, then why did other airlines spare no time and went immediately to introduce their own promotional fares to match Laker's fare; And if it's not price competition, then what can we call the price war going on that makes the introduction of new fares the only thing for airlines to think about.

In a study conducted in Canada by Ritchie, Johnson and Jones (9), mentioned that consumers consider the following four elements in understanding and viewing competition:

1- There must be a choice between at least two alternatives.
2- The availability of lower fares tends to be indication of competition.
3- Quality of service is a function of the competitiveness of the product.
4- The convenient of providing scheduled operations and flight frequencies.

7.3. INTERNATIONAL REGULATION AND COMPETITION:

Sovereignty of a nation over its air space is a vital criterion in international aviation, by which it allows governments have the major say and control in formulating their air transport policies and regulations. For that reason air carriers are greatly dependent on their
governments for upholding traffic rights, especially on international routes.

One reason that makes it difficult for the industry to reach a multilateral agreement on the North Atlantic regulations concerning both the scheduled and non scheduled operations could be attributed to the divergence of policies of America and European countries where the European suggest various regulation of the non scheduled services while the American encourage competition from non scheduled, but at the same time the American regulatory body of CAB disapproves the participation of charter airlines in IATA tariff negotiations.

In regulating international air transport, two alternative means exist; either to implement and extend one particular country's principles to other countries who are prepared to share the same thinking and philosophy, or to agree on certain common principles to be applied by the countries concerned.

In the latter case, this will depend on reaching multilateral agreements through various bilateral negotiations, and this would need to be done by taking into consideration the Chicago Convention principles where "fair and equal opportunity" would be set as the guideline in making international regulations.

The Bilateral air service agreements between countries, such as that of Bermuda type between the UK and the USA in 1946, lay down the rules, regulations and conditions of
how air carriers should operate on routes between the two countries.

In these bilateral negotiations, most foreign governments including the European usually try to equate their carriers' and aviation policies in general with the national interests, while the US government negotiates bilateral agreements based on its perception of the marketplace.

US. policy rests on the assumption of having many US. air carriers operating internationally, and of having a strong consumer movement with its own specific legislation promoting consumerism in international scene, in contrast to the situation in other countries, where there is usually only one carrier operating international routes where in many cases tend to be state controlled and have a relatively weak consumer movement.

With international routes, the North Atlantic no exception, being effected by various governments then the political motives behind the current situation should not be neglected, on the contrary need to be given special attention when criticising or justifying the need for regulation or competition on such a sensitive market.

With the market affected by certain political and national issues that play a large role in defining and regulating competition, then for the airlines to operate in such conditions need to maintain the interests of the public, being their prime objective, by making available different sets of fares with different qualities and conditions to
satisfy all categories of customers and to achieve their economic position by generating higher revenues resulting from fare reductions on no frill services and fare increases on high quality services; while at the same time keeping costs to the minimum, in the end improving consumer surplus and increasing the number of passengers.

On international markets, the North Atlantic being a prime example, competition has been promoted and enhanced by the US government following the passage of Deregulation Act of 1978 and the US International Air Transportation Competition Act of 1979 signed into law in 1980, which improved the competitive role of the American carriers. The latter Act, in facilitating consumer oriented fares, places maximum reliance on competitive market forces leading to an efficient service so enabling more people to travel to more places at lower prices. Also this Act prevents foreign governments and their respective carriers from placing unreasonable restrictions on US. air carriers which might result in their inability to compete effectively.

In addition, the Act had given the CAB the power to investigate, negotiate and if necessary to retaliate if it finds US. airlines having problems with discriminatory practices of foreign countries.

In referring to US air policy, one may see the air transport industry in different and varying modes toward the Civil Aeronautics Board, which sometimes favoured competition
as being the best means of achieving satisfactory results, while at other times allowed its policies to drift towards a greater degree of regulation.

After the passage of Deregulation Act in 1978 and following the success of Laker Airways at the end of the seventies in its operation across the North Atlantic, the US has shown its complete commitment to free competition both in its international as well as its domestic policies. With its free competitive approach, the US aims to achieve the following objectives:

- to meet the needs of all categories of traveller, by providing a wide variety of service and wide price options for the consumer to choose from.
- to provide more competitive fares.
- to offer fewer restrictions on capacity, routes and operating rights on scheduled services.
- to make available more non-stop gateways.
- to eliminate discriminatory and unfair competitive practices faced by its international airlines.
- to increase the provision of competitive air cargo operations. (10)

When the elements and principles of US. deregulation were put into practice in the international arena, the American carriers were no longer exempted from US. Anti-trust laws, and so were prohibited from participating in tariff coordination on the US-Europe market.
7.4. DEREGULATION CRITICS:

Internationally, the deregulation approach has come under much criticism both from within the US and the outside world to the extent that a comprehensive freely competitive international market cannot really exist, no matter how much it is sought, and it will be, in contrast to the domestic market of a country, a very difficult goal to achieve.

Applying deregulation within the USA bringing with it intense competition, with head to head competition between carriers, does not mean that all airlines and all markets elsewhere will experience and accept such severe and competitive situation. With the protection given by many countries to their airlines it would be unlikely to see deregulation working or being implemented efficiently at international level as to that in USA.

C.E. Meyer, President and Chief Executive Officer of TWA, criticises the implementation of deregulation on international scene where he sees it not working "because each of the various governments involved pursues its own priorities and objectives in setting and implementing aviation policy, based on its international social, economic and political needs". (11)

Airline deregulation in the international market has become a tool of US governmental policy, and therefore an increasingly debated subject within management.

The American government's objective has been to provide low cost scheduled airline services for its citizens, where by the deregulatory approach, US air transport policy
makers believe that they will help consumers both inside USA and abroad and also help the airlines to have wider access to the overseas routes.

But under deregulation airlines have easier access to new routes and will no longer be serving the public with the philosophy of "public convenience and necessity" because they will be competing and concentrating to make a profit. Also with every route to bear its own costs, the fare discrimination created out of deregulation is one area where, because of the high demand, airlines will be concentrating in their operations and services in high density routes to make profit.

Generally speaking from the commercial viewpoint it is a common understanding that the rate of return is related to the risk involved in a particular operation.

So with more freedom to abandon markets and higher costs of capital resulting out of deregulation, airlines will seek to raise profits to meet the risk involved by reducing services to low profit destinations and routes.

So here one has to question whether competition offers the best stimulus for airline efficiency and in improving financial position.

Stephen Wheatcroft has stressed that unregulated competition would lead to over capacity, financial trouble for the carriers and bad service for the travellers and suggested that some form of economic regulation is needed in the operation of international air services. (12)
Many European countries, together with most of the third world, are not only showing no interest in applying this US free open-skies policy, but are actively opposing it. The Europeans have emerged with different reactions with Britain and the Netherlands favouring freedom for carriers to set fare levels and gain easier access to routes, while the French and German governments display much scepticism towards any liberalisation of their own policies. Adam Thomson, Chairman of British Caledonian, who is also Chairman of the Association of European Airlines, criticises the US type of deregulation where "US open-skies policy on the North Atlantic routes ignores the economic reality that the long term loser may be the passenger". (13)

The reaction of the European carriers has been to recognise that organised competition is the best way to meet their governments' political and social objectives, commensurate with the economic position of the airlines and the needs of consumer. Gilbert Perol, President of Air France, points that "we should opt for organised competition. This is solely able to satisfy the government's political and social aspirations, the airline's profitability, and the consumers' needs." (14)

The Italians showed their opposition to the deregulatory approach and believe in the necessity of retaining capacity controls. According to Umberto Nardio, Chairman of Alitalia "Forcing other nations to accept deregulation US style is vanity. Do you really believe that, in a world with 110 airlines, most of them owned by their governments, a free market exists?." (15)
While Herbert Culmann, Chairman of the West German airline Lufthansa, believe that "the American attitude represents not only economic illusion, it is political nonsense". (16) At the Lloyds of London Conference that took place in New York in 1979, it was charged that the US free-competition policy is a phenomenon of "American economic imperialism" and by it the US is trying to destroy the multilateral framework which has hitherto existed on the international scene. The international critics are based on the following:

1- As the nations have dissimilar economic policies and national goals, it will be difficult for the US to impose the deregulatory approach on them and at the same time will be neglecting the issue of sovereignty that the Chicago Convention agreed upon.

2- With reasonable frequency of services being one of the main considerations of passenger convenience, it is likely that this be adversely affected by deregulation, causing many routes and markets to be abandoned and thus leaving many parts of the community unserved.

3- Competition is considered to be very effective during boom periods, but the offering of excessive discount fares during a boom will lead inevitably to overcapacity of supply in seats during a time of recession, and so request more regulations in such periods to counter the effects of recession.

4- Open competition policies are not in harmony with fuel policy where the very high cost of fuel makes airlines impose some restrictions on personal and leisure travel in
order that they may continue to make available a stable service for the business traveller, who has no option but to travel, and whose demand is therefore supposed to be price inelastic.

5- Open entry and free competition are not really so effective in achieving lower fares as are regulation and capacity controls.

6- In the operation of a free open-skies system we should not neglect the constraints of economy that exist and affect the industry. Within the air transport industry we find limitations imposed by airports' capacity, tourism restrictions, and air traffic control strikes. (17)

Stephen Wheatcroft, in his report prepared for the Canadian Transport Ministry in 1958, inquired into the advantages and desirability of competition on transcontinental services, where he showed that the following benefits result from implementing competitive air policies:

- the passenger will be provided with efficient services.
- the airlines will offer a choice of adequate services to the traveller.
- the airlines will be in better position generally to maintain and satisfy choice for the consumer.
- efficient airlines will be able to carry on providing their services.
- traffic will develop more rapidly, and in the end provide better results.
On the subject of choosing between allowing complete freedom of competition and applying restrictions and regulations, Thomka-Gazdik, Professor W. Guldimann and Professor Rigas Doganis have each considered the various options that might remedy the situation. Thomka-Gazdik in 1973 gave the following options (18):

1. Leave matters as they were at unilateral regulations;
2. Revitalize the affinity and inclusive tour controls in order to preserve what appeared to be the only meaningful distinction between the general public and a legitimate charter group;
3. Abandon the affinity concept and replace it with bulk or group charters with a "no strings" concept, in other words the planeload transportation of individual passengers who have no affinity other than the desire to travel at the lowest fare;
4. Ban the charter concept itself from the public transport.

While Professor Guldimann, beside continuing in the traditional way, raised the options of running charter operations with either free competition without substantial restrictions or free competition within well defined user categories, or with restricted competition; or bridging existing differences by establishing a multilateral regulatory framework that would mediate between the two extreme positions. (19)

As a compromise Professor Doganis proposed certain recommendations to be in the form of international regulations which would be politically acceptable and economically more justifiable and in "revitalising and changing the role of bilateral agreements" by:
1- Including non-scheduled operations in bilateral agreements.
2- Arranging for bilateral agreements to fix non-scheduled capacity as a proportion of scheduled capacity.
3- Redefining non-scheduled traffic.
4- Having bilateral agreements to designate "indirect carriers".
5- Controlling scheduled fares by a revised IATA system.
6- Insisting on no control of non-scheduled tariffs. (20)

On the issue of free competition, CAB's Chairman Dr. Alfred Kahn, who is a great supporter of deregulation, in a speech presented in 1978 to the Chartered Institute of Transport's Conference on International Transport, made it clear that in order to achieve a reduction in the actual tourist fare there must be effective free competition, and suggested that "the fact that carriers on the North Atlantic do not seem to be earning high or possibly even satisfactory profits does not invalidate the inference of ineffective competition, when the regular fare-paying traveller is forced to pay rates that cover the costs of expensive services he may want". (21)

Spreading free competition to other countries outside USA has become a great issue of conflict within IATA's machinery and it must be remarked here that governments in most European tend to influence or control their airlines. Adam Thomson, BCAL Chairman, affirms that "just about every scheduled airline within Europe is government-owned, and to imagine that a free market under these circumstances
would exist is, at best, naive". (22)

Table 7.1 demonstrates the proportion of state ownership and control in international air carriers.

The IATA Director General, speaking at the International Chamber of Commerce Congress in 1978, asserted the Association's rejection of the US deregulation proposition and stressed that "within the international community there is deep concern at the way the USA is seeking to change aviation procedures". He also pointed that airlines have national, social and economical objectives and not only commercial ones to be considered when formulating aviation policies. (23)

The Director General went on so far as to blame the CAB for creating a chaotic situation in the North Atlantic market, where so many different fares are available to the passenger that it has become difficult even for the airlines, their travel agents, and the passengers to be aware of them.

It must be noted that even if free competition in air transportation, as an economic concept, is acceptable and viable where successful economic efficiency and performance could be achieved by the different airlines where they will attain profit and by which the public will be satisfied in getting the required services at a low fare while in practice, the political difficulty will still remain in gaining acceptance and recognition that a free international air transport market serves the needs of all countries.

Taking into consideration the element of nationalistic
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<td>PAL (Philippine)</td>
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<td>Kuwaiti Airways</td>
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*Source: Intervia, October 1982, PP. 1078-1092.*
prejudice of each country, there are also so many differences in law, language, habits, currency, and political rules and practices between nations. All these make the difficulty in accepting a deregulation approach, applicable in USA which has not yet even been proved to work there, and it appears not to contain enough exportable philosophy to be acceptable and workable in other countries.

The philosophy reflected in the Deregulation Act of 1978 and in the new liberal US bilateral air agreements should not be the same in all agreements negotiated by other countries as consideration should be given to each country where the political and economical conditions are different and so it would not be appropriate to expect the American stream of thinking be accepted by the international community as for the international air transport system to be workable and effective it has to be built on the international interest and understanding.

William Seawell, Chief Executive Officer of Pan American, in his lecture to the Swiss American Chamber of Commerce in Geneva in 1978, took an alternative view of deregulation on the international scene as the "regulatory determinations are made by many governments rather than just one and because various governments have various—and often differing—views as the purposes to be served by their air transport system". (24)

US. Senator Edward Kennedy, in a letter to Jesse Friedman in 1975, stressed that "international air transportation creates economic facts and circumstances which are basically
different from those of the domestic industry, and it is not appropriate to automatically apply to the international field concepts of deregulation of rates and entry that are appropriate for the domestic industry. (25)

Finally, the nations represented at the Second Special Air Transport Conference of ICAO appear to believe that the American policy of freedom and competition is just not right for most international markets.

So in conclusion, one would say that the American belief and commitment to a fully free market could not be easily accepted by most other governments.

Governments need not to be blindly committed to deregulation because it's a fad or just for the sake of saying they're deregulated the industry.

With the airline industry existing as a quasi-public utility for so many years since its creation, it would be surprising seeing it thrown into an approach and discipline of free market without experiencing a reluctance from airlines in accepting such a change and at the same time expect a positive financial rewards for the parties concerned.

Also due to the international constraints mentioned earlier there will be a risk that some of the benefits expected out of deregulation will not be achieved if competition is not contained.
REFERENCES:


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23- International Tourism Quarterly. op. cit. PP. 9.


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CHAPTER EIGHT

THE CAPACITY ISSUE
CHAPTER EIGHT

8. THE CAPACITY ISSUE :

8.1. INTRODUCTION

Accepting the importance of schedule convenience and frequency when providing air services for the passenger and also of being, together with fares, essential factors and ingredients of competition have made airlines to strive in providing an excessive amount of seat supply to meet the above demand criteria.

This level of supply or capacity provided by carriers can not be changed easily even if the demand slowed down except by decreasing the number of frequencies or size of aircraft.

Therefore providing a higher probability of obtaining seat and the supply of greater number of frequencies with more convenient services means creating a greater capacity.

Capacity in air transport is referred as the maximum amount of payload that can be carried by the aircraft which is determined by the number of seats and the frequency of flights.

Some thirty years after signing the Bermuda I agreement between the United States and the United Kingdom, the implementation of the capacity issue was being questioned on the basis that it did not relate to demand.

Jesse Friedman refers to the subject of inefficiency of capacity use in the North Atlantic where he mentions that "the amount of capacity operated is far greater than the public demands or requires, and the capacity operated is inadequately utilised". (1)
Arguing that the US has an unfair advantage over the UK carriers where the American carriers were offering excessive capacity to the market, the UK government expressed its dissatisfaction. This led to the signing of Bermuda II agreement in 1977 which, as mentioned in earlier chapter, introduced some form of capacity control on the North Atlantic. The agreement allowed the "inaugurating" competitor airline to match the frequency of an already serving airline, without putting any controls over frequency or capacity.

The swamping of routes with extra capacity was to be prevented in this new agreement, while permitting increases in the frequency if growth was genuinely sought in the marketplace.

The International Civil Aviation Organisation, at its first Special Air Transport Conference in April 1977, examined this problem, together with the issues of tariff enforcement, international non-scheduled air transport, and the machinery for the establishment of international fares and rates. The Conference suggested that the existing capacity regulations do not match the objective of "fair and equal opportunity ", and recommended that all countries concerned should take into consideration the following points:

1. to coordinate their policies and regulations with regard to capacity control.
2. to include both scheduled and non-scheduled traffic in their considerations.
to ensure that the carriers of both countries concerned have fair and effective opportunity to provide capacity for the carriage of scheduled and non-scheduled traffic.
- to encourage their airlines to make the most efficient use of resources consistent with the provision of adequate air transport facilities.
- to monitor closely both load factors and the quality of service to the public. " (2)

Following the Bermuda II agreement, many changes took place where free capacity was advocated by the Americans and the IATA rate making machinery was in jeopardy since the US issued its Show-Cause Order.

The Second Air Transport Conference of ICAO met in February 1980 to look at the new changes. The feeling was that regulation of capacity had not maintained the objectives sought at its first conference namely: fair and equal opportunity, efficient use of resources (fuel, airport and airway facilities), co-existence of scheduled and non-scheduled services, and the maximizing of the public's interest (consumers, airlines and governments).

Therefore the Conference proposed three choices to facilitate the regulation of capacity based on following:
1- Predetermination where governments set capacity targets with some degree of flexibility depending on market needs, or
2- Free determination in which to give complete freedom to the airlines to establish their own capacity, or
3- Bermuda I approach where governments set only principles, leaving airlines free to establish capacity but subject to government review.
The first choice of predetermination by governments is accompanied by certain criteria to be considered by the parties concerned:

A- The need to relate capacity closely to demand in a flexible manner.
B- The need that the capacity to be provided should primarily be governed by the demand for the traffic between the territories of the two contracting parties.
C- The need to provide effectively for equality and mutual benefit for the carriers of both countries concerned.
D- The need to encourage the development and expansion of air transport on a sound economic basis and in the public interest.
E- The need to match traffic with airport and airway capacity, to make efficient use of human and material resources particularly fuel, and to protect the environment from air and noise pollution.
F- The need to harmonize the provision of non-scheduled and scheduled capacity in relation to total demand. "(3)

For the second choice that of free determination, the following guidelines were recommended by the conference for consideration:

1- Each party shall allow a fair and equal opportunity for airlines to compete.
2- All steps necessary should be taken to eliminate discrimination or unfair competitive practices affecting the airlines of other party.
3- Neither party shall unilaterally limit the volume of traffic, frequency or regularity of service, or the air-
craft types operated by the airlines.

4- No party shall impose on other party's airlines any requirement with respect to the capacity, frequency or traffic which would be inconsistent with the purposes of the agreement.

5- No party shall require the filing of schedules, programs for charter flights or operational plans by airlines of other party for approval except as may be required.

While the third choice, that of Bermuda I type, the following guidelines were recommended for consideration:

1- Air transport facilities shall bear close relationship to the requirements of the public.

2- Airlines shall have a fair and equal opportunity to compete.

3- Each party shall take into consideration the interests of the airlines of the other party.

4- The provision of capacity shall be adequate to meet the traffic demand between the airline's own country and the country of the ultimate destination of the traffic.

8.2. Over capacity:

The increase in the number of airlines and the difficulties in the economy together with the fact that each country has a different national interest have brought the interrelated issues of competition and capacity under criticism.

Most of the parties concerned feel unhappy about it, and are looking for a solution to the present situation whereby stricter controls would be imposed on capacity.
The industry is now facing a situation of excessive capacity and this has led to low load factors and financial losses for the airlines.

As over capacity not only means the availability of too many unused seats but also achieving low load factors at low fares level, this excessive capacity has been calculated on estimates of the availability of both greater frequency of flights and extra seating capacity.

However, in international air transport it is likely to be very difficult in practice to implement either of the extremes of control and regulation on the one hand, or unrestricted competition on the other.

H.A. Wassenbergh refers to excess capacity as the "unused capacity of the aircraft below a certain standard percentage of the aircraft which must be sold to ensure an economical operation of the route concerned over a certain period of time ". (4)

J. Friedman describes excess capacity "in terms of the surplus offered beyond that which is needed to meet public demand satisfactorily and sustain a profitable level of operation ". (5)

Excess capacity is generated by the fact that there is no traffic growth sufficient enough to accompany the available number of seats, leaving empty seats (capacity) unutilised. It is owing to the superiority of the established airlines on the North Atlantic, especially the American carriers e.g. Pan American and TWA, with the advantage of operating...
at low costs compared to those new entrants which make them provide capacity amounts extra than needed.

It can also be said that the demand by US of extra capacity in its negotiations with other countries concerning rights on the North Atlantic can be attributed to the belief that such a market is important to its counterpart countries involved in the negotiations and that these countries would lose in not serving in this market or when even not reaching agreement with the US.

The over capacity situation is caused, as the Edwards report puts it, by the existence of unregulated competition which has led in the end to high costs, with traffic not being sufficient to allow the carriers to operate the services that are necessary in order to compete with their existing rivals. The Edwards Report has also shown that having a high traffic volume means that an airline will operate on:

"1- Higher average load factor as more frequency of flights being operated.
2- Lower cost per seat mile as larger aircraft will be used.
3- Lower cost per passenger.
4- Lower unit cost in sales and advertising." (6)

Stephen Wheatcroft (7) suggests that high traffic will enable the airline to gain the economies of high utilisation of these terminal facilities, to schedule a higher frequency of service and lower seat mile costs will be achieved with the use of larger aircraft than smaller ones.

Nevertheless, one should not always advocate new airlines
to be introduced immediately when there is a traffic increase because the new capacity provided by the new entrants together with the extra capacity offered by the existing carriers due to extra frequencies and the use of large and usually more expensive aircrafts to meet this increase in demand, will be far greater than this increase in traffic and this will eventually mean either looking for new traffic increase to breakeven or the market is left with an excessive or extra unused capacity.

In other words, excessive capacity is a situation that has resulted from the miscalculation of management in their desire to meet the demand that was created initially through their policies of offering lower fares to fill some of the empty seats and that in turn needed extra new capacity to meet the newly created passenger demand, but that has culminated in the carriers' being left with excessive new capacity on their hands that they never initially bargained for.

So the control of capacity is required by the industry in order to improve load factors and lower unit operating costs; and this may be achieved by the better utilisation of available capacity before introducing any new amount of capacity.

It is no surprise that with more carriers, more frequencies of flights, more seats to fill and more destinations to serve, the marketing job facing airlines' management is becoming harder and difficult.
8.3. Capacity control vs share of market:

In measuring or determining capacity of an airline on a route or the total capacity of all carriers on all routes, the load factor is not enough if not accompanied by a reasonable level of profitability as the growth measured will not be sufficient if seats are not filled with an economical and financial rewards.

Also, the seat load factor is not sufficient because the complicated fare structure existing in the market is not giving a better overall operating revenues.

Therefore, maximizing traffic by itself is not enough by airlines' policy to achieve better financial performance as the essential factor is the need to maintain or boost yields.

It would be important to consider when calculating or deciding the load factor, that the availability and usage of different sizes of aircraft could require a different load factor as the probability of obtaining a seat will differ where an aircraft with less number of seats have higher probability of a passenger not securing a seat and therefore require a lower load factor than an aircraft with more number of seats.

In defining a low load factor, William O'Connor refers to the CAB's Statement Draft Regulation 43, of 19 August 1975 as being that situation where it is easy to obtain a seat on a flight, while a higher load factor means increasing difficulty in obtaining a seat especially at peak periods. O'Connor also implies that low load factors mean higher
fares as passenger unit costs will be high and the obvious corollary being that high load factors allow lower fares as unit costs will be lower. (8)

As mentioned earlier, high flight frequencies and high probability of finding seats on a flight are two main and essential characteristics given for a scheduled service. The number of participating airlines, the flight frequencies together with the size of aircraft i.e. number of seats make the total capacity offered on the route. So the increase or decrease in the number of flight frequencies, with the number of seats tending to be relatively constant, is the major factor that effect capacity.

With no initiative by one carrier to cut capacity i.e. the number of flight frequencies originally offered if other airlines do not pursue the same action is a natural expectation in the industry where share of market will be determined by the capacity offered. This reluctance arises because the scheduled airline will be fearing that first, other scheduled carriers will benefit out of this unilateral action by getting better share of the market and second, traffic will be lost to their charter rivals especially when the charter capacity is not brought under the same regulatory machinery of the bilateral air agreements.

Owing to the fact that more pressure is exerted on the scheduled airlines to continue in providing such high
amount of capacity to meet the characteristics features of scheduled service, airlines are forced into a more imbalance situation of supply and demand therefore playing an effective role in harming the efficiency and the financial results of the carriers.

On the North Atlantic, the rival carriers tend to emphasize in their advertising campaign on the number of frequencies they provide on their different routes as being different and convenient than those offered by the others.

Jesse Friedman has referred to the often-drawn conclusion that operating at greater frequencies will result in a greater share of the market. (9)

This can be true and would apply in the case of a free for all situation, as in the North Atlantic, where no effective control exists on capacity offered, and where competing carriers will quickly jump to obtain any loose capacity for their own use should any other carrier reduce its frequencies or even withdraw from the market.

So in the existing situation carriers will maintain their market share no matter how much costly that would be.

Any solution must require the determination of all the parties concerned to modify the existing bilateral agreements, and they will have to abandon any rigid adherence to the philosophy of free open market and impose restrictions on capacity offered.

The present surplus of capacity provided by the airlines is so great that no initial reduction of supply is likely
to have any real negative effect on convenience to the public or in maintaining adequate scheduled flights, and to allow the carriers to continue their operations with such excessive capacity cannot lead to any increase in the quality of the service they provide, in the sense of offering better scheduled flights to the passenger; on the contrary, a level has been reached where the total number of extra seats, offered by all the carriers, is a complete waste, of no benefit neither to the public nor to the carriers themselves.

Improving services by offering direct scheduled services to new US destinations beside the main gateways can only be justified if airlines can perform at positive financial results. Cutting part of the scheduled capacity to enable achieve better financial performance should not be considered as a degrading procedure to the quality of service.

The inclusion of the non-scheduled operations in the bilateral agreements and the provision of rules to control their capacity would be one reasonable way to control the supply of seats to ensure better results. The control of capacity is required to avoid the situation of extra costs being incurred which will then be built in the price levels.

The market has experienced a high rate of increase in capacity mainly due to the increase in the number of flights offered after the appearance of new carriers in late seventies, while the passenger traffic increase did not
match this capacity increase and unfortunately since this increase was sustained by more than one new entrant had surely meant more difficulties for the already existing and committed carriers as this meant they had to provide more capacity to meet this new competition to keep its share of the market, and this result in higher unit costs, while the new entrants are incurring relatively lower unit costs for these new routes involved in.

In embarking into a price war situation to achieve a better cash flow, it would be economically justifiable to apply such price war action where excess capacity is available in the market, by that attempting to reduce their extra capacity by filling empty seats at such marginal costs.

The current situation on the North Atlantic would appear to demand not lower fares, sought by the free-market advocates "to induce a contraction of capacity" (10), but also the immediate agreement to a capacity reduction.

To remain competitive and to offer quality of scheduled flights, the airlines are ignoring the financial or economic factors and consequences arising out of such action.

Bad financial conditions and results should really make the airlines consider the option of reducing capacity, and to see this as a very genuine, and perhaps the only practicable, way of leading them out of the crisis.

Facing severe competition, airlines especially the more efficient ones, in cutting their prices to keep their
market share or gain new share, have not proved to achieve positive results. Also the fact, that due to the protection given by many governments to their airlines to prevent them from collapsing, and the fact, that efficient carriers will do their best to push the less efficient airlines out of business by accepting to cut their fares so that to attract more passengers, by that requiring and creating extra capacity to meet this new wave of passengers, this made the situation worse resulting in harming the carriers to suffer and engage in bad financial results. M. Straszheim trenchantly observes that "it is the commitment of governments to subsidise their flag carriers that underlies the continual 'excess' capacity problem in international air markets". (11) But the fact of the matter is, that to maintain high capacity or low fare scheduled services by governments' subsidies will not solve the problem as it would be an unfair economic justification when these countries can continue injecting cash and provide the support required to keep them operating while at the same time jeopardising the financial position of others. So the major task for airlines presently is to have control over capacity in seating, in fact, cutting the number of carriers themselves or flights may be the only reasonable way out from the present crisis which also avoids an air fares' war between the airlines, but this will need a joint or multilateral acceptance by the
countries and the airlines concerned.

Mutti & Murai stress that "there is a basic reluctance for any airline to act unilaterally in reducing its scheduled capacity, because there is a close relationship between the share of total seats offered and the share of total passengers attracted". (12)

Therefore an acceptance by the whole industry is needed and not just by few airlines.

The question we face today is why the scheduled airlines are not then cutting down their flight frequencies to decrease the capacity offered?

If the question seems simple, the answer appears not as we are usually told that airlines must maintain their competitiveness in the market by providing a share of supply which matches that of its competitors to enable maintain or increase their share of the traffic.

Cooper & Maynard refer to this by saying that "the more flights any one airline has, the larger the share of any given market it stands to get". (13)

But as we have seen, providing extra frequencies and seats to stay competitive may harm the airlines more than benefit them, since it is not enough to have a larger share of the market if that share does not pay for itself, in the sense that extra revenue earned by this activity may not cover the extra costs involved if those extra seats are marketed at low fares and returning a very low yield.

In such a situation, the airlines appear powerless to
help themselves, choosing to remain operating in an unhealthy financial position.

Airlines should not expect that offering the public too many low type fares will help them get over their problems while their capacity is not effectively controlled. The remedy must be more radical and require the understanding by all parties concerned that the solution lies not in attracting new passengers at whatever price to meet the capacity provided. The operators must be made to realize that too many seats are being provided, and realization of this fact will prove to be a stepping stone to the solution.

The truth is that some governments and regulatory authorities, indulging in laying down the sort of air regulations that we now have, have brought such a situation that no one carrier can by itself afford to take action to reduce capacity.

There is also that feeling among some private independent airlines that they have been forced and pushed into competing with airlines that have protective civil aviation policies applied by their governments.

Adam Thomson, Chairman of British Caledonian, is one of those in industry who suggests that "governments and airlines will endeavour to protect their market shares whatever the cost may be. Over half the world airlines are owned by governments .... As the price war escalates I would suggest that those without government support will inevitably disappear". (14)
It seems likely that carriers will soon reach a point when providing additional frequency to that already existing would provide little attraction for passengers and produce little effect on the market share; but it would on the contrary drive carriers towards the increased difficulties of not being able to meet the financial obligations arising out of those extra costs of increased frequencies of flight.

With little effect on the full fare payers and with such severe competition existing, the airlines are trying to persuade as many extra passengers as possible to fly by offering them such low promotional fares which simply do not cover costs.

Merely obtaining a well-filled aircraft is not the solution to the problem where it would still be commercially not viable if the return or yield received is unsatisfactory or insufficient to meet the operating costs and to generate reasonable profit for further investment.

It is true that load factors may have been low when there was a large surplus of capacity, but when it came to remedy the situation and improve load factors, it was at the expense of uneconomic returns as people were encouraged to fly at very low fares.

The present situation of financial ill-health in the airline industry and where costs are constantly escalating, would force the airlines to discipline their approach to scheduled operations and to minimise cost factors in the search for alternative means of operating in more efficient ways.
To limit capacity and depending on the market and the season, one can suggest number of flights to be decreased and this would result in increase or improvement in load factors. To engage in such an action and to avoid any possible disadvantages resulting out of it, it is necessary to have fares under control where any decrease in fares would not be justified during when the services are cut as passengers might consider this as unfair to accept higher fares for a relatively lower quality of services especially for those passengers who tend to consider cutting flight frequencies as sign of lowering quality of service. Here an acceptance by the whole industry is needed not just by certain airlines where one cannot be left with one segment of the industry advocating fare reduction while others ask for a fare increase.

For airlines to decide or implement a strategy of choosing between a profit oriented policy seeking high yields from passengers or achieving a high share of the market is an important issue for airlines when considering capacity while it is true that share achieving policy fulfills the demands of higher number of passengers by catering for a higher share of the market. The disadvantage would be that too much capacity will be offered by airlines, to be in a favourable position to seek or achieve a higher share of the passengers, beside the fact that part of their share would be earning a low yield as this part of demand is motivated and created by the sheer fact of low fares.
In general one could conclude that it would be necessary to impose a ceiling on the capacity granted based on the level of demand required to attract sufficient services, thereby placing maximum reliance on market forces and on actual potential competition and at the same time provide or maintain a convenient system of scheduled services so that to meet the market needs. Finally, for airlines to return to healthy and profitable situation, one may revert to the prescription made by the Strategic Planning Sub-Committee of IATA's Annual General Meeting on 8 November 1982, where it recommended "established economically sensible fare levels, having a genuine relationship with costs of their operations; reduce the erosion of yields caused by illegal practices; and obtain government approval for inter-company co-ordination and refrain from individual extreme measures, in the direction of either liberalization or protectionism". (15)

In Appendix I the writer suggests a set of recommendations as remedial action to the present situation facing the North Atlantic air transport industry.

**********
REFERENCES:


3- Taneja, N. ibid. PP. 76.


5- Friedman, J. op. cit. PP. 31.


9- Friedman, J. op. cit. PP. 33.

10- Friedman, J. op. cit. PP. 48.


15- Interavia, (1983), 'IATA AGM aftermath—there's more to doctoring than diagnosing'. January. PP. 76.

***************
CHAPTER NINE

ANALYSIS OF OPERATING RESULTS
CHAPTER NINE

9. ANALYSIS OF OPERATING RESULTS:

In this final chapter, it is appropriate and essential to analyse the operating results of the North Atlantic market for the period 1970-1980 by looking at such crucial areas as financial results, yields and revenues, costs, profitability, type of fares, fuel prices, seating capacity, passenger traffic and routes and airlines.

In introduction it should be noted that the years 1978, 1979 and 1980 saw a pattern of proliferation of very low fares, entry of new US carriers and other international airlines, availability of new gateways and the shift in the balance of US originating cities to European originating routes.

All this led to the remarkable growth in scheduled traffic and a decrease in charter traffic, also the scheduled carriers fearing the effect of competition caused by the law fare charters introduced its own low promotional fares instead of liberalizing their own charter operations.

Having said all that, one has to refer to the reasons causing this drop in charter traffic and the transfer of passengers in using more scheduled services:

1- The signing of Bermuda II agreement between the United Kingdom and the United States and the liberal interpretation of the reciprocal traffic rights brought by other new bilateral agreements between the USA and European countries made the scheduled operations less regulated where new gateways were introduced and additional airlines were authorised to offer scheduled services.
2- As a result of deregulation, the charter US carriers were permitted to operate both charter and scheduled, dual certification, services.

3- Following the introduction of Laker's skytrain service on the North Atlantic in late 1977 offering scheduled low fares and with the increase in the availability of low fare charter services, the scheduled carriers started offering their own low fares budget, standby and Super APEX which provided 14% share of all IATA scheduled traffic in 1978 and together with the APEX type of fare already available brought the share of all these low fare scheduled services to 27%. This type of fare increased in 1980 to represent 45.9% of all IATA scheduled services operating on the North Atlantic.

Table 9.1 refers to passengers breakdown by fare type using IATA scheduled services on the North Atlantic for the period 1970-1980.

These low fares offered by the scheduled were so attractive, table 9.2 shows a comparison between charter and scheduled fares offered on London-New York in winter 1977/1978, the passenger saw no difference to the low fares of charter services, and also the scheduled carriers saw no need to offer charter services if they can provide such low fares on scheduled basis especially at off season when demand for travel is low. This also led the scheduled airlines to cease operating their charter services.

Also the wave of the new promotional fares introduced by the scheduled carriers, even with restrictive conditions, have attracted traffic from the existing normal fare
### Source
IVA/Air Transport Statistics

**Group Inclusive Tour Introduced in 1967**

*CGIT - Contract But Inclusive Tour Introduced in 1967*

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<td>4.4</td>
<td>4.6</td>
<td>4.8</td>
<td>5.0</td>
</tr>
</tbody>
</table>

**First Class (Including Concorde)**

**Total**

**Others**

**Youth**

**Affluency**

**Budget / Standby**

**Super Apex**

**Apex**

**Examination: 7-17/21-28 Days**

**Economy Normal**

**Passengers Breakdown by Fare Type 1970 - 1980**

**IVTA North Atlantic Scheduled Services**

---

**Table 9.1**
Table 9.2.

LONDON–NEW YORK WINTER 1977/78 FARES

<table>
<thead>
<tr>
<th>CHARTER FARES (£)</th>
<th>SCHEDULED FARES (£)</th>
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<tr>
<td>ABC from 95 Return to 153 £</td>
<td>CONCORDE 862 RETURN</td>
</tr>
<tr>
<td></td>
<td>FIRST CLASS 713 £</td>
</tr>
<tr>
<td></td>
<td>ECONOMY 340 £</td>
</tr>
<tr>
<td></td>
<td>14/21 DAYS EXCURSION 293.50 £</td>
</tr>
<tr>
<td></td>
<td>22/45 DAYS EXCURSION 254 £</td>
</tr>
<tr>
<td></td>
<td>YOUTH 256.50 £</td>
</tr>
<tr>
<td></td>
<td>INCENTIVE GROUP FARES 254 £</td>
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<td></td>
<td>NORMAL G.I.T. 230.50 £</td>
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<tr>
<td></td>
<td>7/8 DAY G.I.T. WINTER 207 £</td>
</tr>
<tr>
<td></td>
<td>APEX 153 £</td>
</tr>
<tr>
<td></td>
<td>STANDBY 64 ONE WAY</td>
</tr>
<tr>
<td></td>
<td>BUDGET 64 £</td>
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<tr>
<td></td>
<td>LAKER'S SKYTRAIN 59 £</td>
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</table>

paying passengers and diverted traffic away from the charter where the charter traffic dropped to 2 million passengers in 1980 compared to a record of 4.4 millions in 1977.

As a result of the spread of promotional fares offered by IATA's airlines and the low fares charged by charter and scheduled carriers outside IATA's machinery, the average revenue per passenger has been decreasing. The fact, too, that operating costs have been increasing faster than revenues has led to a loss-making situation.

With North Atlantic scheduled fares falling 20% in real terms over the period 70-80 and with capacity ever shooting up, the airlines are loosing an aggregate of at least 4 to 5 million Dollars in 1980.

The ICAO Annual Reports show that the Average unit cost of scheduled carriers reporting to ICAO rose from 25.2 US $ per available tonne-Kilometre in 1976 to 41.0 US $ in 1980 giving a 62.7% rate of increase.

Fig. 9.1 demonstrates the dramatic shifts in operating costs and revenues occuring on the North Atlantic during the period 1970-1980, in which airlines have been sustaining losses where the costs have been higher than the yields received which resulted in low operating ratio. This trend has been more serious since 1978 when the gap or the difference between the increase in cost and yield per passenger has been higher bringing the operating ratio to approximately 90 in 1980 being much lower than the figure suggested by IATA's cost committee of 110.

Table 9.3 and 9.4 show the IATA scheduled carriers operating on the North Atlantic incurring an increasing
Fig. 9.2.

North Atlantic operating results

<table>
<thead>
<tr>
<th>Year</th>
<th>Expenses (US $ million)</th>
<th>Operating Passenger Revenue</th>
<th>Operating Passenger Economic Profitability</th>
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<td>1970</td>
<td>1122</td>
<td>125</td>
<td>-</td>
</tr>
<tr>
<td>1971</td>
<td>2122</td>
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<td>1874</td>
<td>96</td>
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</tr>
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<td>(211)</td>
<td>-</td>
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<td>2357</td>
<td>(235)</td>
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<table>
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<th>Year</th>
<th>Expenses per Seat</th>
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<td>11.5</td>
<td>11.4</td>
<td>12.0</td>
<td>11.9</td>
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</table>

**Source:** ITA data, NOWA X-FACT, (1980); ITA/UN International Aviation Policy, pp. 126-127

1970 - 1978

Revenue vs Operating Expenses

ITA Scheduled North Atlantic

Table 9.4
amount of passenger operating expenses and total costs in 1978 at a rate of 24% and 22.8% respectively to that of 1977, while the passenger's total revenue growth was 20.5%.

Although the increase in operating costs may be attributed to landing fees, navigation fees, labour costs and amount of commission paid by airlines to their agents; the most important factor that plays a big share in the operating costs of aircraft and so in the formation of air fares is the price of aviation fuel.

The industry had to face spectacular increases in the cost of aviation fuel where beside the oil price increases in 1973 and 1974 the price of a gallon rose from 12 US $ in 1970 to 123 cents in 1980 (table 9.5).

The increase in fuel prices in 1973 and 1974 forced airlines to raise their air fares to cover the increased operating costs causing total traffic to drop to 12.8 and 12.4 million passengers in 1974 and 1975 respectively compared to 14 million passengers in 1973.

The aviation fuel representing 12% of total operating costs in 1970 for the North Atlantic operations rose in 1980 to represent 28%.

Fig. 9.2 refers to fuel, landing and navigation charges occurring on international scheduled passenger services where fuel costs rose at much higher rate than other costs especially since 1978.

Table 9.6 shows the impact of rising fuel cost on total world international scheduled operations where the fuel
Table 9.5

Aviation Fuel Price
US $ per Gallon

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<th>YEAR</th>
<th>US $</th>
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Table 9.6
The impact of rising fuel cost
on total world international scheduled operations

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<td>Cost per US gallon (US$) (index) *</td>
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<td>(152.5)</td>
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<td></td>
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<tr>
<td>Total operating Expense/ATK (US$) (index)</td>
<td>17.7</td>
<td>19.2</td>
<td>36.4</td>
</tr>
<tr>
<td></td>
<td>(100.0)</td>
<td>(108.5)</td>
<td>(205.6)</td>
</tr>
<tr>
<td>Fuel cost as % of total operating Expense</td>
<td>11.0</td>
<td>12.2</td>
<td>25.0</td>
</tr>
<tr>
<td>Fuel expense per ATK (US$)</td>
<td>1.95</td>
<td>2.34</td>
<td>9.1</td>
</tr>
</tbody>
</table>

* Index based on April–June 1973= 13.5¢/US gallon= 100:
earliest prices available on Route / Area basis.

+ Forecast

Source: IATA publication, (1980), 'Aviation fuel-costs conservation'.
fig. 9.2

Fuel, Landing and Navigation Unit Cost Index
International Scheduled Passenger Services
1972 = 100

Indices based on unit cost per available tonne-kilometre.
expense per available tonne-Km reached 9.1 US \$ in 1979/80 compared to 1.95 US \$ in 1972/1973. The increases in fuel cost and the fuel inefficiencies make long routes less expensive to operate and so cause carriers to move away from the short routes and this will automatically bring severe price competition on these long haul markets.

As the North Atlantic market was experiencing fierce competition and rapid growth in traffic, airlines in general were introducing new fare categories and new types of service in order to attract new segments of the public. Several new low fares such as the APEX, Super APEX and Standby were introduced to compete with non-IATA Laker's single class skytrain scheduled low fare service. These Advance Purchase Excursion fares spread later to other transatlantic markets.

Table 9.1, mentioned earlier, shows the big percentage of competition occurring on the North Atlantic IATA scheduled services to be between the various promotional fares which in 1980 represented 74% of all types of fares available. Analysing the types of fares used by passengers, the share of First class and Concorde services did not show any drastic change, except during 1972 and 1973 when they accounted for 4.8% each year, while in 1980 they represented 6.1% of total IATA North Atlantic scheduled traffic. This drop in First class, together with the drop in Normal Economy share in 1972 and 1973 have benefitted the old type
excursion fares that of 14-17/21 days and 22-29/45 days
Excursions to get 37.5% and 41.1% share of the IATA-scheduled
market for 1972 and 1973 respectively.
These old promotional excursion fares started declining
to 25.2%, 17.9%, 14.1% and 13.5% for 1977, 1978, 1979 and
1980 respectively. This decrease in Excursions was mainly
due to the introduction of new promotional low fares e.g.
APEX in 1975 and then in late 1977 Super APEX, Budget and
Standby fares which were very competitive and more attractive
to the traveller. In addition, Laker's skytrain scheduled
service introduced in late 1977 on New York-London route
and later to Los Angeles and Miami has also effected this
drop in the use of the old Excursions, where Laker's one
way fare on London-New York in winter 1977/78 mentioned
in table 9.1 was £ 59 compared to £ 293.59 and £ 254 return
fare for 14/21 and 22/45 days excursions respectively.
It is no surprise that lowering fares is applauded by the
passenger where the public is seen the main beneficiary
out of the continuous availability of low fare services
by both scheduled and charter carriers but the perceived
benefit to the traveller should not be on the expense of
diminishing returns to the carriers. So the change in fare
preference by the passenger with such a large share of
the traffic coming from these low promotional fares is
effecting and bringing profits down.
Table 9.7 refers to the US airlines' financial results for
their operation on the North Atlantic and it is quiet
clear from it that following deregulation in 1978 the
financial position of these carriers is deteriorating
Table 9.7  
Revenues, Expenses and Income  
for US carriers operating on  
North Atlantic market  
( in thousands $ )

<table>
<thead>
<tr>
<th>Carrier</th>
<th>1978</th>
<th>1979</th>
<th>1980</th>
</tr>
</thead>
<tbody>
<tr>
<td>Braniff</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Total operating Revenues</td>
<td>35,972</td>
<td>93,540</td>
<td>128,539</td>
</tr>
<tr>
<td>Total operating Expenses</td>
<td>31,791</td>
<td>110,012</td>
<td>166,010</td>
</tr>
<tr>
<td>Operating profit/Loss</td>
<td>4,181</td>
<td>-16,472</td>
<td>-37,471</td>
</tr>
<tr>
<td>Net Income</td>
<td>2,650</td>
<td>-8,521</td>
<td>-47,147</td>
</tr>
<tr>
<td>Delta</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Total operating Revenues</td>
<td>21,771</td>
<td>50,788</td>
<td>80,723</td>
</tr>
<tr>
<td>Total operating Expenses</td>
<td>19,429</td>
<td>45,406</td>
<td>81,133</td>
</tr>
<tr>
<td>Operating profit/Loss</td>
<td>2,342</td>
<td>5,382</td>
<td>-410</td>
</tr>
<tr>
<td>Net Income</td>
<td>1,268</td>
<td>3,372</td>
<td>765</td>
</tr>
<tr>
<td>Pan American</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Total operating Revenues</td>
<td>1,031,502</td>
<td>1,152,798</td>
<td>1,389,396</td>
</tr>
<tr>
<td>Total operating Expenses</td>
<td>1,016,792</td>
<td>1,133,563</td>
<td>1,441,751</td>
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<tr>
<td>Operating profit/Loss</td>
<td>14,710</td>
<td>19,235</td>
<td>-52,355</td>
</tr>
<tr>
<td>Net Income</td>
<td>-6,908</td>
<td>12,432</td>
<td>-94,682</td>
</tr>
<tr>
<td>TWA</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Total operating Revenues</td>
<td>846,248</td>
<td>925,052</td>
<td>1,060,137</td>
</tr>
<tr>
<td>Total operating Expenses</td>
<td>799,625</td>
<td>920,610</td>
<td>1,054,633</td>
</tr>
<tr>
<td>Operating profit/Loss</td>
<td>46,623</td>
<td>4,442</td>
<td>5,505</td>
</tr>
<tr>
<td>Net Income</td>
<td>83,964</td>
<td>9,151</td>
<td>5,829</td>
</tr>
<tr>
<td>Northwest</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Total operating Revenues</td>
<td>--</td>
<td>41,904</td>
<td>105,221</td>
</tr>
<tr>
<td>Total operating Expenses</td>
<td>--</td>
<td>62,955</td>
<td>134,493</td>
</tr>
<tr>
<td>Operating profit/Loss</td>
<td>--</td>
<td>-21,051</td>
<td>-29,271</td>
</tr>
<tr>
<td>Net Income</td>
<td>--</td>
<td>-8,398</td>
<td>-12,447</td>
</tr>
</tbody>
</table>

Source: CAB, 'Air Carrier Financial Statistics'.

where the operating profits and net incomes are lowered drastically despite the improvement in passenger load factors shown in table 9.8.

Therefore, it is important to realize that even if there were improvement in traffic and load factors, airlines require to improve their operating results by reducing their operating unit cost especially with the decrease in average revenues resulting from the availability of more lower fares, and to improve the industry's cost efficiency it is necessary to maintain both low costs by the new entrants and the continuing cost reduction by the major established airlines.

In referring back to the subject of fares one could say that due to the greater freedom of choice, the availability of wide range of different promotional fares beside the First and Economy class fares and the involvement and influence of governments in approving fares, the passenger fare structure seems to operate in an extremely complicated and complex situation in contrast to the prederegulatory period when pricing was simple and fares tended to relate to the cost levels of the high cost carriers.

The complicated fare structure in the North Atlantic market resembled the range of products available, even that products have a basic similar character, which have various forms of restriction to cater for a wide spectrum of demand. This complexity of fare structure brings with it management difficulties and higher airline costs.
Table 9.8

Revenue Passenger Load Factors
for US carriers operating on
North Atlantic market

<table>
<thead>
<tr>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Braniff</td>
<td>--</td>
<td>59.2</td>
<td>57.3</td>
<td>63.5</td>
</tr>
<tr>
<td>Delta</td>
<td>--</td>
<td>67.0</td>
<td>78.3</td>
<td>78.2</td>
</tr>
<tr>
<td>Pan American</td>
<td>56.6</td>
<td>61.4</td>
<td>64.3</td>
<td>65.1</td>
</tr>
<tr>
<td>TWA</td>
<td>59.5</td>
<td>68.8</td>
<td>66.9</td>
<td>63.3</td>
</tr>
<tr>
<td>Northwest</td>
<td>--</td>
<td>--</td>
<td>40.0</td>
<td>57.0</td>
</tr>
</tbody>
</table>

Notes: Braniff inaugurated its Atlantic services on 18.3.78.  
Delta " " " '" 30.4.78.  
Northwest " " " " " Feb. 79.

Source: CAB, 'Air Carrier Traffic Statistics'.
The amount of fare flexibility being available in the market and the degree to which airlines have utilized make the projection and extends of its effects difficult to realize and measure.

So with pricing being the root of the marketing strategy then the need arise for a more simplified fare structure. One remark has to be made concerning the dangers of having low fares is that a point may come when extra capacity is required to meet the severe competition and the extra demand for seats and this could mean operating at higher costs and at the same time being so high where the extra revenues derived out of selling so many extra cheap seats were not enough to meet these new operating costs, therefore a loss making situation will be created.

The industry also faces the problems of international inflation and currency fluctuations where the depreciated value of the US Dollar against most European currencies made the United States more attractive destination for foreign travellers and the increased availability of low fares brought a boom in non-USA originating traffic where scheduled carriers operating between Europe and United States recorded an increase of 14.8% in non-US citizens with only 1% in US citizens in 1980. The total scheduled and charter US citizens share of traffic between Europe and USA declined by 2.5% and 5.9% in 1979 and 1980 compared to a growth of 23.2% and 12.5% for non-US citizens for the same years as shown in table 9.9.
<table>
<thead>
<tr>
<th>Year</th>
<th>Total (000)</th>
<th>% Change</th>
<th>Total (000)</th>
<th>% Change</th>
<th>Total (000)</th>
<th>% Change</th>
<th>Total (000)</th>
<th>% Change</th>
<th>Total (000)</th>
<th>% Change</th>
<th>Total (000)</th>
<th>% Change</th>
</tr>
</thead>
<tbody>
<tr>
<td>1975</td>
<td>1,213</td>
<td>-</td>
<td>881</td>
<td>-</td>
<td>1,722</td>
<td>-</td>
<td>1,213</td>
<td>-</td>
<td>880</td>
<td>-</td>
<td>1,722</td>
<td>-</td>
</tr>
<tr>
<td>1976</td>
<td>1,221</td>
<td>2.1%</td>
<td>913</td>
<td>2.1%</td>
<td>1,334</td>
<td>5.9%</td>
<td>1,221</td>
<td>2.1%</td>
<td>913</td>
<td>2.1%</td>
<td>1,334</td>
<td>5.9%</td>
</tr>
<tr>
<td>1977</td>
<td>1,229</td>
<td>2.5%</td>
<td>941</td>
<td>2.4%</td>
<td>1,448</td>
<td>9.3%</td>
<td>1,229</td>
<td>2.5%</td>
<td>941</td>
<td>2.4%</td>
<td>1,448</td>
<td>9.3%</td>
</tr>
<tr>
<td>1978</td>
<td>1,231</td>
<td>2.2%</td>
<td>946</td>
<td>2.1%</td>
<td>1,457</td>
<td>6.4%</td>
<td>1,231</td>
<td>2.2%</td>
<td>946</td>
<td>2.1%</td>
<td>1,457</td>
<td>6.4%</td>
</tr>
<tr>
<td>1979</td>
<td>1,235</td>
<td>2.6%</td>
<td>959</td>
<td>3.0%</td>
<td>1,470</td>
<td>9.5%</td>
<td>1,235</td>
<td>2.6%</td>
<td>959</td>
<td>3.0%</td>
<td>1,470</td>
<td>9.5%</td>
</tr>
<tr>
<td>1980</td>
<td>1,243</td>
<td>2.3%</td>
<td>968</td>
<td>3.9%</td>
<td>1,484</td>
<td>9.1%</td>
<td>1,243</td>
<td>2.3%</td>
<td>968</td>
<td>3.9%</td>
<td>1,484</td>
<td>9.1%</td>
</tr>
</tbody>
</table>

One final criterion to be mentioned that has shown an important and crucial significance in studying and analysing the North Atlantic operations concerns the capacity of supply offered by airlines.

A surplus in seating capacity is being developed and brought into the market due to the increase in flight frequencies especially at a time when frequencies are considered crucial in achieving market domination when no multilateral understanding and agreement can be reached to cut frequencies, the expansion in the number of points served by the carriers when in many new bilateral air agreements the U.S. and foreign airlines were authorised to serve many US cities beside New York, the use of large wide body size aircrafts, and the arrival of new carriers, all this resulted in an uneconomical breakeven load factors as the traffic dispersed into extra number of routes.

Table 9.10 shows the traffic carried by the individual airlines operating on the North Atlantic with most of these new comers appearing in late seventies as a result of the liberalized situation created in the market where entry has been freely open to new airlines following signing new air service agreements by the United States with the United Kingdom and some other European countries mentioned in earlier chapter.

In concluding this chapter one can say that the pressure and the threat on the established carriers from new entrants will always be there where the potential for new airlines to enter the market will exist with the initial capital
Table 9.10
Total North Atlantic traffic by individual carriers 1972 - 1980

<table>
<thead>
<tr>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>1- British Airways</td>
<td>1,165</td>
<td>1,350</td>
<td>1,153</td>
<td>1,217</td>
<td>1,358</td>
<td>1,797</td>
<td>2,100</td>
<td>2,106</td>
<td></td>
</tr>
<tr>
<td>2- British Caledonian</td>
<td>-</td>
<td>86</td>
<td>66</td>
<td>-</td>
<td>7</td>
<td>71</td>
<td>95</td>
<td>149</td>
<td></td>
</tr>
<tr>
<td>3- Pan American</td>
<td>2,069</td>
<td>2,391</td>
<td>1,791</td>
<td>1,643</td>
<td>2,070</td>
<td>2,030</td>
<td>2,146</td>
<td>2,521</td>
<td>2,230</td>
</tr>
<tr>
<td>4- TWA</td>
<td>2,084</td>
<td>1,920</td>
<td>1,797</td>
<td>1,736</td>
<td>2,055</td>
<td>2,017</td>
<td>2,417</td>
<td>2,491</td>
<td>2,352</td>
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<tr>
<td>5- Air Canada</td>
<td>692</td>
<td>763</td>
<td>762</td>
<td>741</td>
<td>733</td>
<td>614</td>
<td>793</td>
<td>856</td>
<td>844</td>
</tr>
<tr>
<td>6- CP Air</td>
<td>219</td>
<td>238</td>
<td>261</td>
<td>290</td>
<td>316</td>
<td>369</td>
<td>392</td>
<td>400</td>
<td>453</td>
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<tr>
<td>7- Aer Lingus</td>
<td>281</td>
<td>277</td>
<td>247</td>
<td>198</td>
<td>215</td>
<td>227</td>
<td>290</td>
<td>327</td>
<td>268</td>
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<tr>
<td>8- Air France</td>
<td>638</td>
<td>624</td>
<td>632</td>
<td>613</td>
<td>647</td>
<td>677</td>
<td>717</td>
<td>723</td>
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<td>9- SAS</td>
<td>417</td>
<td>474</td>
<td>402</td>
<td>401</td>
<td>460</td>
<td>480</td>
<td>521</td>
<td>556</td>
<td>524</td>
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<td>10- Alitalia</td>
<td>590</td>
<td>535</td>
<td>513</td>
<td>427</td>
<td>441</td>
<td>491</td>
<td>522</td>
<td>504</td>
<td>534</td>
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<td>11- Sabena</td>
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<td>265</td>
<td>243</td>
<td>253</td>
<td>232</td>
<td>213</td>
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<td>12- Iberia</td>
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<td>304</td>
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<td>235</td>
<td>250</td>
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<td>297</td>
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<td>246</td>
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<td>641</td>
<td>673</td>
<td>748</td>
<td>792</td>
<td>875</td>
<td>929</td>
<td>1,051</td>
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<td>610</td>
<td>660</td>
<td>607</td>
<td>593</td>
<td>642</td>
<td>655</td>
<td>703</td>
<td>789</td>
<td>818</td>
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<tr>
<td>22- Braniff</td>
<td>-</td>
<td>-</td>
<td>-</td>
<td>-</td>
<td>-</td>
<td>-</td>
<td>118</td>
<td>333</td>
<td>397</td>
</tr>
<tr>
<td>23- PIA</td>
<td>9</td>
<td>-</td>
<td>-</td>
<td>-</td>
<td>23</td>
<td>33</td>
<td>39</td>
<td>39</td>
<td>57</td>
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<tr>
<td>24- CSA</td>
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<td>NA</td>
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<td>NA</td>
<td>NA</td>
<td>27</td>
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<td>25- Royal Air Maroc</td>
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<td>28</td>
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<td>NA</td>
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<tr>
<td>29- Laker</td>
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<td>253</td>
<td>NA</td>
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<tr>
<td>30- Delta</td>
<td>-</td>
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<td>-</td>
<td>-</td>
<td>79</td>
<td>NA</td>
<td>252</td>
<td></td>
<td></td>
</tr>
<tr>
<td>31- Northwest</td>
<td>-</td>
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<tr>
<td>32- Capital</td>
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<td>33- Trans America</td>
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<td>34- Air Florida</td>
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<td>35- World</td>
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<td>36- Western</td>
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</tr>
<tr>
<td>37- Air Berlin</td>
<td>-</td>
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<td>-</td>
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<td>2</td>
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</tr>
<tr>
<td>38- Kuwait Airways</td>
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</tbody>
</table>

Total 13,013 14,027 12,859 12,418 13,834 15,122 16,828 18,589 18,775

investment needed to start and operate is not enormous like that in other industries and especially with lower operating costs. But a point will come where the operating costs of these newly entered carriers will rise to meet the extra or new costing obligation to satisfy a higher number and possibly divergent type of passengers. Also when the established carriers lower their cheapest restricted excursion fares in the off-season to match the unrestricted low fare offered by the charter or the new comers, a situation of much confusion could arise where such established carriers as British Airways might face criminal and civil anti trust suits in United States courts if say a lower fare British carrier such as Laker Airways or any new carrier that might appear in the future to operate on the UK-USA market were unable to survive the heightened fare competition due to the introduction of these low fares by the established. With the new pressures of increased deregulation, the airlines to survive need to be more efficient in their operation and to be innovative they require to be effectively competitive and profitable.
CONCLUSIONS
CONCLUSIONS:

Having investigated and examined the North Atlantic market by looking at its crucial issues of capacity and competition, the researcher now focuses on the final conclusions reached out of the study on which his remedial actions to the crisis lay upon:

1- The American experience of deregulation:

With United States looking toward competition as the only possible way for air transport industry to operate at healthy environment does not mean that other countries have to change and accept accordingly.

As no evidence available to suggest that deregulation in the USA had achieved satisfactory results in the early years of its implementation, it is surprising that the American Administration should embark so quickly in applying it into an international market, such as the North Atlantic, involved with many different nations by exerting pressure on others especially the European countries to follow suit in accepting deregulation.

It would have been more reasonable if deregulation of the US airline industry had been given more time to reshape business domestically and for its practical effects to be valued, only then the international community would have been in a position to accept the economic advantages and the practicality of such a change, instead of being so quick in thrusting it upon other unwilling countries when its first experiment had not yet been proved workable.

So it could indeed be said that this unilateral practice
by the United States, in imposing its own views of what it thinks best in the public interest, can prove very difficult for other countries to swallow.

The political and socio-economic barriers existing between various countries brings operating restrictions on many international airlines. With the need by the international community for an extensive network of regular and reliable air services together with the necessity for a body such as IATA to control negotiation of fares to reach compromise formula that take into account the diverse economic and monetary circumstances as well as the various categories of demand, therefore the competition process needs a regulatory framework within which to operate effectively.

Internationally, the moves towards deregulation seem complicated by the sheer fact that no common political framework or system exist that suits and satisfies all the countries.

But, on the other hand, one has not to be reluctant in admitting to consider competition in air transport as a process that would enable or make use of new and better ideas. There still be space to accept the idea that competition is the force that will keep the market volatile and providing different levels of service to the public at an economical and feasible level for the airlines, but the fact is that this will only be realised efficiently if there remain some guiding restrictions as a framework within which to exercise the competition process.
2- The satisfaction out of air policies:

The availability of more than one airline operating international services in one country with one being privately owned and the other being partially or wholly controlled by government would need an air policy that ensures the satisfaction for both carriers where having a profitable airline would require not the same understanding and approach to that of serving as a public utility. Owing to the fact that the North Atlantic market involves many European countries together with United States and Canada, then it is very important to realize that these countries have wide range of policies that are not always similar.

The varying economic and political systems that exist even in Europe where most countries are members of the European Economic Community (EEC), have caused vastly different economic approaches to civil aviation to emerge, this is, of course, specially relevant in the democracies where the election of new government is often marked by great shifts in political and economical ideology. This diversity of economic systems means each country has its own and different approach in achieving its economic objectives with the objective of maintaining its airline industry being part of this economic reality. Therefore it would be no surprise that the air policy objectives of one country e.g. the United States might not be compatible with other countries requirements, and so the reconciliation between them looks difficult to accomplish.
3- The multilateral harmony:

It has been widely accepted that bilateral agreements tend to be the only really effective international regulatory means available to the air transport industry when multilateral agreements cannot be reached.

But if these agreements are formulated for the benefit of international interests, then individual countries should not be permitted to introduce and peddle on unfavourable policy leaving the other members of the international community being forced into conforming with alien policies to their own detriment.

In these circumstances bilateral agreements may even be a step away from the introduction of acceptable policies to the international scene when one country e.g. the United States apply its open sky policy in bilateral agreement as tactical step to force the results of this bilateral agreement to be accepted by other countries no matter how unfortunate results had that bilateral agreement produced.

With the bilateral agreements approach being machined and implemented, where the capacity issue has been dealt with, and as the market involves so many airlines, routes and countries, then the effectiveness would be more if a multilateral approach is sought to bring together the capacity limitation issue on a broader scale than leaving it to the dual understanding and agreement of only the two countries concerned in each particular bilateral agreement.
Also the capacity reduction measure should only be taken as part of wider scale of action including the costs reduction so that this capacity reduction does not take the shape of harming the scheduled convenience of having very high load factors, therefore a balance of interests must be maintained in achieving these two objectives. In achieving the objectives of having lower costs by cutting flight frequencies and being effective in not harming the scheduled quality, would require the redistribution of the availability of types of fares where the business sector would not be effected in obtaining the seats required at relatively no change and by making the allocation acceptable to all the different type of passengers.

4- The governmental and political role:

It is very important to notice the fact that the influence and role of many governments in their airlines' affairs will not change dramatically in the near future due to the great determination of most governments in protecting their national airlines. It is essential to remember that when negotiating and approving fares for their airlines, governments tend to consider and protect the commercial features within the pricing policies where they do not jeopardize the survival and continuity of their carriers. The determination of governments is maintained as long as the airline industry continue attracting tourists and business passengers and providing foreign currency beside the political and economical importance.
For that reason, the continuing existence of international airlines is a reality that need no questioning in which they will remain being subsidised by their governments where these airlines have been trying to stay in the market, meeting fierce competition and striving to keep their market share only by disregarding the costs of competitiveness.

The international scheduled airlines, especially those of western Europe operating on the North Atlantic, who are either partially or wholly government controlled and whom tend to be the main international airlines (flag carriers) of their countries would remain and continue providing services at uneconomical fares whom it won't be realistic for these countries to leave their carriers with financial difficulties but to rush in helping them to avoid their collapse, this is so as long as:

a- these governments are accepting and adhering to the undisputable importance of the International Air Transport Association (IATA) where no other workable and replaceable machinery has been introduced to meet the general consent of the interested parties.

Here it is essential not to forget that IATA is the body approved by most of world airlines to set air fares and it is the creation of governments and not a private cartel with the special and peculiar power of these governments in it;

b- the International Civil Aviation Organisation (ICAO), whom most if not all of the countries concerned are part
of, continue providing its support to IATA machinery; 
c- the machinery and influence of air regulatory bodies 
of most countries in most cases remains under the advise 
and control of governments; and 
d- there is no compromise on the issues of meeting the 
demands and the interests of passengers, airlines and 
nations and in ensuring the long term economic stability 
of the industry. So here, one has to raise one simple 
question, can the air carriers meet these two fundamental 
obligations that of providing services and of receiving 
a reasonable rate of return? 

Finally, the researcher concludes not to leave the 
international air transport industry to the mercy of one 
particular system, advocated by only one sector of this 
important and sensitive market, to be forced upon and 
implemented by other unwilling countries. 
One has to keep in mind in answering what would be best 
for the whole industry one simple fact: 
Should the industry allow the present competitive and 
deregulatory trends in the airlines' operations to continue 
and expand in such a free open skies style expecting bad 
financial results with the possibility of more airlines 
going out of business, or should it seek a wider measure 
of understanding allowing a system of controlled 
competition which protects the interests not only of 
carriers but of passengers too as well as the industry 
itsel with all its international multiplicity.
SUGGESTIONS FOR FURTHER RESEARCH:

During the course of the work, the researcher faced many questions that could be a starting material for further research within the subject of competition and capacity in the air transport industry as a whole or specifically on North Atlantic.

These questions fall entirely within the boundaries of marketing management approach.

If the researcher was to pursue a new work, then he would surely not miss one of the following issues:

a- The functions performed by the different non-price competitive factors, if considered to be more effective in building sales than the equivalent of a price reduction, can appeal to air traveller and they may help to secure more consumer loyalty where a lower fare may not be significant enough to be noticed by some passengers.

b- To test whether each passenger has a pattern of preference toward a particular type of air service reflected in the frequencies with which he or she uses that service, and that these preferences change relatively slowly over the time.

c- Does advertising, as a product differentiation criterion, curtail competition in the open sky-freedom air policy approach by putting up the cost of entry and limiting price competition and so making demand for travel more inelastic.

**************
APPENDIX I

RECOMMENDATIONS

To enable the air transport industry on the North Atlantic achieve the objectives of all interested parties in providing an adequate level of services to the travelling public and at the same time maintain a strong, efficient and commercially effective industry, the following remedial actions can be recommended:

1- The achievement of profitability by the airlines and the fulfilment of public service depend on the co-ordination of both governments and airlines. Governments have to resolve the basic regulatory policy differences which have contributed to the air carriers' economic decline in recent years and should at the same time discourage their carriers from increasing their supply of capacity.

2- A joint investigation by the airlines is urgently required to examine tariffs and ways of adjusting supply to meet the differing types of demand. From the general marketing point of view, market research is needed, the passengers' views must be more accurately determined concerning low fares, the effect they have on quality of service, and how they might wish their money be better used while at the same time understanding the airlines' legitimate need to sell more seats and keep costs down. This may be done by testing the market and finding out how the air traveller is accepting high fares by measuring the elasticity of demand principally at a time when costs are not coming down.
Any successful policy aimed at the growth of passenger traffic has to remember that air fares must remain affordable by the passengers.

3- A greater sense of recognition is required by all parties concerned of the importance of costs factor when pricing and setting fares, also that improvements in load factors and more revenue from each flight are two essential prerequisites of future profitability.

In addition, as the fuel prices effect and play a big role in the high trend in costs, the recent changes occurring in world oil prices may ease the pressure on airlines.

4- Achieving a better load factor will not by itself solve all the problem, there should be better utilisation of the capacity provided and at the same time passengers have to be paying fares that are built and related to costs thus resulting in higher yields.

5- With a view to the new noise regulations which will come in force in 1986 where many airlines are seeking to change and modernise their fleets to meet these new requirements, there is thus a remarkable opportunity for those concerned to agree now on how to reconstruct their capacity and plan to meet realistically the actual demand for scheduled services, at the same time there must be understanding with the non-scheduled carriers in order to reach new bilateral agreements which settle the capacity issues.

A free for all open-sky policy cannot help the industry
to get out of its present crisis and complex situation, and in the absence of greater international understanding, resort must be made to the traditional machinery of such bilateral air agreements. Here one must note that neither a return to the old policy of total regulation would help the situation, and on the other hand it would only force the industry to suffer more and damage the economy of many countries in continuing advocating liberalisation in that seeking immediate profit while neglecting the long range importance of the industry to all of us and the generations to come and its value for the world's economy. It is not up to a few to impose their will on the industry with threats to implement the rules of competition, rather than that the industry should seek survival at healthy environment and by giving fair and equal opportunity for all to participate and within agreed rules which everyone subscribes to and accept.

6- The notion of equal opportunity should be given more consideration when setting international air policies. It is unrealistic to regard equal opportunity to compete as currently existing while no conditions are laid down of who is allowed to make use of these opportunities and without there being clearly accepted distinctions and definitions of the diverse markets in which particular airlines have a stake. To allow a large established scheduled international carrier e.g. British Airways or Pan American and a
supplemental carrier e.g. World Airways or Laker to operate in the same market and with identical rules cannot be considered competition on an equal basis. It would be too easy for Laker to skim the benefit of competition by achieving higher load factors and higher yields out of their revenue while having substantially lower operating costs. While the scheduled airline is left to uphold the public interest by operating all the various unrewarding routes with necessarily much higher operating expenses.

On the other hand, it would not be considered a fair and equal opportunity when these established carriers can use their great resources together with the direct or indirect subsidies made available to them by their governments, in such a shrewd and tactical way to match the low fares applied by those low cost carriers no matter how uneconomical they are and go even further to offer lower fares, in that dragging airlines to follow suit. Such action may cause the low cost carriers not being able to continue as they have to go into providing new capacities to be competitive and attractive to passenger. The inability of continuing in such difficult financial circumstances will surely mean unfair and unequal opportunity for airlines to operate.

**********
APPENDIX II: ROUTES SCHEDULE OF BERMUDA AGREEMENT II

Section 1: Scheduled Combination Air Service Routes for the United States

US Route 1: Atlantic Combination Air Service

<table>
<thead>
<tr>
<th>Gateway Points</th>
<th>Intermediate Points</th>
<th>Points in UK Territory</th>
<th>Points Beyond</th>
</tr>
</thead>
<tbody>
<tr>
<td>Anchorage</td>
<td></td>
<td>London</td>
<td>Frankfurt</td>
</tr>
<tr>
<td>Atlanta</td>
<td></td>
<td></td>
<td>Hamburg</td>
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<tr>
<td>Boston</td>
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<td></td>
<td>Munich</td>
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<tr>
<td>Chicago</td>
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<td>Berlin</td>
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<tr>
<td>Dallas/Ft. Worth</td>
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<td>Detroit</td>
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<tr>
<td>Houston</td>
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<tr>
<td>Los Angeles</td>
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<td>Miami</td>
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<td>New York</td>
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<td>Philadelphia</td>
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<tr>
<td>San Francisco</td>
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<tr>
<td>Seattle</td>
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<tr>
<td>Washington/Baltimore</td>
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</tbody>
</table>

An additional point to be agreed between the Contracting Parties.

- May not be served nonstop until three years after this Agreement enters into force.
- In addition, Austria and Belgium may be served for three years after this Agreement enters into force; the Netherlands, Norway and Sweden may be served for five years after the Agreement enters into force; and these points shall be considered as appearing in Column (D) for the specified periods.
- Only one United States airline may be designated to serve each point in Column (D) on this route, including those in footnote 2, except for Frankfurt for which two airlines may be designated on US Routes 1 and 2 taken together.

US Route 2: Round the World Combination Air Service

<table>
<thead>
<tr>
<th>Gateway Points</th>
<th>Intermediate Points</th>
<th>Points in UK Territory</th>
<th>Points Beyond</th>
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<tbody>
<tr>
<td>New York</td>
<td></td>
<td>London</td>
<td>Frankfurt</td>
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<tr>
<td>Washington/Baltimore</td>
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<td>Turkey</td>
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<tr>
<td>Seattle</td>
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<td>Lebanon</td>
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<td>Los Angeles</td>
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<td>Syria</td>
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<td>San Francisco</td>
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<td>Tokyo</td>
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<td>Pakistan</td>
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<td>Bangkok</td>
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<td>New Delhi</td>
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<tr>
<td>Bangkok</td>
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<td>Calcutta</td>
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</tbody>
</table>

Points on Segment (a):

- Not more than seven flights per week may operate in each direction on each segment.
- Not more than two United States airlines may be designated to serve Frankfurt on US Routes 1 and 2, taken together.
- Segments (a) and (b) shall be combined, except as may be agreed pursuant to Article 2, paragraphs (3).
## Section 3: Scheduled Combination Air Service Routes for the United Kingdom

### UK Route 1: Atlantic Combination Air Service

**UK Gateway Points**
- London
- Manchester
- Prestwick/Glasgow

**Intermediate Points**

<table>
<thead>
<tr>
<th>Points in US Territory</th>
</tr>
</thead>
<tbody>
<tr>
<td>Atlanta(*)</td>
</tr>
<tr>
<td>Boston</td>
</tr>
<tr>
<td>Chicago</td>
</tr>
<tr>
<td>Dallas/Ft. Worth(*)</td>
</tr>
<tr>
<td>Detroit</td>
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<tr>
<td>Houston</td>
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<tr>
<td>Los Angeles</td>
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<td>Miami</td>
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<tr>
<td>San Francisco</td>
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<tr>
<td>Seattle</td>
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<tr>
<td>Washington/Baltimore</td>
</tr>
</tbody>
</table>

**Points Beyond**

(*) May not be served nonstop until three years after this Agreement enters into force.

### UK Route 2: Atlantic Combination Air Service via Canada

**UK Gateway Points**
- London
- Manchester
- Prestwick/Glasgow

**Intermediate Points**
- Canada

**Points in US Territory**
- Boston
- Chicago
- Dallas/Ft. Worth(*)
- Detroit
- New York
- Philadelphia
- Washington/Baltimore

**Points Beyond**

### UK Route 3: Atlantic Combination Air Service Beyond to Mexico City

**UK Gateway Points**
- London
- Manchester
- Prestwick/Glasgow

**Intermediate Points**

<table>
<thead>
<tr>
<th>Points in US Territory</th>
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</thead>
<tbody>
<tr>
<td>Boston</td>
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<td>Detroit</td>
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<tr>
<td>New York</td>
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<tr>
<td>Philadelphia</td>
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<tr>
<td>Washington/Baltimore</td>
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</tbody>
</table>

**Points Beyond**

(*) May not be served nonstop until three years after this Agreement enters into force.
**UK Route 4: Atlantic Combination Air Service Beyond to South America**

<table>
<thead>
<tr>
<th>(A) UK Gateway Points</th>
<th>(B) Intermediate Points</th>
<th>(C) Points in US Territory</th>
<th>(D) Points Beyond</th>
</tr>
</thead>
<tbody>
<tr>
<td>London</td>
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<td>Atlanta(*)</td>
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<td>Manchester</td>
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<td>Colombia</td>
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<tr>
<td>Prestwick/Glasgow</td>
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<td>Manaus</td>
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<td></td>
<td></td>
<td></td>
<td>Peru(*)</td>
</tr>
</tbody>
</table>

**UK Route 5: Atlantic Combination Air Service Beyond to Japan**

<table>
<thead>
<tr>
<th>(A) UK Gateway Points</th>
<th>(B) Intermediate Points</th>
<th>(C) Points in US Territory</th>
<th>(D) Points Beyond</th>
</tr>
</thead>
<tbody>
<tr>
<td>London</td>
<td></td>
<td>Anchorage</td>
<td>Japan</td>
</tr>
</tbody>
</table>

(*) May not be served nonstop until three years after this Agreement enters into force.

(*) Without rights to carry local traffic between Houston and Peru.
APPENDIX III

ARTICLE 11 OF BERMUDA TWO AGREEMENT (FAIR COMPETITION)

(1) The designated airline or airlines of one contracting party shall have a fair and equal opportunity to compete with the designated airline or airline of the other contracting party.

(2) These designated airline or airlines of one contracting party shall take into consideration the interests of the designated airline or airlines of the other contracting party so as not to affect unduly that airline's or those airlines' services on all or part of the same routes. In particular, when a designated airline of one contracting party proposes to inaugurate services on a gateway route segment already served by a designated airline or airlines of the other contracting party, the incumbent airline or airlines shall each refrain from increasing the frequency of their services to the extent and for the time necessary to ensure that the airline inaugurating service may fairly exercise its rights under paragraph (1) of this article. Such obligation to refrain from increasing frequency shall not last longer than two years or beyond the point when the inaugurate airline matches of the frequencies of any incumbent airline, whichever occurs first, and shall not apply if the services to be inaugurated are limited as to their capacity by the licence or certificate granted by the designating contracting party.

(3) Services provided by a designated airline under this Agreement shall retain as their primary objective the
provision of capacity adequate to the traffic demands between the country of which such airline is a national and the country of ultimate destination of the traffic. The right to embark or disembark on such services international traffic destined for and coming from third countries at a point or points on the routes specified in this agreement shall be exercised in accordance with the general principles of orderly development of international air transport to which both contracting parties subscribe and shall be subject to the general principle that capacity should be related to:

(a) the traffic requirements between the country of origin and the countries of ultimate destination of the traffic;
(b) the requirements of the area through which the airline passes, after taking account of local and regional services; and
(c) the requirements of through airline operations.

(4) The frequency and capacity of services to be provided by the designated airlines of the contracting parties shall be closely related to the requirements of all categories of public demand for the carriage of passengers and cargo including mail in such a way as to provide adequate service to the public and to permit the reasonable development of routes and viable airline operations. Due regard shall be paid to efficiency of operation so that frequency and capacity are provided at levels appropriate to accommodate the traffic at load factors
consistent with tariffs based on the criteria set forth in paragraph (2) of Article 12 (Tariffs).

(5) The contracting parties recognize that airline actions leading to excess capacity or to the underprovision of capacity can both run counter to the interests of the travelling public. Accordingly, in the particular case of combination air services on the North Atlantic routes specified in paragraph (1) of Annex 2, they have agreed to establish the procedures set forth in Annex 2. With respect to other routes and services, if one contracting party believes that the operations of a designated airline or airlines of other Contracting Party have been inconsistent with the principles set forth in this Article, it may request consultations pursuant to Article 16 (Consultations) for the purpose of reviewing the operations in question to determine whether they are in conformity with these principles. In such consultations there shall be taken into consideration the operations of all airlines serving the market in question and designated by the contracting party whose airline or airlines are under review. If the Contracting Parties conclude that the operations under review are not in conformity with the principles set forth in this Article, they may decide upon appropriate corrective or remedial measures, except that, where frequency or capacity limitations are already provided for a route specified in Annex 1, the Contracting Parties may not vary those limitations or impose additional limitations except by amendment of this Agreement.
(6) Neither Contracting Party shall unilaterally restrict the operations of the designated airlines of the other except according to the terms of this Agreement or by such uniform conditions as may be contemplated by the Convention.
APPENDIX IV
SECTION 102 OF THE AIRLINE DEREGULATION ACT OF 1978

In the exercise and performance of its powers and duties under this Act with respect to interstate and overseas air transportation, the Board shall consider the following, among other things, as being in the public interest, and in accordance with the public convenience and necessity:

(1) The assignment and maintenance of safety as the highest priority in air commerce, and prior to the authorisation of new air transportation services, full evaluation of the recommendations of the Secretary of Transportation on the safety implications of such new services and full evaluation of any report or recommendation submitted under section 107 of this Act.

(2) The prevention of any deterioration in established safety procedures, recognizing the clear intent, encouragement, and dedication of the Congress to the furtherance of the highest degree of safety in air transportation and air commerce, and the maintenance of the safety vigilance that has evolved within air transportation and air commerce and has come to be expected by the travelling and shipping public.

(3) The availability of a variety of adequate, economic, efficient, and low-price services by air carriers without unjust discriminations, undue preferences or advantages, or unfair or deceptive practices, the need to improve relations among, and co-ordinate transportation by, air carriers, and the need to encourage fair wages and equitable working conditions.
(4) The placement of maximum reliance on competitive market forces and on actual and potential competition (A) to provide the needed air transportation system, and (B) to encourage efficient and well managed carriers to earn adequate profits and to attract capital.

(5) The development and maintenance of a sound regulatory environment which is responsive to the needs of the public and in which decisions reached promptly in order to facilitate adaption of the air transportation system to the present and future needs of the domestic and foreign commerce of the United States, the Postal Service, and the national defence.

(6) The encouragement of air service at major urban areas through secondary or satellite airports, where consistent with regional airport plans of regional and local authorities, and when such encouragement is endorsed by appropriate State entities encouraging such service by air carriers whose sole responsibility in any specific market is to provide service exclusively at the secondary or satellite airport, and fostering an environment which reasonably enables such carriers to establish themselves and to develop their secondary or satellite airport services.

(7) The prevention of unfair, deceptive, predatory, or anticompetitive practices in air transportation, and the avoidance of-

(A) unreasonable industry concentration, excessive market domination, and monopoly power; and

(B) other conditions;

that would tend to allow one or more air carriers unreason-
ably to increase prices, reduce services, or exclude competition in air transportation.

(8) The maintenance of a comprehensive and convenient system of continuous scheduled airline service for small communities and for isolated areas, with direct Federal assistance where appropriate.

(9) The encouragement, development and maintenance of an air transportation system relying on actual and potential competition to provide efficiency, innovation, and low prices, and to determine the variety, quality, and price of air transportation services.

(10) The encouragement of entry into air transportation markets by new air carriers, the encouragement of entry into additional air transportation markets by existing air carriers, and the continued strengthening of small air carriers so as to assure a more effective, competitive airline industry.

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