

Remarks of Paul Gretch
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BABI's Air Transport Sub-Forum Conference
Tuesday, 17th September 2002
London, England

One of the overriding issues in aviation during the last thirty years has been where to draw the line on government involvement. Obviously and happily that line has increasingly been drawn to limit government's role and to enhance the central roles of the marketplace and airline management. The result has been large-scale deregulation, first in the United States and then in Europe.

Nevertheless, compared to other economic sectors, governmental involvement is substantial and is likely to remain so. Of course, this is entirely appropriate in areas such as safety and security, competition law and the environment. Beyond those areas the philosophy in the U.S. has been to create the framework for vigorous and fair competition and get out of the way.

Of course, it has never been that simple, and the difficult times that the industry is now facing on both sides of the Atlantic raise new questions of the government's appropriate role, a question that I will return to in a minute.

But first let me state my belief that the ultimate economic fate of the industry remains in individual boardrooms and executive offices. The essential economic problems in the industry certainly have been accentuated by the tragic events of last September, but would have to be faced even without those events. Foremost for most major carriers in Europe and the U.S. are costs that in many cases far outrun the zone of profitable operations no matter how canny management is in maximizing revenues in the current economic environment. Right now in the U.S., many carrier managements are questioning the assumptions of their business plans- the nature of their hubs, their pricing structure, their capacity decisions. And that is where such decisions belong- and it is how well those decisions are made that will determine the fate of individual carriers far more than governments.

What then can or should governments do to help in these perilous times? Well, one way not to go is back to the days of government subsidy which sapped the efficiency of carriers and undercut fair competition. Now, I know that questions were raised in Europe over the decision of the U.S. Congress to help U.S. carriers to overcome the specific catastrophic consequences of 9/11, but that program was designed under stringent conditions to meet injuries directly related to monumental unforeseen events. Without it we might have found ourselves without an operating industry. It was not designed to be and is not a blueprint for the future.

But, again, what role for governments? One aspect is to carry out our stewardship in the safety, environmental, and the newly complex security areas without compromise but with sensitivity to the workings and needs of the industry. A prime role is to provide the proper international framework for industry growth. It has been black letter U.S. policy to create opportunities for service and competition wherever possible- through our decade- old open-skies policy that has resulted in 58 agreements and an expansionary spillover into other major aviation relationships that remain short of open skies, and through our related support for international alliances when they have not been adverse to competition. One of the most important new agreements in the past year has been with France. In signing it with then French Transport Minister Gayssot, my Secretary, Secretary Mineta, hailed it as an “historic agreement that gives more freedom of choice to travelers and shippers.”

Our efforts in this area are far from over. We will use every forum- bilateral or multilateral- that promises progress.

We are very likely on the cusp of a new chapter in the evolution of U.S.- European aviation relations, if, as now seems possible, the European Commission receives a new mandate to engage the United States more broadly on aviation issues. New possibilities can be explored in areas already engaged by our open-skies agreements and in areas going beyond them. It has never been our view that our open-skies model is the be all and end all of liberalization. Rather it was designed as a practical way to move us forward to a new level of aviation freedom- and it has, I believe, more than any other initiative in recent international aviation history. Its influence has been enormous all over the world. Uniformly, it has benefited both our carriers and the carriers of our partners. The fact is that in Europe not a single major carrier has seen its market position erode- in almost all cases just the reverse.

Now we are ready and willing to look to new horizons in Europe and elsewhere in the world.

Which I am afraid brings me naturally to the frustrating story of United States- United Kingdom aviation relations. We have been laboring for decades under the burden of a backward-looking agreement, Bermuda II, that limits designations, frequencies and pricing decisions. Crucially, it has limited service to Heathrow Airport to two passenger carriers from each side, so that it has been impossible over time to develop a satisfactorily competitive environment, even in the context of an increasingly capacity restrained facility like Heathrow. Bermuda II even excludes altogether certain U.S. points from service to Heathrow. It has hobbled the operations of major U.S. carriers and frustrated the transatlantic ambitions of BMI, who can fly to the U.S. from Manchester but not from London.

This has been bad news for travelers, particularly business travelers, who pay the highest premium fares per mile in any European-U.S. market.

And for shippers too, since there are very significant restraints that have kept major firms such as Federal Express from developing needed services from the U.K.

Open-skies has nevertheless seemed to be in sight over the last several years on more than on occasion. But each time hopes have been dashed.

The reason is that the U.K. has consistently tied open-skies to the approval and immunization of an alliance between British Airways and a U.S. carrier.

BA's desire for such an alliance makes total sense in an increasingly globalized aviation world where alliances are becoming the norm. BA in fact belongs to an alliance, Oneworld, which includes, among others, American Airlines. But Oneworld does not have the advantage of antitrust immunity from the U.S. and U.K. governments that would permit the alliance members to closely collaborate on such matters as pricing and capacity. This is an advantage that their rivals, such as Skyteam and Star, do have.

The problem has been that, except for a period when BA was contemplating an alliance involving KLM and its U.S. partners, BA's requests for antitrust immunity have raised serious competition questions because they have involved another powerful Heathrow carrier, American.

Nevertheless, earlier this year the U.S. tentatively approved such an alliance on the condition that the U.S. and U.K. would bring into being an open-skies agreement, and that there was provision for a number of slots at Heathrow that would make possible a suitable counterbalance to the established, powerful, immunized incumbents. In general terms our view of this case was endorsed in their tentative determinations by the U.K.'s Office of Fair Trading acting in close consort with the European Commission.

It was the condition that would have entailed the transfer of slots that the applicants decided was too stiff a price to pay. They withdrew their application. We felt and still feel that our conditions were necessary to carry out our duties as the guardians of competition. Such conditions might not have been necessary if Bermuda II had been scrapped long ago and competition at Heathrow permitted to grow over time.

It is instructive to contrast this situation with the decisions concerning the request of two different carriers, United and BMI, whose potential alliance raised no significant competitive questions. It was approved subject to one major condition—the existence of open-skies.

So we are left where we have been for these many years. But the U.S. position remains clear. We are willing to do an open-skies agreement with the U.K. untied to any other transaction. We are willing to do this, not because we believe that

such an agreement solves all problems and is the best of all possible worlds, but because it is doable now, in the clear interests of the consumers and economies of both countries, and the course that is the most consistent with the general trade philosophies of and practices of both countries.