

State of the Industry

By Abdul Wahab Teffaha – Secretary General

Arab Air Carriers Organization

Mr. Nabil Chettaoui - President of AACO

Ladies and Gentlemen,

First of all I would like to reiterate my gratitude to AACO President, Mr. Nabil Chettaoui, his assistants, and all the people who have worked in organizing this 41st AGM for their great efforts. I would also like to thank all our members, industry partners, speakers, and the representatives of the press for their participation in this event.

Mr. President

Ladies and Gentlemen,

It has been customary for AACO during the last decade to publish an annual report, which includes analysis of the aviation industry and the issues that this industry faces, in addition to particular issues that the Arab air transport industry is dealing with; You will find in your folders this annual report; I thank you in advance for reading it while I also welcome any comments you have thereon for its development.

Today, I will focus on 3 major issues:

1. The global financial and economic crisis and its impact
2. Issues for the Arab aviation
3. AACO's work and its future

Nobody expected, at the beginning of this year, that the world is heading to an economic crisis of such intensity. The dynamics of the current global crisis, its impact, outcome, and how to resolve it, will all be under debate. No observer will be able to truly assess the impact of this meltdown in such a short period of time.

The economic cost of the current crisis, which exceeded thousands of billions of dollars, and its global impact, is incomparable to anything we have witnessed in the past, even the crash of 1929 which led to the Great Depression afterwards. What is

relevant to our industry in this context is that the crisis of 1929 led to an economic project termed at the time, by the late President Roosevelt, “The New Deal.” This New Deal put several restrictions on market economy, and gave the state greater role in controlling its rhythm and in supervising and regulating its activities. Moreover, the New deal gave the state a bigger role in pumping funds and investments to jump-start the economic growth back then. Consequently, the 1929 crisis prompted the United States government to play a direct role in regulating the economy and its activities.

Whether this New Deal succeeded or not remains the subject of debate back then and today. In any case, the New Deal remained in effect till the late seventies and early eighties of the last century, when deregulation was introduced in many of the economic sectors, including air transport. At the same time, the wave towards global liberalization of trade and services, on top of which was the deregulation of air transport.

At this point, a few questions come to mind:

- 1 - Will the current crisis prompt governments to exert more control on economic activities, including air transport? And will these governments tune down calls of market laissez-faire, and bring us back to a more restricted form of market economy?
- 2 - When governments did intervene, by injecting massive funds, or through their political and economic tools, to organize a rescue operation for companies exclusively owned by the private sector, then could it be that all the talk of self-correcting market economy was nothing but an illusion?
- 3 - What about the proclamations of the dominance of globalization and that of national ownership and control will be a thing of the past including the imminent demise of the flag carrier concept? Have these proclamations received a painful blow when the globalization of institutions propagated a real estate crisis in the United States into a global economic crisis of unseen severity?
- 4 - Is private ownership really the only effective way of doing business, with the news of mismanagement and lack of effective oversight going public, especially when investors were lured by major investment corporations, into two massive crises in less than a decade: the internet and the real estate bubbles?

I hope I do not come across as an advocate of renouncing market economy, of non-privatization, or of non-liberalization of air transport. I do however advocate that policy makers do not get carried away by the heat of the moment. They rather need

to examine every move they want to do, guided only by the long term interests of their national economy.

Mr. President,

Although the answers to these questions are still subject to heated debate, there is no doubt that states will create safety nets in defense of their national institutions, if nothing but to avoid an imminent rerun of the 1929 social catastrophe.

To be more specific, I would like to address some issues affecting the air transport industry as a result of this particular crisis. When the air transport industry met at the IATA AGM last June, the main concerns were, high fuel prices, the inability of the airlines to offset the rising costs with an increase in revenue; signs of economic slowdown and the increasing cost of money due to the credit crunch. A maximizing factor in the industry's concern was the fact that many airlines have narrow margins in cutting cost, due to the airlines' tremendous efforts during the 2001-2006 crises to bring down these costs.

Three months later, and the world slides into a much greater crisis. The air transport industry today, despite the decline in oil prices, did not unravel the costs problem: Present oil prices are closer in many cases to the prices of the hedging programs done by many airlines. Economic slowdown turned into a global economic recession, which triggered a decline in traffic, which the airlines could not match in capacity withdrawal. The increased cost of money has deeply worsened with the scarcity of lenders, if existing.

Mr. President,

I hope the consequences of this crisis would not translate into strong reregulation on airlines market access, or on airlines' ownership. On the contrary, this industry hungers for flexibility to revive traffic, and even greater flexibility in cooperation, even consolidation within transparent and economically balanced frameworks that safeguard the best interests of the countries involved. Cooperation and the ability to consolidate are exactly what can reestablish the lost balance between supply and demand, and trim costs back into their optimal levels. Simultaneously, and to assist airlines to survive this crisis, Governments are urged to reform the infrastructure and to revisit their taxation policies, and to shoulder responsibility over the security burdens, in addition to relaxing restrictions on the movement of people and goods. All these measures are way less costly than the possible collapse of some airlines under the pressure of this crisis, forcing governments to rescue them, similar to what

happened recently with financial institutions. The track record of this industry, its self-correcting aptitude, the transparency of its process, in addition to the pivotal role it plays in global economic development, call for support from Governments to contribute in reducing unnecessary costs on one hand, and help to stimulate the market on the other.

Mr. President,

I would like to focus on the situation of the Arab air transport industry, knowing that we will in a while listen to Mr. Giovanni Bisignani's keynote speech that will undoubtedly tackle the broader industry issues.

The current crisis is perhaps the most important issue that faces the Arab air transport industry. It is true that Arab airlines were able to grow and expand throughout the years of the last crises, and although these airlines have invested heavily in modern aircraft, and despite the positive investment by Arab governments in expanding infrastructure, there is no question that the magnitude of this crisis and the indications of traffic slowdown will affect the Arab airlines.

However, there are some dampening elements which may soften the depth of the crisis on the Arab airlines:

- 1- VFR traffic because of the large number of Arab emigrants
- 2- Labor traffic within the Arab world, and with Asia
- 3- Religious traffic
- 4- Business travel, provided that the Arab economic growth is sustained
- 5- New fleet, denoting lower operating costs
- 6- The modern infrastructure, acting as a point of global hubs attraction

However, Arab airlines operate almost everywhere. Even though the elements above may provide a cushion for Arab airlines, they will not provide insulation from the drop in traffic that will affect the whole world.

**Mr. President
Ladies and Gentlemen,**

The industry will ride this storm, together with the Arab airlines. However, managing the crisis is not enough. We need to make use of it to create a better future economic environment.

The volume of the air transport market in the Arab world is about one third of the Arab region's population; the annual number of passengers in mature markets ranges between 150-200% of the population number. In order to stimulate the Arab market it is necessary to ease restrictions on the movement of people and goods, and to facilitate the market access for Arab airlines. That could be achieved through codeshares between the national carriers to ensure equal opportunities if there are restrictions or reservations on unilateral free market access. These two measures would certainly contribute to the development of the Arab economy, in terms of number of passengers, and also in the form of economic development and job creation in the travel and tourism chain. Meanwhile, the global economic crisis will give new impetus to the airlines' calls for closer cooperation, through going beyond the alliances formula into cross equity exchange, or even consolidation in the longer term – when the regulatory environment permits. In the Arab world, consolidation has not been brought up so far, even though we regard this matter necessary to make it possible for Arab airlines to deal at par with a future dominated by mega airlines. Therefore, I believe that the practical steps to support the Arab air transport industry are the following:

- 1- To put the Damascus Convention into force, along with its legal instruments that open the door for Arab airlines to operate freely within certain economic caveats that would prevent capacity dumping, predatory pricing, and operational financial governmental subsidy.
- 2- To develop legal instruments, whether on the Arab, regional, or even bilateral levels that permit cross-border equity stake-holding, or closer cooperation between concerned Arab airlines that paves the way to consolidation, all this while preserving the national identity of the concerned airlines, a la Air France and KLM.
- 3- Arab governments to genuinely look into the optimization of air routes. Restrictions that used to prevent passage over no-fly zones are no longer viable; the truth of the matter is that such restrictions are futile in the face of the cutting edge openly accessible satellite technology that scans the globe. Every minute of avoidable flying time burns more than 60 liters of fuel – at a cost of US\$ 55 - and emits over 150 kgs of carbon dioxide in the air. More than anything, it will assist airlines cut down cost and limit carbon emissions.
- 4- It is fundamental that governments review airport, passenger, and fuel taxes and charges among others. The sum total of these charges is by no means comparable to the economic value that a growth of tourists numbers can bring forward to national economies.

Mr. President,

Your association, AACO, is at the heart of the industry issues and strives to always be the framework through which you can address these issues. On the practical level, reduce your costs and cooperate to maximize your marketing power, and therefore increase your revenue. The Joint Projects continue to provide a reduction in the member airlines' cost of operations, in particular through Joint Fuel Purchasing and Joint Ground Handling agreements. AACO assisted the airlines in their negotiations for the implementation of E-tickets within the timeframe specified by IATA, and led negotiations for the adoption of CRSs which would empower the member airlines to implement direct sales through the internet, and finally concluded a collective distribution contract between a large number of AACO members and one of the major GDSs. We will continue to work during the next phase with the three prominent GDSs serving the stakeholders in the value-chain of travel and tourism.

Moreover, AACO RTC has developed its activities, by launching a Masters Degree Executive Program with Helwan University in Egypt very soon. We have also signed training and technical framework agreements that will contribute in cutting costs down.

On the other hand, the cooperation between 9 member airlines on the networking level through Arabesk is a reality. We will, through AACO's framework, put some practical ideas to boost cooperation between the Arab airlines within the precincts of the current regulatory environment.

AACO also cooperates with ACAC on various topics; and we have lately reached an agreement with the European Commission on the Euro-Arab aviation relations that will be addressed later in the working papers. We continue a close cooperation with IATA on many levels - such as the reduction of taxation and charges in the Arab region, rationalization of air routes, training, and others - and we always look at opportunities to expand this cooperation.

Mr. President,

AACO, in its 43 years of existence has been through two phases; the establishment phase, and then the added value phase, when it turned into the provision of economic value to its members, in addition to providing a framework for the coordination between the Arab airlines, and the defense of their interests. This economic benefit of AACO translates into direct financial benefits through the Joint Projects, and also through value-added work that cannot be enumerated. The Secretariat General values greatly the constant support of its members, and believes that members' trust

should be met by the Secretariat General's level with greater strive towards developing its work to maximize members' best interests, especially that the current crisis has placed increasing pressures on the Arab airlines. Accordingly, we will, with the guidance of the Executive Committee, look into the future of AACO's work, and how to develop AACO's functions and mechanisms.

Finally allow me, Mr. President, to thank you again for your constant support, and to also extend my thanks and gratitude to the Chairman and members of the Executive Committee, who deploy extra efforts to guide and support AACO's work. I would like also to extend my gratitude to all the CEOs for their support, and to thank all my colleagues in the Arab airlines especially those who participate in the committees and groups, and who also participated in the negotiations, spending long and tedious hours in defense of all members' interests even if it was with our industry partners, whom we are honored of their support.

My closing thanks Mr. President are to my colleagues in AACO for their exemplary efforts and for their belief that their work is a mission before being a profession.