State of the Industry
Presented by Mr. Abdul Wahab Teffaha - Secretary General
Arab Air Carriers Organization

Your Excellency Engineer Khalid Al-Molhem, AACO President
Your Excellencies,
Ladies and Gentlemen,

Allow me at the beginning to extend my great appreciation to the President of AACO, His Excellency Engineer Khalid Al-Molhem, and to his Deputy and team who have worked on the preparation of AACO’s 42nd Annual General Meeting. I wish to thank them for their commendable efforts, which the audience has experienced firsthand, and that is befitting of the Kingdom and its peoples’ genuine Arab hospitality. I would also like to extend my appreciation to all our members, speakers, industry partners and press representatives for their participation in this assembly.

Mr. President,
Ladies and Gentlemen,

We have enclosed in your files the Annual Report of AACO, which includes a summary of the key issues facing the air transport industry, and the role of AACO in helping members meet these issues. The report comprises comprehensive facts on air transport, with a focus on air transport in the Arab world. Your files also include the Annual Bulletin of Air Transport Statistics (AATS), with emphasis on the Arab world. We hope that these publications would bring the reader closer to the current standing of this industry and to its pivotal role in driving the wheels of the economy; that, in addition to the role of AACO and of its members.

Mr. President,

My speech today will focus on four issues that are essential to the future course of the Arab Air Transport Industry, namely:

1 – The Global Economic Crisis
2 – The Arab Regulatory Framework
3 – The Environment and Industry's Role in Environmental Protection
4 – AACO’s Work
On the global economic crisis, we all recall last year when we met during the AACO AGM in Tunisia, when the manifestations of this deep financial crisis started to unfold. The air transport industry had only just felt the extent and gravity of the crisis, and it was as if it had entered a dark tunnel, still unacclimated with the sudden blackout. Perhaps the panel discussion that took place a year ago in Tunisia among a group of CEOs, who debated the prospects of the crisis, was the first attempt by the industry to draw attention to this crisis, to realize its magnitude, implications, and to probe its way out of it.

Despite the thousands of billions of dollars that were injected by many countries, we are not out of the tunnel yet, albeit we can now see the light at the end of it. The cost of this crisis, no less than US$ 5 trillion, is enumerated in figures we used to call "astronomical" in the past. Regrettably, and far from the mind's eye, this crisis has manifested itself, and is very real. The economic recession that hit most of the world economies thumped the air transport industry into an unprecedented decline, unseen even during the worst of the past crises.

The depth of this crisis, its permeation to different economic sectors, hit the most important driver of the economy: credit capability. This constraint enhanced the negative consequences of the crisis and marred this year as the worst in the air transport industry.

The industry was barely out of 6 years of successive strikes, having witnessed one year of prosperity in 2007, but soon faced the steep rise in costs in 2008, particularly fuel costs. This only worsened the ramifications of the crisis on the industry. It was not possible for many airlines to accumulate sufficient financial reserve to enable them to cope with the crisis, a crisis that reemerged after 6 years of pressure on costs, and a one-year break when the airlines had to adapt with unparalleled skyrocketing fuel prices.

Mr. President,
Ladies and Gentlemen,

The three decades I have spent so far in the airline industry started with the early years of a structural change. Since the beginnings of air transport liberalization in the United States, two terms were constantly and enduringly repeated. They stuck to my mind, and I believe to the mind of everyone who works in this industry: Crisis Management, and Cutting Costs. An industry
whose mission stands on two negative elements is no doubt an industry afflicted by a structural problem. The reason I believe that these two elements are negative is that, unfortunately, crisis management as means to meet the challenges, and cutting costs as a strategy for existence, have become the measure of success and failure for this industry.

Where, for example, is the vision that business and investment should focus on alternative expressions, namely: expansion and exploiting opportunities, even during crises management? Where is the vision of achieving the highest return on investment rather than focusing only on cutting costs?

Crisis management and cost reduction are not wrong policies per se. However, the downside is that they have become the symbol of this industry, despite its true image as one of the main drivers of world economy, and that it represents a base of globalization on one hand, and of development on the other.

One cannot help but question why an industry of such importance, of such economic role and development would give of itself the constant stigma of an industry in crisis, and of low return on investment, at a time when all the industries around it are less in trouble and more appealing to investment.

The problem is that open skies had freed the industry’s ability to offer capacity, as if it has allowed the industry to free one of its two arms, leaving the other completely tied up. The outcome is that this industry now endures a structural crisis of over-capacity, resulting in price competition and a decline in the return on investments, coupled with high taxes, discriminatory measures, and legislative procedures, mostly excessive in nature.

The air transport industry before deregulation and liberalization in 1978 is not the same afterwards. The industry was regulated in capacity, frequency, aircraft types and traffic rights. Moreover, the industry's stakeholders, armed with antitrust immunity, used to coordinate prices. The industry was able to operate with minimal load factors, without the risk of a structural crisis that would result from market forces. Liberalization removed restrictions from the industry, but took away the immunity on pricing coordination. It is normal that price competition would become the main instrument for airlines to increase their market share. Indeed, airlines resorted to pricing policies in competition, and brought about a downward trend in yields ever since. Within the same framework, airlines adopted marketing policies to improve
total revenues by raising load factors. They put into use effective yield management on the one hand, and cost control on the other, resulting in enhanced profit opportunities. Throughout 2007, the industry reached the highest load factors, close to 90% on average for some airlines. Despite this, the economic rules of an industry, such as the air transport industry, do not allow an endless routine of slashing costs, increasing operations and productivity, and maintaining high load factors. How often do we hear calls to cut the overcapacity, before, and especially during crises? Let us be realistic: what airline, given the chance to maintain its capacity but expand its market share by attracting customers from other airlines shall volunteer to pilot the capacity cuts? Besides, any attempt to coordinate capacity, outside the framework of antitrust laws, is illegal. Is the industry doomed to remain free in adding capacity, but unable, within the norms of free market economy, to consolidate and strike a greater balance between supply and demand?

Mr. President,

The remedy is simple, and it has been the potion of other industries: let go of the other arm of the air transport industry. Let it consolidate, exercise control, and expand vertically and horizontally. Let it achieve balance between supply and demand; only then can this industry achieve a return on investment that would attract the necessary investment rather than the burden of debt. Perhaps the Istanbul Declaration, which IATA played a leading role to achieve, is one of the most important documents beyond the Chicago Convention and the Bermuda model for agreements. The Chicago model is no longer the proper regulatory framework for this industry: for an industry whose aircraft are able to fly into any destination in the world with only one stop. Is it sound judgment to hold on to a framework completed in the age when the airplane flew at 300 kilometers per hour, for a range of 1500 kilometers, at a 5-tonne payload, with no more than a compass for navigational aid? Is it rational that this Convention still regulates aircraft that fly at almost the speed of sound with a payload of 200 tonnes and a range of 17000 kilometers using satellite-based navigational tools and the latest information technology?

It is the very same agreement that still governs a major service industry at a time when all other service industries have become global in every sense of the word; industries where we do not see flagship campaigns, no defense of the national identity, and no deterrence to horizontal or vertical expansion. This industry, including the Arab air transport industry, needs to be treated at par with any other industry to be able to integrate, consolidate and freely
access markets. It should be able to grow, expand and manage capacity in order to achieve an adequate return on investment. These solutions would not make this industry immune to crises, but will give it the opportunity and flexibility to engage crises in a manner that secures the continuation of the reform process, and would open the door for those who cannot carry on to exit the market.

What is true on a global scale is truer on the Arab level... There are legal tools that allow airlines to operate freely, to consolidate, and to accept Arab investment as a national investment. However, these legal tools, namely the Damascus Convention, are rarely applied. During the Arab Economic Summit in Kuwait, Arab leaders emphasized the importance of implementing such agreements, and the establishment of a common Arab market, all the way to the foundation of a unified transport market. We do hope that this is the first step on a path that would eventually join Arab countries together under the Damascus convention, then the Istanbul Declaration. It is true that Arab airlines have successfully managed to sustain growth during the crisis, perhaps the only ones in the world; however, the Arab air transport market comprises no more than one-third the population of the Arab world, instead of twice the size of the population.

The importance of forming a single Arab transport market is a universally accepted notion. The reality is that this market might not be possible after some time. Soon, the time will come when some Arab countries find in other regional parties a suitable air transport partner, even with the absence of the same legal instruments that prevent the implementation of this partnership with Arab countries, who in turn would adopt the same non-Arab partner. In this area, AACO, together with the Arab Civil Aviation Commission Civil and the European Commission have signed a set of principles, which if applied, would enhance the prospects of establishing a single Arab air transport market, albeit through a Euro-Mediterranean Partnership. These principles have set up a kind of balance. It is very important to take advantage of that balance to build future relations with the European Union. Therefore, we call on members to coordinate with the Arab civil aviation authorities to ensure the inclusion of these principles in agreements with European countries, or with the European Union.
Mr. President,
Ladies and Gentlemen,

We are less than two months away from the Conference of the Parties of UNFCCC at Copenhagen this December. There is no doubt that the environment issue is fiercely competent on the priority lists, battling its way to the top order of priorities; it might have actually won the priority battle already over other measures to end the economic crisis. It is true that the air transport industry does not constitute more than 2% of the emissions of greenhouse gases in the atmosphere. It is also true that the industry, over the last six decades, has reduced these emissions by about 70% in terms of emissions Tonne-Kilometer. Nonetheless, it is also true that one of the obligations of this industry is to contribute positively to the international effort to reduce the carbon footprint. The industry is no stranger to this concept and the decisions taken at the last IATA AGM represent a first of a kind initiative by the industry to positively deal with reducing the environmental impact through economic measures.

It is quite normal to have a divergence of interests in this domain. The Kyoto Protocol laid the responsibility of global warming primarily on developed countries. Developing countries acknowledge that the responsibility is shared but not equal. No doubt, the Copenhagen Conference will spend a long time on this. However, we should go to Copenhagen hand in hand and united. We should coordinate ahead of time with our governments that the air transport industry is ready to play a positive and active role to deal with this problem. In turn, the International Civil Aviation Organization (ICAO) should set the details of how the industry can positively contribute in that regard. Most members agreed that the unified voice of the industry at Copenhagen is crucial, and a must. This unity in Copenhagen must come in support to IATA’s proposal to treat this industry as a sector, and in support of its stated objective for the positive contribution of the industry to the environment. It should also point to that ICAO should take up all aspects related to aviation and the environment, ICAO being the global framework involved in civil aviation issues. It is also necessary to request from all states not to take unilateral actions in the international air transport area because the industry can all but live without the complexities of dissimilar complex schemes for dealing with the environmental structures. Governments should also commit that any income earned from airlines in this area would be earmarked to improve the environmental impact of this industry.
Although this is the principal position of AACO, we had to realistically deal with the possibility of applying a unilateral Cap and Trade emissions scheme by the European Union. As the European Union’s intentions in that regard became clearer, AACO, through an Environmental Working Group established by the Damascus AGM, promptly adopted an urgent plan to disseminate awareness about the European program, to clarify how to deal with it. Despite our objection to the scheme, the working group explored solutions on how to adhere properly to its terms. Luckily, it was with the kind directives of the Chief Executive Officers and the hard work of the environmental working group in cooperation with SITA, that our airlines were among the first airlines in the world that are straightforwardly ready to conform to the European measures. We still hope that the Europeans would join a global environmental scheme put in place by the International Civil Aviation Organization (ICAO).

The AGM will discuss the Environment issue, and the policies to that regard, during its closed session. AACO has also worked on multiple tasks, and followed up on regulatory issues as well as on joint projects under AACO umbrella. These projects have contributed positively to the revenues of member airlines, helped them cut cost, develop their human resources, in addition to building up their international standing. The joint projects, which contributed over US$ 300 million to the bottom line of our members, have become the backbone of our work. Consequently, the future strategy of AACO takes up strengthening and expanding these projects to boost the value of AACO to its members.

In conclusion, allow me Mr. President to extend to you a personal credit for your outstanding Presidency of AACO and of the Executive Committee. Allow me also to thank the members of the Executive Committee and all the Chief Executive Officers, the teams, working groups, and committees in our member airlines for their guidance and efforts to serve the members. Finally, let me also thank our industry partners who, in the midst of a major crisis, continue to support AACO and to promote its values. To you, on my behalf, and on behalf of my colleagues at the Secretariat General, to whom I also extend my appreciation and recognition to their relentless efforts and dedication to their work, allow me to convey our pride in serving you.