



THE AIR TRANSPORT INDUSTRY IN THE REAR-VIEW MIRROR

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A QUOTE OF JEFFREY SHANE:

“Now that deregulation, liberalization, and even Open Skies are default policies for aviation in so much of the world, it’s easy to forget what a revolution in public policy these developments represented. Even those of us who lived through the transition have difficulty remembering how crazy it used to be.”

Jeffrey N. Shane the United States Undersecretary of Transportation for Policy,
US Department of Transportation (DOT) from 2003 to 2008

HOW CRAZY WAS IT IN 1984, WHEN I JOINED THE RLD?

- Just a few examples:
 - the distorted capacity balance between FR-NL had to be restored
 - Inclusive tour passengers were separated from 'camping trip makers' on charter flights to Greece
 - KLM had to pay royalties to BA for each KLM-transfer passenger via Amsterdam to London
 - Pooling agreements prevented European airlines from competition

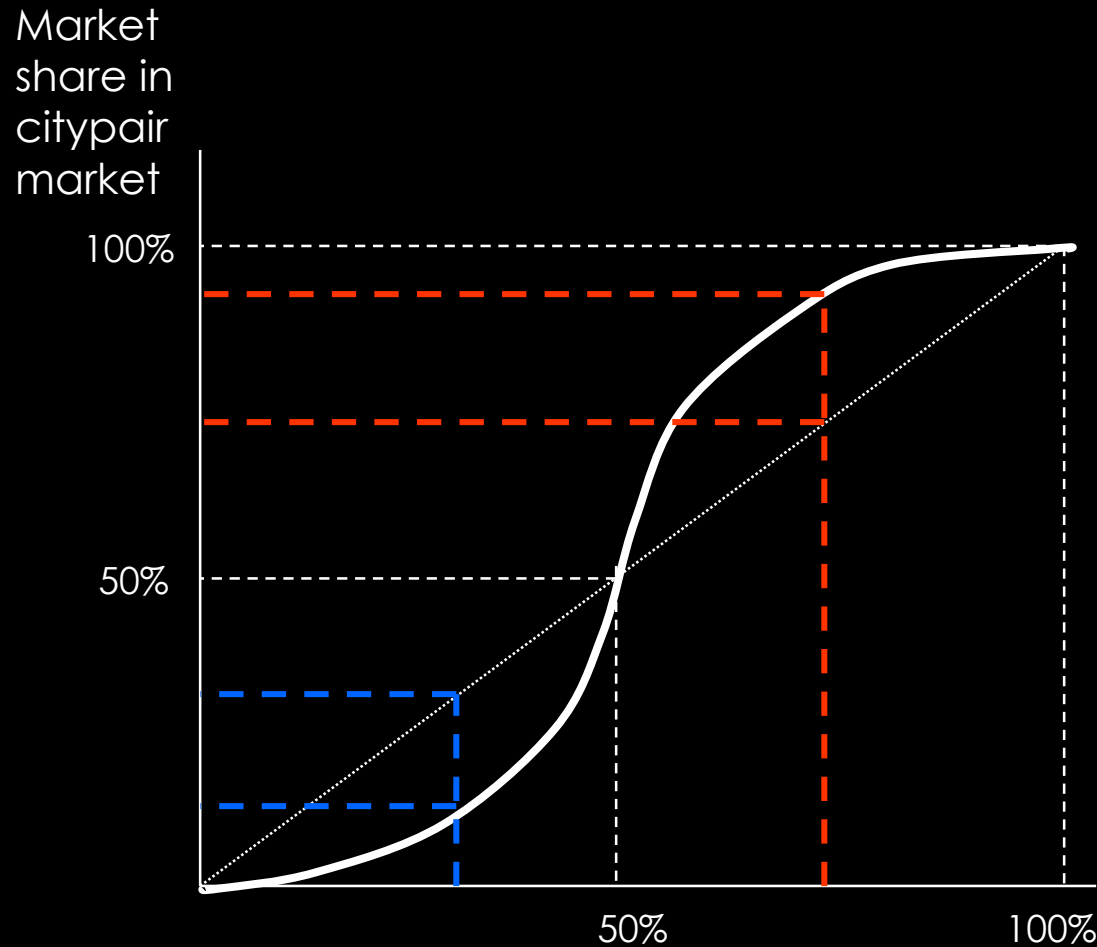
THE RLD: THE OPPOSITE OF PARKINSON'S LAW

- **Parkinson's law:** the smaller the British Empire the bigger the Colonial Office in the UK
- In 1984 the RLD was a kingdom in the Kingdom (aviation was a 'service publique')
 - A pilot school in Eelde (sold for fl.1 to KLM)
 - A safety oversight directorate also for the certification of new Fokker aircraft (currently an understaffed part of ILT inspectorate)
 - An air traffic control directorate (now a separate public body to allow for exceptional salaries surpassing that of the MP)
 - An economic/legal/air-transport policy directorate
 - An airports policy directorate
- Current staff of the air transport directorate within the ministry concerns about 25 fte's, while air transport in the Netherlands increased from 11 mln pax in 1984 to 70 mln now

BUT 1984 WAS AN EXCITING YEAR!

- Since 5 years the US domestic market had been deregulated and US carriers started to re-invent the hub & spoke system (SIN, AMS 6th freedom hubs already existed for quite some time!) De Neufville of MIT disagreed!
- First liberal European BASA concluded: UK-NL
 - Multiple designation
 - Market access: any point in either country 3d + 4th freedom
 - No capacity restrictions
 - Double disapproval of fares
- Shortly thereafter for the first time three competitors popped up on a European route.

frequency competition intensified



- BMA immediately matched the frequencies of BA and KLM on LON-AMS, be it with smaller aircraft

- Today the S-curve no longer holds for LCCs: frequency competition has been replaced by fare competition.

Frequency share
at a city pair with
two competing airlines

IN THE EIGHTIES MY COLLEAGUE GOT FRUSTRATED EVERY WEEK WHEN HE RETURNED FROM BRUSSELS

- My colleague was appointed in 1985 'to do the Brussels business'
- But he was talking to deaf ears at home: the consequences of the Nouvelles Frontières judgement (1986) remained a rather abstract issue in our office.
- Surprise however: a stepwise liberalization into a single aviation market was ready for implementation in 1987 and almost completed in 1993.
- In that period the popularity of my colleague skyrocketed in The Hague
- However, aviation in the single market didn't change much in the nineties, only the advise of the Comité des Sages put an end to state aid: 'one time, last time'
- Note that since then some Member States continued to suffer from dyscalculia.

A DAY IN SEPT 1992: KLM'S CEO WELCOMES MY COLLEAGUES AT THE GATE WITH FLOWERS

- NL was used again by the USA as test bed to start a new bilateral open skies policy.
- First Open Skies BASA (versus Open Market BASA USA-NL 1978)
 - Multiple designation (1978 idem)
 - Any point in the US and 'any point' in the Netherlands (in 1978 only five points in the US)
 - No capacity or frequency restrictions (1978 idem)
 - unlimited 5th freedom rights (quasi cabotage for US carriers in Europe)
 - No tariff controls (Double disapproval of fares in 1978)
 - Unlimited charter rights (idem 1978)
 - Break of gauge as well as code sharing permitted
- BUT: neither cabotage within the US nor foreign ownership relaxation in US carriers (neither allowed in the EU-US Open Skies agreement in 2007)!

THE SECOND STEP AFTER THE OPEN SKIES BASA: CREATING THE FIRST ALLIANCE

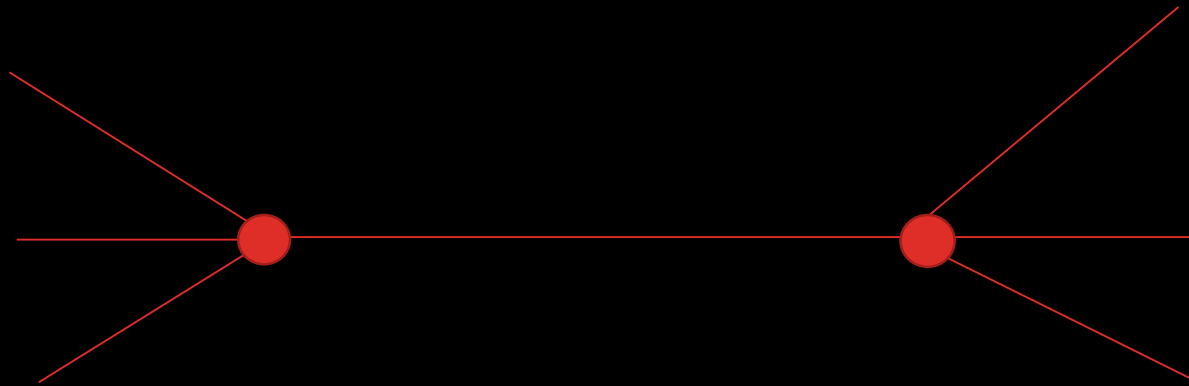
- Until 1992 foreign ownership restrictions and nationality clauses only allowed for airline cooperation in route specific code shares
- The architect of modern airline alliances is Paul Mifsud, KLM's VP Government and Legal Affairs in the USA: he proposed DoT to apply ATI to international cooperation of airlines (see also oral history reviews DePaul University)
- Per 1-1-1993: US DoT allows an ATI enabling close cooperation between NW and KLM

THE NW-KL ALLIANCE

- NW in dire straits: part of the shares to be sold. FT invited KLM in the Wings holding for its cargo expertise. KLM acquired 19.3% in NW and started code share flights in 1991.
- Personal click between Leo van Wijk (KLM) and Mike Levine (NW)
- First metal neutral JV NW-KLM in 1997
- Success formula (see next slide)

THE BEHIND-BEYOND MARKETS US-EUROPE

- Full network integration, revenues/cost sharing and integrated marketing
- Transatlantic connected hubs



- Exploding behind-beyond markets
- Concerns about decreasing competition on inter hub routes

THE ECHO OF THE ALLIANCE SUCCESS LANDED ON MY DESK

- For the physical planning procedure of Schiphol's fifth runway new air traffic forecasts were developed early nineties
- Innovative combination of 3 macro-economic scenarios prepared by CPB (Global Shift, Eur Renaissance, Balanced Growth) with 3 aviation scenario's: BaU, Eli and Gli
- Result: 3 realistic combinations out of 9: GS and BaU, **ER and Eli**, and BG and Gli
- Steering group of Min EZ and Min V&W: middle scenario chosen as 'development strategy' which was the best fit for the conflicting economic and environmental interests
- CPB prepared a social CBA, confirming that an extra runway resulted in a strong positive welfare effect (strong direct benefits, limited external costs)

THE CONSEQUENCES FIVE YEARS LATER

- actual traffic growth at Schiphol had followed the high scenario BG/Gli
- Political turmoil: minister accused of not adequately informing the parliament and Dutch GAO investigation started in my office
- We could simply explain that some earlier unforeseen impacts better fit in the BG/Gli scenario (reflecting the raison d'être of various scenarios);
 - Open Skies
 - ATI and NW-KLM alliance
 - New wave system at Schiphol

SOME LESSONS LEARNED

SCENARIOS:

- never submit an odd number of scenarios to political decision-makers
- Apparently Eurocontrol is not yet hindered by political decision making: see “European Aviation in 2040; Challenges of growth”
 - Three scenarios, the middle one earmarked by Eurocontrol as ‘the most likely one’

SOCIAL COST BENEFIT ANALYSIS:

- Social CBA (high direct effects) does not correspond with the current social discussions on further traffic growth at Schiphol (high external effects)



THANK YOU FOR YOUR ATTENTION !

ANOTHER TIME I'LL TELL YOU ABOUT.....

- The current landscape of global airline alliances and the EU-US Open Skies negotiations might have resulted in a completely different picture if BA would have been willing to pay a little more for the KLM shares in
- ATI & Open Skies agreement UK-US already put in place for a JV NW+CO and BA+KLM (See for more details oral history interviews of DePaul university)
- What the then CEO of BA did not believe became true: KLM was taken over by KLM.
- Negotiations followed on the conditions of the take-over: 40 so-called key destinations to be kept at Schiphol