Competition and Investment in Air Transport

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Legal and Economic Issues

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Preface

Here are some basic facts.

Half the world is living in cities. It is not probable that globalization will stop and, with exponential development, this city population will only grow globally. An OXFAM report published in January 2015 states that 1 % of the world's richest people own 42 % of the total global wealth while the other 99 % own the balance 58 %. Of these, the world's richest 20 % own almost all of the 58 % leaving just 5.5 % to almost 80 % of the world. In just 2 years, the top 1 % will have more wealth than the other 99 % if this trend continues.[1] An ageing population, many with disposable incomes, is another irreversible trend. Against this backdrop, increasing urbanisation; expanding middle class; and rise in migration, tourism and international students are current and future trends.

Amidst these revealing figures, a PWC Global Airline CEO Survey conducted in 2014 states that airline CEOs expect three trends to dominate over the coming years: technological advances; shifts in the global economy; and demographic changes that would transform their businesses.[2] Development and international cooperation is a buzz word in many developed and developing countries. Air travel will double in 2035 as against today's figure. In January 2015, ongoing projects for airport construction amounted to the value of US $543 billion globally.

These facts and figures incontrovertibly spell out the future of air transport and the inevitable fact that liberalization of air transport is a compelling need to meet demand. However, protectionism of market access is looming its head, taking us back to the frustrating 1970s and 1980s. Technology is changing rapidly, affecting the way air transport is being conducted around the world.

Globalization and deregulation are no longer intrinsically linked to each other.

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[1] *Wealth: Having It All and Wanting More*, OXFAM: January 2014 at 1.

[2] *Strategic Sights Set on Transformation and Innovation*, PWC Global Airline CEO Survey 2014, www.pwc.com/transport at 1.

Although the prevailing cross border flow of people will increase, the quantum of cross border investment of foreign direct investment would probably remain at the current rate of around 10 %, thus attracting continued protectionism in air transport.[3] The World Bank, in its January 2015 Report,[4] expects overall global growth to rise moderately to 3.0 % in 2015, and average about 3.3 % through 2017. The Report posits that a growth rate of 2.2 % will be seen in high income countries in 2015–2017, which would be an increase of 1.8 % as against 2014, on the back of gradually recovering labour markets, ebbing fiscal consolidation, and still low financing costs.

Growth is projected to gradually accelerate in developing countries, rising from 4.4 % in 2014 to 4.8 % in 2015 and 5.4 % by 2017.

Competition in air transport is integrally connected to and impacted by various drivers such as environment and climate change, foreign trade and investment, economic growth of nations, liberalization and the enhancement of national security, and even the commercialization of outer space activities, which is in turn affected by globalization—a phenomenon which opened trade barriers through politics and diplomacy. Integration of the world trading machine into a globally connected process occurred with the twin forces of globalization and the information revolution. Air transport is hedged between these two factors, attenuating the advantages offered by both.

In early July of 2015, the 3-year long study on the expansion of London's Heathrow Airport was released with the recommendation that a third runway be built at Heathrow to accommodate traffic growth and promote London as a growing global hub. The main drivers of this recommendation were that London is lagging behind other European hubs such as Schipol and Frankfurt, which were offering significantly more flights out of Amsterdam and Frankfurt to China and other emerging markets in Asia, and that Dubai's airport capacity has exceeded the total airport capacity of all of Britain, thus weakening Britain's connectivity with the key points of economic growth in the world that offer opportunities for trade. The simple fact is that, unless British air transport facilities and infrastructure are brought to par with the rest of its competitors, Britain will be out of the competitive field. This brings to bear the incontrovertible need for capacity growth with which the intrinsic link between competition in air transport and connectivity could be strengthened.

Also at the time this book was being written, the five major airlines of Europe (Air France KLM, EasyJet, International Airlines Group, Lufthansa Group and Ryanair) met with a view to seeking a new European policy on air transport. They suggested *inter alia* that there should be a more airline-friendly liberalization policy in Europe that could seek reductions in airport charges at major airports through tighter regulation, which in turn would save consumers €1.5 billion in lower fares. Airport Council International—the voice of airports worldwide—countered that the suggestion was ludicrous and extraordinary because it hinged on one key assumption—that

[3] Pankaj Ghemawat, *World 3.0: Global Prosperity and How to Achieve it*, Harvard Business Review Press: 2011 at 29.

[4] *Global Economic Prospects: Having Fiscal Space and Using it*, January 2015, at 21.

any such reduction in airport charges would be passed on 100 % by airlines to passengers. ACI further contended that independent research showed that airline interest does not necessarily equal consumer interest and that to assume airlines would pass mandated reductions in airport charges on to consumers was ludicrous to say the least. ACI further complained that most airlines do not even effectively refund airport charges and other ticket taxes to passengers who do not take their flight.

Air transport has certainly come full circle where competition is rife. During its incipient days, the days of PANAM, TWA, KLM and QANTAS in the 1950s and early 1960s, flying was a luxury, where passengers dressed up for the trip as if they were attending a wedding and sat in lounge chairs throughout their journey enjoying gourmet food. Then came the transition to cost cutting and coach class where airlines were packed like sardines with mostly the budget complying tourist and start-up businessman. First class was a rare commodity reserved for the few rich and corporate high ups. Now, in the early twenty-first century, we seem to be back where we started. Of course, coach class is still the major component, but the opulent ostentation with which first class and business class passengers are treated and the facilities they enjoy both in the air and on the ground simply boggles the mind.

For the air traveller who can afford it (mostly in instances where his/her company pays for the trip), the buzz words for airlines are "passenger experience". There are sleeping rooms and a cigar lounge in Lufthansa's first class lounge. Airlines such as Lufthansa and Qatar Airways drive their first class passengers right up to the plane in a limousine. Foot massages, six senses spas and even acupuncture and facial treatments are standard features at most first class airline lounges. Some services have personal butler services, three roomed cabins with 32 inch televisions on the wall and an in-house chef who can turn out anything you fancy. It is reported that in Cathay Pacific's Wing lounge—reserved for first class passengers—the arm chairs are designed by an Italian architect and the walls of the lounge are eucalyptus. There are private cabanas, showers, beds and even a soaking tub. At Virgin Atlantic's premium check-in at London Heathrow, first class passengers can drive right up to the terminal, sit comfortably in a plush reclining chair while their documentation is processed, be fast tracked through security and whisked off to the Clubhouse Lounge, which is equipped with a *mixologist* who will mix your drink to your liking; a Jacuzzi, roof deck and salon. Of course, one cannot forget the black truffle martini. This goes way beyond the standard VIP check-in, chauffeur service and lounge that is standard in business class.

Virgin is reported to have a Revival Lounge that trusses you up when you arrive, which offers you a shower, a clothes pressing service while you shower and a chauffeur driven car waiting for you to take you home. Abu Dhabi airport has even a shoe shine service and a barber, all at your disposal to give you a fresh, wet shave!

Tyler Dickman, CEO at Lounge Buddy which is an app that provides information on global availability of airport lounges has commented: "your biggest risk is forgetting that you are in an airport and missing your flight", as reported recently in the Montreal Gazette.

So why is all this happening? Thomas Piketty, in his bestselling book *Capital in the Twenty First Century* says that inequality began to rise sharply in the 1970s and

1980s, which brings us to the present where half of the population of the world own nothing; the poorest 50 % own less than 10 % of national wealth and generally less than 5 %. The richest 10 % of the world command 62 % of the total wealth while the poorest 50 % own only 4 %. The basis for this trend is the equation r > g (where *r* represents the rate of return on one's capital and *g* represents the growth of the economy). Piketty, who is a professor at the Paris School of Economics says: "indeed, in the United States, as in France and Europe, today, as in the past, income from capital always becomes more important as one climbs the rungs of the income hierarchy. . .the upper centile (the richest 1 %) consists of several social groups, some with very high incomes from capital and others with very high incomes from labour". Taking the United States as an example, Piketty concludes that "it is perfectly possible to imagine that the top centile's share of total wages could reach 15–20 % or 25–30 % or even higher".

With regard to r > g, when the rate of return on capital exceeds the growth rate it invariably results in increased inequality in terms of distribution of wealth. If the growth rate (g) is 1 % and the rate of returns is 10, the investor has to invest only a tenth of his/her annual capital to ensure the growth of his/her annual capital income over the average income. This economic fact has led to rising and continuing inequality in the world where, in colloquial and clichétic terms, the rich get richer and the poor get poorer.

It is said, although not accepted by economists as a rational yardstick, that 50 % of the world is poor, 40 % belongs to the middle class and 10 % is wealthy, of which 1 % is super rich. As was said earlier, the richest 10 % of the world command 62 % of the total wealth while the poorest 50 % own only 4 %, which gives one a perspective of why airlines have got back to bending backwards in competing with their rivals for excellence in first and business class service. Etihad Airways describes its first class service in its Airbus A380 called "The First Apartment" as follows: "*The First Apartment is upholstered with the finest Poltrona Frau leather and features a wide armchair, an ottoman and even includes space to walk around in. The ottoman opens out into an 81-inch long bed.*

A companion can join you for a meal or meeting in your spacious First Apartment. When travelling with a partner the divider between Apartments can be lowered to join rooms.

The First Apartments come equipped with an adjustable 24-inch flat screen TV, which can be viewed from the armchair or while relaxing in bed, together with a vanity cabinet with ample lighting and space for your personal effects, a chilled drinks cabinet and a wardrobe."

With all this fanfare, air transport is a contentious industry mainly due to the fact that there is intense competition among air carriers and the countries they represent as national carriers. The conflict between the United States carriers and the carriers of the United Arab Emirates is a case in point which is discussed in some detail in this book.

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