The effect of the EU – USA “open skies” agreement on North Atlantic air transport

Introduction

Regulations in transport due to the importance of this sector affect not only the economy but also the international and global relations. Air transport is one of the most technologically advanced sectors of economy with a central role in the globalization of travel and business. Yet it has been regulated by restrictive rules that remained largely unchanged for years\(^2\). This was changed by the so called “open skies” agreement between US and EU\(^3\). The European Union approved the “open skies” agreement concluded with the United States of America. The agreement provides for all transatlantic routes to be opened up to European and American companies. It also includes an arrangement to develop the agreement further on matters such as airline ownership. For the first time, European airlines could fly without restrictions from any point in the EU to any point in the US. New services and new partnerships have emerged as a result and closer cooperation on key issues between USA and EU has been made possible. The Agreement represents important steps towards the normalization of the international aviation. The ultimate objective of the European Union is to create a transatlantic Open Aviation Area which means a single air transport market between the EU and the US with free flows of investment and no restrictions on air services, including access to the domestic markets of both parties.

The evolution of air transport relations between EU and USA

The air transport agreement between EU and USA was signed in April 2007. The both parties recognized the importance of the Chicago Convention\(^4\). The agreement was applied from March 2008 for all EU Member States, and then amended by a protocol, signed in June 2010. Norway and Iceland accession to the air transport agreement was made possible by additional protocol which applied from June 2011\(^5\). According to the European Commission the agreement represents an important step towards the normalization of the international aviation market. The ultimate objective of the European Union is to create a transatlantic Open Aviation Area which is a single air transport market between the EU and the US with free flows of investment and no restrictions on air services, including access to the domestic markets of both parties\(^6\). The agreement is thus of historical meaning and supports not only aviation liberalization but also the growth of international trade. Aviation plays however significant role in driving globalization, enabling trade by bringing business people together, moving high-value, time-critical products, and contributing to the expansion of travel and tourism\(^7\).

The EU and USA have agreed that the Open Aviation Area will be achieved in stages. The above mentioned agreement was named the first stage agreement. It was followed by the second stage agreement. The second stage agreement of 2010 builds further benefits by providing advances including additional investment and market access opportunities, as well as strengthening the framework of cooperation in regulatory areas such as safety, security and in particular the environment.

The agreement can be regarded the most important air services agreement in the world as it allows to open market access for air services between all EU Member States and the US\(^8\).\(^9\).\(^10\). It also creates the market which makes up almost sixty per cent of global aviation. Furthermore, it created a regulatory platform to address all mutual concerns related to EU-US air services. It provides numerous commercial advantages which include
greater access for EU airlines to the "Fly America" program. The United States and Europe have committed to the goal of removing remaining access barriers and agreed to review progress towards this objective on a regular basis. According to the Association of European Airlines, other important benefits of the agreement are: the removal of all discrimination between EU airlines, allowing them new opportunities to fly on any transatlantic route between the EU and the US, the removal of remaining market access restrictions on flights between the EU and the US, thus creating a level playing field between EU carriers, the commitment of both sides towards compatible practices and improved cooperation in the areas of safety, security, government subsidies and the environment, establishing a Joint EU - US Committee to resolve questions regarding the interpretation of the agreement and to harmonize standards between the European Union and the United States, creating new cooperation arrangements between EU and US competition authorities, facilitating the joint assessment of alliances between EU and US carriers, creating new opportunities for foreign carriers to wet-lease aircraft to US airlines for use on international routes between the US and any third country.

The impact of agreement implementation on air transport

EU-US Open Skies Agreement encouraged the free market competition by removing restrictions on international route rights and designated airline numbers, frequencies, capacities, and aircraft types. Any sales, ground handling services, cargo consolidation, and transport may be established in one country by an office in another country. Designated airlines are allowed to create alliances (code sharing or leasing arrangements) with airlines of either country and with the option to authorize code sharing between airlines and surface transportation companies. Furthermore, carriers may choose to operate under the charter regulations of either country while agreeing to safety and security standards. In a liberalized market, more efficient airlines would replace less efficient ones, or less efficient airlines would adopt the practices of more efficient ones, leading to significant cost savings and an increase in industry efficiency. This substitution would occur through two mechanisms: industry restructuring (e.g. mergers, acquisitions, joint ventures), and increased competition (e.g. a carrier from one EU country could establish a transatlantic hub in another EU country). This same process of expansion and consolidation would allow air carriers to exploit size-related economies, leading to further efficiency gains. For example, a merger or ‘deep’ alliance might allow two carriers to spread certain fixed costs over more passengers (scale economy). The carriers might achieve added savings by reconfiguring their combined network to connect more flights to certain hub airports (scope economy). They might also achieve higher utilization – e.g. by combining traffic to raise load factors (density economy).

According to CAPA Centre for Aviation traffic between Europe and North America, as measured by RPKs, (Revenue Passengers Kilometers) grew at an average rate of 2.6% p.a. between 2003 and 2011, compared with a world average rate of 5.8% [6]. In the global crisis year of 2009, traffic on the North Atlantic suffered a 6.2% decline, much heavier than the 2% fall seen globally. In 2010 and 2011, growth recovered to around 3%, but in 2012 traffic was more or less flat year on year, with growth by European carriers more or less cancelled out by cuts by US carriers.

A look at traffic growth rates by European airlines and US carriers on the North Atlantic, together with the overall growth rates implied by Boeing traffic data for the

<table>
<thead>
<tr>
<th>Year</th>
<th>RPK (billion)</th>
<th>Average growth 2012-2032</th>
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<tbody>
<tr>
<td>2007</td>
<td>634.21</td>
<td></td>
</tr>
<tr>
<td>2008</td>
<td>660.55</td>
<td></td>
</tr>
<tr>
<td>2009</td>
<td>624.92</td>
<td></td>
</tr>
<tr>
<td>2010</td>
<td>640.17</td>
<td></td>
</tr>
<tr>
<td>2011</td>
<td>659.48</td>
<td></td>
</tr>
<tr>
<td>2012</td>
<td>710.02</td>
<td></td>
</tr>
<tr>
<td>2013</td>
<td>1,448.03</td>
<td>3.6%</td>
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</tbody>
</table>

**Table 1. North Atlantic Traffic development (RPK in billions) In years 2007 – 2032**

Source: Boeing: Current Market Outlook 2013 - 2032

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route region, shows that US carriers outpaced their European competitors throughout the mid 2000s, but the reverse has been true since 2009. Overall growth on the North Atlantic has generally under-performed against total world air traffic, with the exception of 2008, the year that EU-US Open Skies came into operation, when it matched world traffic growth. This is a modest piece of evidence that, perhaps, Open Skies had a positive impact on traffic in 2008, but the effect since then is difficult to demonstrate. Both European and US carriers have seen traffic growth averaging around 3% over the past 10 years. Looking ahead to long term forecasts, Airbus and Boeing expect average growth between 3% to 4% until 2032. This is slower than forecast average growth in world traffic of around 5%, but represents a materially higher rate than in the past. Perhaps these forecasts assume that the full impact of Open Skies is still to be felt on traffic growth, but the evidence so far is that Open Skies has had more of an effect on improving load factor and yield than on traffic growth. The North Atlantic is the world’s third largest traffic flow region and the largest intercontinental flow, perhaps not surprising given that internal North America and internal Europe are number one and number two overall regions respectively. Due to the slower traffic growth forecast for the North Atlantic than for the world overall, this share is forecast to fall to 6.5% in 2035. Nevertheless, it is still expected to remain the world’s largest intercontinental flow.

One of the consequences of EU-US Open Skies was to allow the granting of antitrust immunity to joint ventures among market participants that were previously competitors. Sky Team’s Air France - KLM/Delta/Alitalia Joint Venture, Star’s Atlantic Plus/Plus Joint Venture and oneworld’s BA/Iberia/AA/Finnair Joint Venture are all immunized and the alliances control 83% of capacity across the North Atlantic. If Virgin Atlantic joins SkyTeam, this will rise to 88%. While EUR-US Open Skies did not allow non-US control of US airlines or non-US control of EU airlines, it did perhaps ease the path for mergers within each bloc. At least it now meant that an EU carrier could be acquired by another EU carrier without fear of losing its US traffic rights, which are the most important intercontinental routes for most EU airlines. The merger of Austrian into the Lufthansa Group and the formation of IAG from BA and Iberia took place after EU-US Open Skies. The creation of larger European airline groups may have provided some additional stimulus for US carriers to merge (although they already had plenty). United/Continental and the more recently announced AA/US Air deal have followed Open Skies, which also created the environment in which the Virgin Atlantic/Delta transaction was agreed (although not a full merger). The three European and two US mega carrier groups control 59% of the North Atlantic seat capacity.

Summary

The aviation markets of European Union and the United States represent together approximately 60% of global aviation. The economic benefits associated with the implementation of the agreement are noticeable however it seems to be too early for making final summaries. Undoubtedly the potential economic benefits of removing the barriers to the EU-US transatlantic market are very significant and not to overvalue. Open Skies agreement is an important development in the evolution of the global air transport industry. The open skies is very likely to result in great choice for travelers, lower fares and better levels of air service for many parts of Europe and United States.

The comprehensive North Atlantic air transport agreement liberalizes the aviation market and brings it closer to trade and investment patterns in the broader US-EU relationship. It also provides significant advantages across the board for the air services sector, consumers, businesses who rely on express delivery services, commercial air travel and tourism.

Streszczenie

Północno - Atlantycka umowa “Open Skies” zawarta między Unią Europejską a Stanami Zjednoczonymi jest istotnym krokiem w kierunku liberalizacji rynku lotniczego w tym regionie. Poprzez eliminację barier w dostępie do rynku, umowa przyczyniła się do poprawy konkurencji na rynku lotniczym dzięki bliższej współpracy linii lotniczych, zawieraniu umów „joint venture”, obniżeniu cen oraz zwiększeniu konkurencyjności. Artykuł opisuje to procesu zawarcia umowy, jak również kluczowe korzyści z niej wynikające a także wpływ umowy na rynek lotniczy.

Wpływ umowy UE – USA “Open Skies” na transport lotniczy na obszarze Północnego Atlantyku

22Ibid
23Ibid
Abstract

The North Atlantic “Open Skies” agreement between EU and US is an important step toward liberalization of the aviation market in this region. Through the elimination of the access barriers, the agreement significantly contributed to the improvement of the air traffic by closer cooperation, joint ventures, price reduction and increased competition in this field. The article describes the background of this process as well as the key benefits of the agreement and its influence on the aviation market.

Literature:
[14] Rurkowski J., Lotnicze relacje Unii Europejskiej i Stanów Zjednoczonych w świetle umowy Open Skies, Studia Europejskie 2010/1
[15] Second Stage EU-US "Open Skies" agreement – guide,