

Gleiss Lutz

# Liberalizations in the Past – Lessons for the Future?

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# Introduction

*„In the exercise of its sovereignty every nation has the right as well as the duty to itself to develop its air power, as represented in part by its air transport, to the extent needed by its domestic and foreign commerce and other legitimate objectives. World organizations may well require sufficient international control so that air transport does not become an instrument of unfair nationalistic economic competition or political aggression and thus the source of serious international misunderstanding and dangerous ill feelings.“*

John Cobb Cooper, 1947

# Liberalizations in the Past

# United States of America

## Background (1938 - 1970s)

### *Civil Aeronautics Act (1938)*

- air transport considered as natural monopoly
- competition would result in wasteful duplication of services
- strict regulatory regime
- objectives
  - prevention of destructive competition
  - protection of infant air transportation industry

# United States of America

## Liberalization (1978)

*Report by Subcommittee of Congress on past development of air transport industry:*

- positive aspects
  - industry growth promoted
  - technological improvements achieved
  - reasonable industry profits allowed
- negative aspects
  - market prices for air travels remained high
- conclusion: air transport sector not receptive to destructive competition
- new objective: competition and greater availability of air transport services for general public

# United States of America

## Liberalization (1978)

### *Airline Liberalization Act (1978)*

- objective: fostering competition
- tool: free market entrance on domestic markets
- regulation limited to ensure
  - compliance with antitrust laws
  - consumer protection
  - avoidance of predatory pricing

# United States of America

## Further developments

- strong consolidation with emergence of global players
- competition was enhanced
- worldwide dominance of US airlines (also due to “open-skies” policy initiated in 1978?)

## Conclusion

- liberalization was a success
- remark: no state-carrier ever existed in the US



# Australia

## Background (1936 - 1970s)

- geography favouring air transport industry (like U.S.)
- domestic markets:
  - 1936: Foundation of private-carrier Australia National Airways (ANA)
  - 1946: Foundation of state-carrier Trans Australian Airlines (TAA; later renamed Australian Airlines)
  - initially subsidization of TAA to drive ANA out of market
- international markets: monopoly of Qantas

# Australia

## Background (1936 - 1970s)

- *Two-Airline-Policy* on domestic markets
  - no more subsidies
  - equal treatment of both domestic airlines
- strict separation between domestic and international services
- control of market entry by prohibition of import of aircrafts
- 1957: Ansett Transportation Industries takes over ANA  
(renamed to Ansett-ANA)

# Australia

## Liberalization (1975 - 2002)

- evaluation by government:
  - competition had not been fostered
  - airlines offered same services at same prices
- deregulation
  - free access to domestic markets granted (even to foreign airlines)
  - separation between international and domestic markets maintained

# Australia

## Further developments

- 1992: merger between Qantas and Australian Airlines
  - Qantas approved to domestic markets
  - Australian Airlines approved to international markets
- 2002: Ansett-ANA bankrupt

## Conclusion

- liberalization resulted in a monopoly, something the government always wanted to avoid
- competition existed until the merger of Qantas and AA

# Great-Britain

## Background

- 2 state-carriers:
  - British Overseas Airways Cooperation (BOAC) engaged in long-haul flights
  - British European Airways (BEA) operated in Europe
- main private carriers:
  - Caledonian
  - British United Airways

# Great-Britain

## Liberalization (1969 - 1987)

- Edward-Report (1969): air transport to be treated like any other industry, i.e. exposure to competition recommended
- *Multiple-Airline-Policy*
  - strengthening of competition **among** british air carriers; and
  - strengthening of british air carriers **in relation** to foreign airlines
- 1970: merger between private carriers Caledonian and British United Airways establishing British Caledonian (BC)
- only few air traffic rights transferred from BOAC to BC
- 1972: merger between BOAC and BEA to British Airways (BA)

# Great-Britain

## Liberalization (1969 - 1987)

- BA and BC incurred heavy losses due to oil crisis in the 1970s
- government split up markets, allowed no direct competition between both airlines
- 1981: decision to privatize BA
- Civil Aviation Agency and government pursued different goals
  - CAA: tried to enhance competition among british air carriers
  - government: promoted BA due to coming privatization of BA
- no additional transfer of air traffic rights from BA to other airlines
- 1987: BA's ipo generating GBP 900 million

# Great-Britain

## Further developments

- BA remained dominant carrier in UK, finally taking-over BC in 1987; today one of leading air carriers worldwide
- BA expanded significantly to position for Single European Market

## Conclusion

- today BA faces domestic competition from Virgin Atlantic Airways, British Midland Airways and Ryanair
- despite "destructive approach" by government a competitive surrounding emerged thanks to private entrepreneurship



# Germany

## Background

- dominant state-carrier Lufthansa (LH)
- exposed to little political influence
- 1982: first attempt to privatize failed due to
  - national defence considerations
  - foreign policy (LH used as an "ambassador" to strengthen bonds with other countries)
  - trade interests: support of Airbus

# Germany

## Liberalization (1990 - 1997)

- liberalization and regulatory changes in air transport sector initiated by EU not by German government
- 1990: German government fostered "privatization" for financial reasons
  - Germany's reunification
  - emergence of European Monetary Union

# Germany

## Liberalization (1990 - 1997)

- LH in serious crisis
  - heavy investments by LH in new fleet to prepare for Single European Market (EUR 4 billion)
  - fierce competition from US airlines, BA and KLM
  - Gulf War I
  - LH short of bankruptcy in 1992 (debt: EUR 3.2 billion)
  - LH asked for privatization to be freed from administrative burdens
- no support or protection of LH by government
- 1997: LH's privatization

# Germany

## Further development

- LH remained dominant carrier in Germany and additionally became one of leading airlines in the world
- presently faces competition from Air Berlin (and Ryanair)

## Conclusion

- liberalization was not pursued by government, but happened as a "side effect" to privatization
- highly destructive approach by government
- management saved the airline and ensured a smooth transition from a state-carrier to a private entity

# Lessons for the Future

# Lessons for the Future

## Waves of liberalizations

- 1st wave in the 1970s (USA, UK, Canada, Australia)
  - approach: control of liberalization process and protection of state-carriers in transition by the state
  - challenges: oil crisis
- 2nd wave in the 1990s (EU)
  - approach:
    - regional deregulation in several steps
    - establishment of alliances by air carriers
  - challenges: Gulf War I and competition from formerly privatized airlines

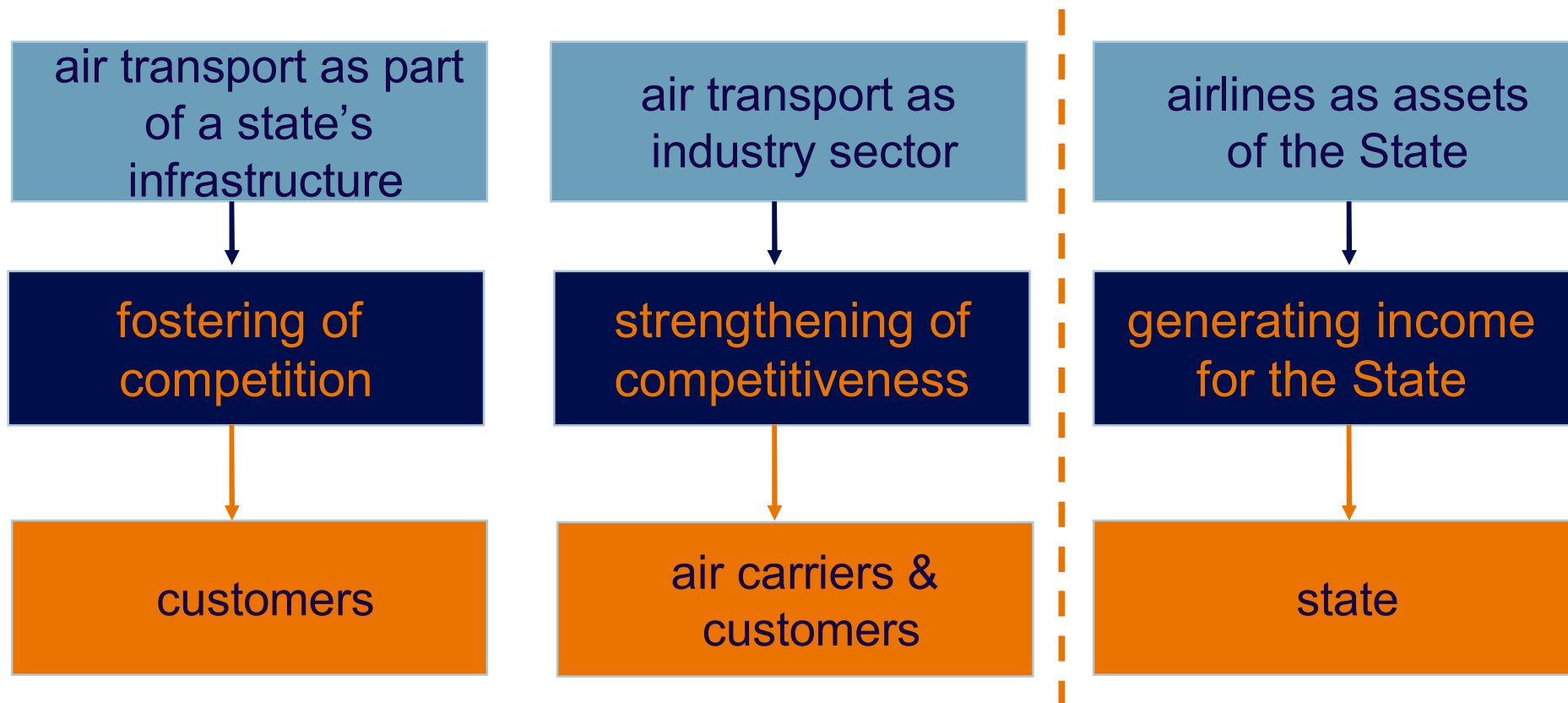
# Lessons for the Future

## Waves of liberalizations

- presently: 3rd wave (Middle East and South-East Asia)?
  - o approach
    - sixth freedom traffic (Middle East)
    - no frills carriers (South-East Asia)
  - o challenges: terrorism and even more competition from even more formerly privatized airlines

# Lessons for the Future

**The nature of the air transport industry determines the objective and beneficiaries of liberalization!**





# Lessons for the Future

## Structure of liberalization

- transition from a state-carrier to a private entity needs time
  - change of mentality
  - positioning of competitors
  - process of trial and error for management
- don't try to outsmart the management (example: BA und LH)
- the market situation determines the speed of liberalization and the level of required protection (infancy – teenage – grown up)

*Don't let yourself rush into liberalization. Today's proponents of liberalization once used to be protectionists!*

# Lessons for the Future

## Tools of liberalization

- air traffic rights
- limitation of route permits (*Theory of Contestable Markets*)
- market entrance to foreign air carriers
- (division of markets)
- regional approach

*If liberalization shall result in an improvement of competition or strengthening of competitiveness it requires the existence of competitors!*

Thank you for your attention!

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### **Publications**

The „Open-Skies“ Decision of the European Court of Justice: The Advent of a New Era? (Annals of Air and Space Law 2003)

The Impact of EU Law on the Regulation of International Air Transportation (Ashgate 2007)

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german, english, french, polish

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