Article

Investing in Air Transport – A Prudent Move?

Ruwantissa Abeyratne*
International Civil Aviation Organization, Montreal, Canada

TABLE OF CONTENTS

I. INTRODUCTION

The Air Transport Action Group (ATAG) of the International Air transport Association (IATA) reports that aviation transports globally 2 billion passengers every year and 40 percent of the inter-regional goods by value.[1] Forty percent of tourists now travel by air and the air transport

* DCL (McGill), Ph.D (Colombo), LL.M (Monash), LL.B (Colombo). The author has worked in the field of aviation law and management for over twenty five years. He is currently Co-Ordinator, Air Transport Programs at the International Civil Aviation Organization. He is also Professor of Aero Political Law and Policy at the John Molson School of Business, Concordia University, Montreal. He is a fellow of the Royal Aeronautical Society and the Chartered Institute of Logistics and Transport.

1. Air Transport Action Group, *Facts & figures*, *at* http://www.atag.org/content/showfacts.asp?folderid=430&levell=2&level2=430&.

industry generates a total of 29 million jobs annually through direct, indirect, and catalytic impacts.[2] Aviation's global economic impact is valued at $2.960 billion, which is equivalent to 8 percent of the world's gross domestic product.[3]

In addition to its total output and employment impacts, civil aviation has a broader influence on overall economic growth, deriving from non-quantifiable benefits for the users of air transport, businesses, and individuals alike. Air transport acts as a facilitator for the development of markets and trading of goods as well as services.[4] In 2005, airline scheduled services carried 2.022 billion passengers (at an annual increase of 7.1 percent over 2004) and 37.7 million tons of freight worldwide (at an annual increase of 2.5 percent).[5] Approximately 45 percent of some 714 million international tourists and some 40 percent by value of the world's manufactured exports were transported by air that year.[6]

In the immediate aftermath of the events of September 11, 2001, where civil aircraft were used as weapons of destruction, aviation insurers gave seven days notice that on September 17, war risk third party liability coverage according to policy terms applying to the write back coverage for war, hijacking, and other perils would be withdrawn.[7] The most compelling reason for the cancellations was the emergence of an exposure in terms of third party bodily injury and property damage that was seemingly unquantifiable.[8] The International Union of Aviation Underwriters (IUAU) assessed that the total losses in respect to third party bodily injury and property damage caused by these events could exceed the previous greatest single catastrophic loss of $20 billion caused by Hurricane Andrew in 1992 by a significant margin.[9]

In general terms, it was assessed that the price to be paid to revive or reinstate adequate coverage for third party war risk coverage would cost the airlines an additional premium of $1.25 per passenger carried.[10] If airlines were to purchase coverage for limits of $950 million in excess of the already available $50 million they would have to pay $1.85 per passenger carried.[11] In view of the fact that the airports, refuellers, ground

2. *Id.*
3. *Id.*
4. International Civil Aviation Organization, Annual Report of the Council, at A-98, Appendix 13 (2005).
5. *Id.*
6. *Id.*
7. *See SGWA/1-IP/4*, SPECIAL GROUP ON AVIATION WAR RISK (SGW1) (International Civil Aviation Organization), Dec. 2001, at i-1.
8. *Id.*
9. *Id.*
10. *Id.*
11. *Id.*

handlers, and other service providers in the aviation industry contribute to an accumulation of risk, and since many of them may serve a particular airline at one location, underwriters were disinclined to offer coverage for these providers.[12] However, many insurers showed willingness to extend coverage for an additional $100 million over the $50 million coverage already provided.[13]

Many States stepped in to address issues regarding cancellation of insurance and assumed responsibility for the operation of air services by their national carriers and the circumstances, rules, and regulations under which they are carried out.[14] Most provided immediate relief in the nature of concessions and guarantees for their airlines.[15] The unity displayed by the community of nations and the global aviation community is evidence enough that, irrespective of the absence of empirical data supporting the importance of the economic contribution of civil aviation to the world, there is implicit recognition of the indispensability of air transport as a critical driver of the world economy.

The most fundamental premise in investment is that an investor applies resources to an enterprise expecting returns on investment. The issue, therefore, is whether investing in civil aviation[16] would provide the investor, whether a State or private entity, with worthwhile returns to justify investment in the first place and to continue so doing. In order to determine this, it is necessary to look into the investment climate of the world, the investment climate of the air transport industry, and the economic benefits brought about by civil aviation. In a global investment

12. *Id.*

13. *Id.*

14. *See generally* RUWANTISSA I.R. ABEYRATNE, AVIATION IN CRISIS 2-7 (Ashgate 2004) (providing additional information on action taken by States as a result of the insurance crisis, where States guaranteed the continued operation of their air carriers).

15. Some notable examples were found in the United States, where the administration proposed a plan to have taxpayers cover most of the losses that insurance companies would suffer in future terrorist attacks. The European Commission announced, on 10 October 2001, that it would allow member states to help European airlines recover from the turmoil after the attacks on September 11. The Commission, which in the past was critical of government assistance to airlines, urged governments to extend compensation to cover the rise in premiums until the end of the year, and proposed setting up a fund to cover the higher premiums. Japan's government stepped in to help the struggling airline industry as companies tried to cope with rising insurance costs and falling demand in the aftermath of the suicide attacks on the United States. The Ministry of Land, Infrastructure and Transport announced that the government would guarantee third-party insurance up to $2 billion for Japan's airline carriers to cover any shortfall in claims after insurers reduced coverage to $50 million following the September 11 attack. Hong Kong's Civil Aviation Department on 4 October 2001 gave the green light for 15 airlines to levy insurance surcharges on passengers on Hong Kong Routes. *See* Abeyratne, *supra* note 14.

16. Throughout this book, civil aviation is meant to refer collectively to air transport representing the airline industry, airports, aircraft manufacturers and other support industries providing services to air transport.

climate, where in the developing world alone 1.2 billion people survive on less than $1 a day, where 53 percent of the entire world live on less than $2 a day,[17] and where youths have more than double the unemployment rate as others, a good investment climate should, as of necessity, foster productive private investment as the engine of growth and poverty reduction.[18] As will be discussed later in this chapter, in civil aviation in particular, investments create jobs and opportunities for people and expand the variety of goods and services available, while reducing their cost. This in turn benefits the consumer and supports a sustainable source of tax revenues to fund other important social goals.

The World Bank has reported that a robust global investment climate is central to growth and poverty reduction.[19] In this regard, the preeminent goal of governments should be to create opportunities for the private sector for investment while at the same time creating expansion and employment within the State sector. In other words, the goal should be to create a sound investment environment for everyone so that society as a whole would benefit. Of course, this is easier said than done, as developing nations have their own internal concerns and pressing needs brought to bear by both social and natural factors. It calls for a certain symbiosis between the developed and developing world as well as an enduring commitment from the international community to assist the developing world in three main areas: removing distortions in developed countries that harm the investment climates of developing countries; providing increased and effective assistance; and sharing knowledge and experience. These three areas of contribution from the international community have to be applied to the basic axiom that economic development requires adequate and effective transportation. Each country has a theoretically optimum amount of transport capacity. Transportation plays a multifaceted role in the pursuit of development objectives of a nation as well as the need to maintain international communication networks.[20] Air transport enables goods and passengers to be transferred between and within production and consumption centres. Therefore, it could be argued that investment is vital to air transport.

The largest investment in air transport lies in the procurement of aircraft, which is usually done by the airlines themselves.[21] In 2003, 861

17. *World Development Report 2005 Overview: A Better Investment Climate for Everyone*, THE WORLD BANK, 2005, at vii.

18. *Id.*

19. *World Development Report 2005*, *supra* note 17.

20. *Id.*

21. *The World of Civil Aviation 2003-2006*, ICAO CIRCULAR 307-AT/129, INTERNATIONAL CIVIL AVIATION ORGANIZATION, at 30.

turbo jet aircraft were ordered, compared with 497 in 2002.[22] The financial commitment of airlines for jet aircraft orders in 2003 was about $60 billion, up from $40 billion in the previous year.[23] ICAO[24] records that at the end of 2003, there were 1151 western built commercial jets in storage, compared with 1182 at the end of the previous year.[25] It is quite clear that there is overcapacity of aircraft seats and freight capacity.[26] Compared to investments being made in aircraft purchases, other aviation investments are relatively small, because airports and other aspects of infrastructure are funded by the States or instrumentalities of State and pertain to finite resources.[27] Airport real estate is leased, although parts of a terminal may be built by airlines for their exclusive use.[28] In air transport, total costs rise in direct proportion with output, which means that unit costs do not decline radically with expanding sales.[29] One of the most burdensome expenses regarding airports concerns rents which have been excessively high, reducing the margin of profit in this usually gainful industry.[30] These onerous financial burdens on the air transport industry do not detract from the fact that civil aviation was meant to perform an indispensable service to humanity.[31] For example, the 1958 Federal Aviation Act of the United States stipulated the following:

> It shall be the duty of every air carrier to provide and furnish interstate and overseas air transportation, as authorized by its certificate, upon reasonable request therefor and to provide reasonable through service in such air trans-

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22. *Id.*

23. *Id.* In 2003, 917 turbo jet aircraft were delivered, compared with 999 in 2002. The backlog of unfilled aircraft orders at the end of 2003 was 3,272 aircraft, compared with 3,407 at the end of 2002.

24. The International Civil Aviation Organization (ICAO) is a specialized agency of the United Nations charged with regulating international civil aviation globally. *See Preamble to the Convention on International Civil Aviation, available at* http://www.icao.int/cgi/goto_m.pl?icao/en/pub/memo.pdf.

25. *The World of Civil Aviation 2003- 2006, supra* note 21, at 31.

26. RIGAS DOGANIS, THE AIRLINE BUSINESS IN THE 21ST CENTURY 16 (Routeledge 2001).

27. RUWANTISSA ABEYRATNE, AIR LAW AND POLICY 50 (PublishAmerica 2007).

28. DUDLEY PEGRUM, TRANSPORTATION 467-468 (Richard D. Irwin ed., Homewood, Inc. 1973).

29. ALAN H. STRATFORD, AIR TRANSPORT IN THE SUPERSONIC ERA 262-264 (Macmillan Press 1973) (1968).

30. Walter Robinson, *Let Air Canada Heal Self Inflicted Wounds*, HAMILTON SPECTATOR, Apr. 2, 2003, at A11. Developing countries are said to invest almost $200 billion per year in infrastructure, which is about 4 percent of the global outlook and 20 percent of the total investment in the developing world. *See, e.g.*, H.S. Bhatia, *Private Sector Investment, Management and Expertise Important to Airport Development*, ICAO JOURNAL, Sept. 1996, at 17. Canada's eight largest airports pay more than $250 million a year to the federal government in rent which is passed through to airlines and their passengers as a hidden tax. *Id.*

31. U.S. Department of State, *Verbatim Minutes of Opening Plenary Session: Proceedings of the International Civil Aviation Conference*, Chicago, Ill., Nov. 1 to Dec. 7, 1944, Volume 1 at 42.

portation in connection with other air carriers. . . .[32]

Travel and tourism, the largest combination of industries and the largest creator of wealth, is estimated to generate $3.5 trillion a year in activity and potentially provides employment to 130 million people worldwide.[33] This accounts for 10 percent of the world GDP, 10.3 percent of the world wages, 9.8 percent of the profits, and 11.7 percent of indirect and direct taxes.[34]

Be that as it may, there are some factors which effectively preclude air carriers from operating profitably.[35] One factor is the restriction placed on ownership and control of airlines, which in some instances permit only 25 percent of foreign ownership and control.[36] The *International Air Services Transit Agreement*[37] Article 1, Section 5, provides that:

> Each contracting State reserves the right to withhold or revoke a certificate or permit to an air transport enterprise of another State in any case where it is not satisfied that substantial ownership and effective control are vested in nationals of a Contracting State, or in case of failure of such air transport enterprise to comply with the laws of the State over which it operates, or to perform its obligations under this Agreement.[38]

In the period since the 1950s, however, international civil aviation grew in breadth and scope and States increasingly used the right to withhold or revoke a foreign airline's certificate, or in the alternative, permitted it to operate in their *national* airspace as a means of regulating *international* air transport.[39] Specifically, States limited foreign investment in their flag carriers by requiring a nationality clause based on Article1(5) of the IASTA in each of their bilateral agreements on air traffic rights.[40] In this way, States prevented airlines from third countries from benefiting from a bilateral exchange of traffic rights.[41] The requirement

32. Federal Aviation Act of 1958 § 404(a), 72 Stat. 731, 760 (1958) (codified as amended material in scattered sections of 49 U.S.C.).

33. *Id.*

34. H.S. Bhatia, *supra* note 30, at 17.

35. Doganis, *supra* note 26, at 16-18.

36. ISABELLE LELIEUR, LAW AND POLICY OF SUBSTANTIAL OWNERSHIP AND EFFECTIVE CONTROL OF AIRLINES: PROSPECTS FOR CHANGE 33 (Ashgate 2003).

37. International Air Services Transit Agreement art. 1, § 5, Dec. 7, 1944, 59 Stat. 1693, 84 U.N.T.S. 389 [hereinafter IASTA] (IASTA has been ratified as of May 2005 by 122 States, 17 of which have ratified during the last five years). *See also* International Air Transport Agreement art. 16, Dec. 7, 1994, 59 Stat. 1701, 171 U.N.T.S. 387 (article 16 addresses the same issue; however, because very few States signed the Agreement (12 States), it did not go into effect).

38. *Id.*

39. Constantine G. Alexandrakis, *Foreign Investment in U.S. Airlines: Restrictive Law is Ripe for Change*, 4 U. Miami Bus. L.J. 71, 75 (1994).

40. International Air Services Transit Agreement, art. I, Dec. 7, 1944, 59 Stat. 1693, 84 U.N.T.S. 389.

41. *Id.*

for airlines to seek permission to land in or take off from a territory of a State is another feature unique to the airline industry in terms of trade and competition.[42] This requirement has its genesis in the Charter of International Civil Aviation—the Chicago Convention of 1944[43]—which sets the regulation for the conduct of international civil aviation, Article6 of which provides as follows:

> No scheduled international air service may be operated over or into the territory of a Contracting State, except with the special permission or other authorization of that State, and in accordance with the terms of such permission or authorization.[44]

Commencing in the early 1950s, States responded, both through the Chicago Convention, and through IASTA, to the growth of civil aviation by availing themselves of the prerogative given by IASTA to withhold or revoke an airline operational permit to enter into their territories for purposes of landing and takeoff on a commercial basis.[45] By the same token, States used this right to restrict foreign investment in their own airlines or flag carriers by including a clause with specific conditions on nationality of their aircraft in the bilateral air services agreements, which they signed with other States in conformity with Article 6 of the Chicago Convention.[46]

There is no documented definition of, or agreed meaning to the term substantial ownership and effective control.[47] This *in limine* creates certain ambivalence in the field of trade and competition in the airline industry, particularly for an airline that is not fully owned and operated by a State or instrumentality of State.[48] The real difficulty in arriving at a conclusive definition of the term arises when an airline is privatized and the government no longer holds the majority of the shares and there is no demonstrable evidence of national ownership.[49] The international community has, as a practice, got used to identifying ownership of an airline with the voting shares of the company, often equating substantial ownership to more than 50 percent of the voting shares.[50] However, it can no longer be viewed in this simplistic manner, particularly owing to the wave

42. *Id.*

43. Convention on International Civil Aviation, signed at Chicago on 7 December 1944. ICAO Doc 7300/8, Eighth Edition, 2000.

44. *Id.*

45. Alexandrakis, *supra* note 39, at 75.

46. *Id.*

47. *See Ownership and Control, Report of the Think Tank,* World Aviation Regulatory Monitor 2000, IATA, Government and Industry Affairs Department: Geneva, 7 September 2000, at p.4.

48. *Id.*

49. *Id.*

50. *Id.*

of privatization experienced by the airline industry.[51] For example, 45 percent of voting shares held by a private entity in a national airline may arguably be termed substantial ownership even though 55 percent of such voting shares may be held by nationals of the State which designates the airline as its national carrier.[52]

The issue of effective control on the other hand, is a more complex issue than ownership as it is no longer a question of percentages, but rather relates to who controls the airline concerned. In broad terms, this may mean who directs policies of the airline and hires and fires personnel. An indicative definition of control can be found in the United States where legislation concludes that control is "possession, direct or indirect, of the power to direct or cause the direction of the management and policies of a person, whether through the ownership of voting securities, by contract, or otherwise."[53]

There is a distinct variance in characteristics and effect between substantial ownership on the one hand, and effective control on the other. The former may often be established through a presumption of nationality, while the latter may involve complications brought to bear by nationality issues, such as the nationality of members of a supervisory board, and nationality and rights of directors of a board.[54] Furthermore, the nationality criterion pertaining to ownership may even be obviated with some ease, as in the case of the European Union, which, in 1997, introduced legislation recognizing a community air carrier could operate air services anywhere within the fifteen member States of the Union, Norway, Iceland, and Liechtenstein.[55] The European Union effectively replaced the national carrier with a community carrier by this legislation.[56]

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51. Robert W. Poole, Jr., at 15, *Guidelines for Airport Privatization, How-To Guide No. 13* (Reason Foundation, Los Angels, CA.), Oct. 1994, *available at* http://www.reason.org/htg13.pdf.

52. Commission Decision 95/404/EC on a Procedure Relating to the Application of Council Regulation (ECC) No. 2407/92 (Swissair/Sabena), 1995 O.J. (L 239) 19, at 9.

53. The *Securities Exchange Act*, 17C.F.R. 240.12b-2 (1988 & Supp. 1995). The European Union, by Council Regulation No. 2407/92 of July 23, 1992, identifies effective control as a relationship constituted by rights, contracts, or other means. This relationship grants, *inter alia*, the right to exercise a decisive influence on an undertaking, in particular, the right to use all or part of the assets of an undertaking and determine the composition, voting, or decisions relating to the running of the business or undertaking. *Id.*

54. Ruwantissa I.R. Abeyratne, Crisis Management: Toward Restoring Confidence in Air Transport- Legal and Commercial Issues, 67 J. Air L. & Com. 595, 644 (2002) citing *Ownership and Control, Report of the Think Tank,* World Aviation Regulatory Monitor 2000, IATA, Government and Industry Affairs Department: Geneva, 7 Sept. 2000.

55. Council Regulation 2408/92 on Access for Community Air Carriers to Intra-Community Air Routes, art. 3, 1992 O.J. (L 240) 8.

56. *Id.*

II. Civil Aviation and the Alleviation of Poverty

Apart from estimates, the world community has no way of quantifying the economic contribution of the aviation industry to global economic growth. The reason for this is that the aviation industry is only the fuel which drives the world trade machine. Therefore, although world trade can be quantified, it is impossible to determine what part of that trade was driven by aviation. Aviation moves people across boundaries, thereby contributing to the tourism industry, which some argue is the largest industry in the world.[57] Aviation moves goods and services around the world, from the fish caught in the lakes of Uganda and the horticultural products of Kenya to Europe to the Asian worker to the Middle East. Without international aviation, the poor fisherman and horticulturist of Africa will not be able to sustain their professions and the unemployed worker would not find employment overseas. Therefore, it can be argued that aviation greatly assists in poverty alleviation, which is one of the main objectives of the International Bank for Reconstruction and Development, otherwise known as the World Bank.[58]

Another facet to aviation is that it moves people and goods across borders, thus facilitating global business. For instance, when an aircraft carries business people from Europe to Asia, aviation plays the seminal role of being the first link in the chain that might trigger any business transactions emanating from such travel.

At best, the current approach adopted by the world community to world trade regarding aviation is unfortunate for the aviation industry and in particular the air transport industry, which is relegated to a back seat in the face of other priorities such as poverty alleviation, health, and education. Although no rational argument exists to promote aviation over the other priorities mentioned (although it is a fact that institutions such as the World Bank must, as they correctly do, set their priorities towards eradicating poverty, ensuring health, and providing education),[59] it should not necessarily follow that aviation should be treated as inconsequential when it comes to support. If aviation is to be treated as a driver of the global economy, then the sustainability, safety, and security of the industry must, as of necessity, be treated with some degree of priority.

The irony in the above situation is that in Africa, and some parts of Asia and South America, air transport is one of the solutions to the problem of poverty. In the African continent in particular, which accounts for

57. Tourism: World's Largest Industry- From Zero To A Trillion $ In 100 Years (Lessons From the Future, Volume II), http://www.drtomorrow.com/lessons/lessons2/13.html (last visited October 9, 2007).

58. The World Bank, http://www.worldbank.org.

59. *Id.*

just 2 percent of the world GDP but hosts 13 percent of its population, the aviation industry has a vital role to play in achieving sustainable development.[60] Africa, being the smallest region for air services in the world, accounts only for 4.1 percent of the global passenger traffic and approximately 2 percent of the freight traffic of the world.[61] The tourism sector too is negligible in Africa compared to other regions of the world.[62] In 2001, tourism represented 3.4 percent of the GDP, although it has the fastest growth rate of tourist arrivals.[63] Therefore, the major potential contribution of air transport to Africa and its poverty alleviation program would be through air transport contribution to tourism. "Tourism contributes to poverty reduction by generating economic growth, providing employment opportunities and increasing [incomes generated through taxes and other levies]."[64] Tourism also serves as a major contributor to the trade balance in many African countries.[65]

Traditionally, the air transport industry fortunes have been irregular.[66] The airline industry, despite its glamour and perceived commercial power, has experienced marginal profitability and cyclical fiscal growth in the long term, with periods of growth and profit being watered down by less successful periods to follow.[67] One of the reasons for this fluctuating pattern is that the airline industry is driven by variable factors, such as operational and technological changes as well as regulatory control.[68]

To clearly view the aviation industry's ability to cope with the difficulties faced by the air transport industry, it is necessary to examine the dimensions of air transport, which are the only means through which one can glean the extent of its contribution to the world economy. Two things have to be done if the air transport industry is to be recognized as a major contributor to the world economy and trading process. The first is to treat air transport as a trading tool and not as a luxury. A liberalized trading process must be applied in the context of air transport. It is incontrovertible that liberalization of air transport is a global trend that is irreversible and has been ongoing since the 1980s.[69] In the liberalization

60. The Contribution of Air Transport to Sustainable Development in Africa, Air Transport Action Group (ATAG) IATA, A Report by the Oxford Economic Forecasting Group, October 2003 at 10.

61. *Id.* at 1.

62. *Id.* at 38.

63. *Id.* at 38.

64. *Id.* at 37.

65. *Id.* at 36.

66. Abeyratne, *supra* note 14, at 1.

67. *Id.*

68. *Id.*

69. Jeffrey N. Shane, ICAO Global Symposium on Air Transport Liberalization, (2006), *available at* http://www.dot.gov/affairs/jeffshane091806.htm.

process, fluctuations of global economic factors, as well as the national approaches to market access, continue to be the most critical elements in air services agreements between States. These factors remain integral to substantive regulatory liberalization should a State decide to radically alter its stance toward opening the skies. In considering liberalization of market access, States invariably face two basic issues: the extent of liberalization, i.e., how open the market access should be in terms of the grant of traffic rights; and the approach to liberalization, i.e., whether liberalization should be national, bilateral, regional, plurilateral, or multilateral, and the pace with which liberalization should be pursued.

The first step to poverty alleviation through aviation is liberalization of market access. Liberalization is realized when carriers are not fettered with unduly restrictive bilateral air services agreements. It would be largely up to each State to decide on the parameters of the air service agreements, depending of course, on its national and economic interest. Although basic third and fourth freedom traffic rights[70] are provided in most bilateral air transport arrangements as a starting point, most arrangements go beyond to cover a whole range of traffic rights, as well as other market access considerations.[71] The extent of market access being available to air carriers could vary widely because of such determinants as the competitive advantages and disadvantages of both States and carriers. Other factors affecting market access include size, location, and stage of development of States, and the competitive strategies open to particular economies driven by national policy. As for the approach to liberalization, the experience of the last two decades seems to suggest that States will endeavor as much as possible to utilize all the existing avenues in pursuing liberalization. This is assuming that States do not face an overt or covert threat to their economies.[72] A case in point is a State depending heavily upon tourism, where it will be in the interest of that particular State not to depend entirely on market decisions of air carriers bringing in tourist traffic to its territory.[73] "[M]any States have unilaterally introduced liberal air transport policies," frequently taking to consideration "a broader perspective of national interest including economic development and trade benefits."[74] It would be surprising if a State were to advocate and pursue liberalization without reservation, purely in order to promote

70. Third freedom traffic rights are rights of an air carrier to operate point-to-point air services from its country of origin to another country carrying passengers and freight for hire., Freedoms of the Air, http://www.icao.int/icao/en/trivia/freedoms_air.htm. Fourth freedom traffic is the exact reverse of third freedom. *Id.*

71. Worldwide Air Transport Conference: Challenges and Opportunities of Liberalization (2003), *available at* http://www.icao.int/icao/en/atb/atconf5/docs/ATConf5_wp008_en.pdf.

72. *Id.* at 2.8.

73. *Id.*

74. *Id.*

a liberal global air transport industry to the detriment of its own economy and industry. The bilateral approach continues to offer flexibility and viability through which States can expand air services while retaining the control over the pace and direction of liberalization. However, the serious disadvantage of bilateralism is that it may also be a constraint toward any attempt at achieving liberalization on a wide scale. This is because of the inherent inflexibility of the system in not being able to facilitate accord between a large number of involved States.

The underlying objective for liberalization in the long run should be to optimize efficient and economical trade and communication links among States, and to promote to the fullest possible extent national and regional growth and development. Simultaneously, each State should be ensured a meaningful participation in international air transport in accordance with the Chicago Convention. In the meantime, States can be expected to continue to pursue liberalization in market access at their own choice and pace, taking into account the related benefits and risks, using bilateral, regional and/or multilateral avenues as appropriate. Liberalization may also be gradual with phased introduction or by blocks of market access such as air cargo.

Second, air transport has to be linked to poverty alleviation. One must recognize that both big businesses and poor industrialists depend on air transport for the export of their goods and services. It is incontrovertible that tourism and aviation could pave the way for a new export-led trading structure that could, in turn, create sustainable development structures within lesser-developed countries.

III. The Economic Contribution of Civil Aviation

ICAO records that in the year 2003, airlines of the world carried 1,657 million passengers and some 35 million tons of freight.[75] During that year the world gross domestic product (GDP) grew approximately 3.9 percent in real terms, almost one percent higher than in the previous year.[76] While air transport is the main mode of business travel, and, therefore, contributes significantly to global commercial activity, there is no empirical study to compare the contribution made by the air transport industry to the world gross domestic product in real and quantifiable terms. ICAO has estimated that in the year 1998, the direct contribution of civil aviation, in terms of the consolidated output of air carriers, other commercial operators, and their affiliates, was $370 billion.[77] Direct on site employment at airports and air navigation services providers gener-

75. *The World of Civil Aviation 2003-2006, supra* note 21, at 3.
76. *Id.*
77. ICAO, Economic Contribution Of Civil Aviation, ICAO Circular 219, 2 (2004).

ated 1.9 million jobs, while production by aerospace and other manufacturing industries employed another 1.8 million people.[78] Overall, the aviation industry directly employed no less than 6 million persons in 1998.[79]

These direct economic activities have multiplier effects upon industries providing either consumer products or aviation-specific and other inputs.[80] In simple terms, "every $100 of output produced and every 100 jobs created by air transport trigger additional demand of some $325 and in turn 610 jobs in other industries."[81] For example, the total economic contribution of air transport, consisting of the direct economic activities and the multiplier effects, was estimated to generate $1,360 billion output and 27.7 million jobs worldwide in 1998.[82]

The total output result suggests that about 4.5 percent of the world output (in terms of real gross domestic product) may be attributed to air transport and its multiplier effects.[83] The findings on the direct contribution and multiplier effects remain generally relevant beyond the assessment year, particularly in view of the steep demand contractions of air travel in 2001, followed by two years of stagnation.[84] The ramifications of these preceding years for the entire civil aviation business testify of its importance for the local, regional, and national economies in which they are embedded.

In addition to its total output and employment impacts, civil aviation has a broader influence on overall economic growth, deriving from non-quantifiable benefits for the users of air transport, businesses, and individuals alike. Air transport acts as a facilitator for the development of markets and trading of goods as well as services.[85] In 2001, airline scheduled services carried more than 1.6 billion passengers and 30 million tonnes of freight worldwide.[86] Approximately 45 percent of some 714 million international tourists and some 40 percent by value of the world manufactured exports were transported by air that year.[87]

Measuring the economic contribution of civil aviation gives an account of the impact that air transport, aerospace, and other affected industries have in generating output and creating employment throughout a

78. *Id.*
79. *Id.*
80. *Id.*
81. *Id.* at 3.
82. *Id.*
83. *Id.*
84. Ruwantissa Abeyratne, *Sustainability of Air Carriers and Assurance of Services*, 68 J. AIR L. & COM. 3, 3 (2003).
85. ICAO, *supra* note 77, at 2.
86. *Id.*
87. *Id.*

given economy. Furthermore, air carriers and other operators purchase a wide range of products (goods and services) from primarily airports, air navigation services providers, governmental agencies, public corporations as well as aerospace manufacturing and other industries.[88]

At the national level, the stimulating economic impact of civil aviation as job creator and contributor to economic growth is evident when airlines, airports, air navigation services providers, aerospace industries, and their respective affiliates meet a growing direct demand for air transport services. This is accomplished by expanding operations and fleets, ordering more goods and services from suppliers, and by hiring more employees. These direct economic activities have multiplier effects upon other industries throughout an economy.[89] A wider or narrower spread of these multipliers will depend on the circumstances, notably the size of the industries associated with civil aviation and the assessment approach taken.[90] "For example, countries with significant aerospace manufacturing will show a wide spread, while those with limited air transport services may have a relatively narrow spread."[91] Non-aviation travel and tourism businesses, "such as hotels and restaurants, travel agencies, tour operators, and retailers" greatly benefit from trip-related expenses of airline passengers.[92]

The United States has shown exponential growth in the aviation industry and, as such, ICAO considers "the impetus of civil aviation in the United States economy . . . a good case study to demonstrate the procedural steps of the assessment phases" of the ICAO study on the economic contribution of civil aviation.[93]

> It has been evaluated over a number of years by Wilbur Smith Associates on behalf of the U.S. Federal Aviation Administration. In 2000 (the most recent year for which data is available), the provision of airline services, general aviation activities, airport operations, and acquisition of aircraft totalled an output value of $177.3 billion and created more than 1.2 million jobs. Expenditures associated with business and leisure trips by air totalled $176.3 billion and created over 3.1 million jobs. These direct and catalytic expenditures generated additional expenditures of $654.6 billion and over 5.5 million jobs through the indirect demand of suppliers and induced demand effects. These results for the U.S. economy can also be expressed as multiplier effects of the direct demand: every $100 of output produced and every 100 jobs created by civil aviation in 2000 trigger[ed] another U.S. $469 of output

88. *Id.*
89. *Id.* at 2-3.
90. *Id.* at 3.
91. *Id.*
92. *Id.*
93. ICAO, REPORT BY THE COUNCIL ON EVALUATION OF THE ECONOMIC CONTRIBUTION OF CIVIL AVIATION, Working paper: Economic Commission A35-WP/42, 4 (July 29, 2004).

> and 717 jobs in many different industries. The value of all economic activities of civil aviation and air travel-related expenses, plus indirect and induced multiplier effects, totalled U.S. $1,008.2 billion and employed 10 million people who earned $310.1 billion in 2000.[94]

Finally, compared to 1987, total output increased by 27.4 percent, while the number of jobs increased by 23.7 percent, and income rose by 31.8 percent.[95]

The fragile nature of the air transport industry calls for stringent measures to sustain the economic contribution of civil aviation to the world. At best, the air transport industry fortunes have been irregular.[96] The airline industry has experienced marginal profitability and cyclical fiscal growth in the long term, with periods of growth and profit being watered down by less successful periods to follow.[97] One of the reasons for this fluctuating pattern is that variable factors such as operational and technological changes, as well as regulatory control, drive the industry.[98] Overcoming the challenges ahead would essentially require a balance between these areas.

The shift in focus that confronts competition in commercial aviation largely lies in the compelling need for measures that would enable airlines to maximize on the potential available in the market. This would prevent the industry from falling apart. Since the beginning of regulated civil aviation in 1944, and until recently, competition was rigidly regulated and often based on predetermined capacity as a determinant of a carrier entitlement to enter a market. This stultified the global air transportation system.[99] The transition from a somewhat smoothly running, but cumbersome aviation industry was not easy because the air transport industry was comfortable and languid with established legacy carriers dominating a vastly untapped market.[100] However, the air transport system of the past had its advantages. Granted, there were not large aircrafts, there were not as many connections, and airline tickets could not be purchased online. In the past, a passenger almost anywhere in the world could purchase a ticket to fly seamlessly to almost any part of the world, through a complex but reasonably efficient set of working relationships

94. *Id.*
95. *Id.*
96. Abeyratne, *supra* note 14, at 1.
97. *Id.*
98. *Id.*
99. Chicago Convention on International Civil Aviation, Dec. 7, 1944, 61 Stat. 1180, T.I.A.S. 1591, 15 U.N.T.S. 295 [hereinafter Chicago Convention]; and World Trade Organization, International Trade in Air Transport: Recent Developments and Policy Issues, World Trade Report 2005: Exploring the Links Between Trade, Standards and the WTO 213, 224-26 (2005) [hereinafter World Trade Report 2005].
100. *Id.* at 224-26.

between hundreds of individual air carriers.[101] Transaction costs were low, where a single call to a travel agent at the corner of the street could finalize a transcontinental flight.[102] This was mostly possible because individual airlines themselves ensured the provision of all their services, infrastructure, and procedures to connect passengers and freight both within their own networks and those of connecting carriers.[103] At the airport, the passenger did not encounter heat sensitive monitors that sought to establish that he was the carrier of a communicable disease, nor were there physical checks of passengers and baggage. Industry standards and facilitation measures were in place through ICAO and the International Air Transport Association (IATA). Furthermore, procedures and clearance at the airport were hassle free and not subject to color coded security alerts.

Today, the story is somewhat different. Things have become more sophisticated. It was inevitable that they had to because market conditions changed and the demand for air transportation grew, (and keeps growing), at roughly double the rate of the growth in the general economy.[104] The exponential infusion of capacity to meet this demand requires costly systems and infrastructure to serve the consumer.[105] An inevitable corollary was that air transport became more expensive.[106] However, if only this were the issue, things would have been easily manageable. The prolific use of air travel by the public made air transport an easy target for terrorism and the free movement of disease causing vectors.[107] The threat of terror brought its own problems, requiring more expensive aviation insurance and the necessity to cancel flights every now and then.[108] Additionally, the proliferation of air travel brought in environmental concerns of aircraft noise and engine emissions,[109] problems of airport congestion, and slot allocation.[110] Worst still, competition between carriers to offer capacity made some of the carriers expand with the only objective being to provide services at any cost.[111] Critical services required for aviation safety, such as efficient ground handling and precise engineering were outsourced, with no guarantee of one hundred

101. *Id.* at 222-23.

102. Ruwantissa Abeyratne, *Competition in Air Transport – The Need for a Shift in Focus*, 33 TRANSP. L.J. 29, 30 (2006).

103. *Id.*

104. *Id.*

105. *Id.*

106. *Id.*

107. Ruwantissa Abeyratne, *Forensic Aspects of the Aerotoxic Syndrome,* 21 Med. & L. 179, 179-88 (2002).

108. ICAO, 2001 Annual Civil Aviation Report, ICAO J., Sept.-Oct. 2002, at 6, 12 (2002).

109. *See* World Trade Report 2005, *supra* note 104, at 224.

110. *Id.* at 223.

111. *Id.*

percent safety of a flight.[112]

The above notwithstanding, neither a single nation nor the global aviation community ever deregulated safety and security.[113] Responsibility still continues to devolve upon governments to provide additional capacity, find the money to fund safety and security inspectors, and ensure that their carriers operate air services with full insurance coverage, however expensive. This responsibility is in place so that the world economy will not run aground for lack of international air services.[114] Fortunately, all 188 States who are signatories to the Convention on International Civil Aviation (Chicago Convention) signed at Chicago on December 7, 1944, can rely on ICAO to find regulatory solutions that would keep the crisis from becoming unmanageable.[115] In the recent past, ICAO has regulated safety and security, established and conducted security and safety audits on Contracting States, adopted much needed principles of guidance on facilitation, assisted in preventing the spread of disease by air carriage, and even developed a global aviation insurance scheme in case things go wrong in the insurance industry the way they did immediately after September 11, 2001.[116]

"Since its inception as a regulated industry, the overriding theme of international civil aviation has been, and continues to be, the pursuit of friendship and understanding among the people of the world," with the ultimate objective of ensuring global peace.[117]

> Toward this end both the principles of air navigation and aviation economics have to ensure that aviation is developed in a manner that would make sure the world has a safe, reliable, economical, and efficient civil aviation system. An inherent characteristic of aviation is its ability to forge inroads into human affairs and promote international discourse. It also promotes international goodwill and develops a feeling of brotherhood among the people of the world.[118]

Therefore, it has been claimed that problems of international civil aviation constitute an integral part of the universal political problems of world organization, and, therefore, aviation problems cannot be solved without involving the world political and diplomatic machinery.[119] It is at this crossroads that one encounters the profound involvement of the International Civil Aviation Organization.

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112. *Id.*
113. Abeyratne, *supra* note 102, at 32.
114. *Id.*
115. *Id.*
116. *Annual Review of Civil Aviation 2003*, 59 INT'L CIVIL AVIATION J. 4, 5-6 (Sept. 2004).
117. Taïeb Chérif, *Foreward* to KOSTAS IATROU & MAURO ORETTI, AIRLINE CHOICES FOR THE FUTURE: FROM ALLIANCES TO MERGERS (Ashgate 2007).
118. *Id.*
119. Abeyratne, *supra* note 102.

At present, the most critical challenge facing international civil aviation is to sustain the air transport industry and assure the consumer continuity of air transport services. The initial setback suffered by the industry as a result of the events of September 11, 2001, and the combined impact of the economic downturn and precipitous decline in air travel during the period that immediately followed, portended an inevitable gloom for the air transport industry, which resulted in the abrupt downfall of air traffic globally during 2001.[120] The retaliation by the world community against terrorism increased the airline passenger's fear and reluctance to use air transport.[121] Increasing costs of security enforcement and insurance prompted air carriers to cancel or postpone their new aircraft requisition orders.[122] Many carriers, particularly in developing countries, were compelled to revisit their cost structures and downsize their human resource bases.[123]

In the years that followed, the build up to the war in Iraq in 2002, the war in 2003, and the outbreak of Severe Acute Respiratory Syndrome (SARS)[124] all added to the initial setback of September 2001.[125] These unfortunate historical landmarks indeed proved to be the four horsemen of the Apocalypse resulting in serious ramifications for air carriers. Their ill effects were seen in the rising costs of security and insurance, massive layoffs of employees, drastic reduction of non-profitable routes, closure of facilities, and cessation of aircraft operations.[126] In the manufacturing industry, previously ordered aircraft delivery was deferred, resulting in significant cutbacks in employment in the aerospace industry and a colossal loss to the industry in 2002.[127] Airports and air navigation service providers suffered a similar fate, losing income from user charges and non-aeronautical revenues, while simultaneously facing enhanced insur-

120. Markus Franke, *Competition Between Network Carriers and Low Cost Carriers—Retreat Battle or Breakthrough to a New Level of Efficiency?*, 10 J. AIR TRANSP. MGMT. 15, 16 (2004).

121. *2001 Annual Review of Civil Aviation 2003*, 57 INT'L CIVIL AVIATION J. 12 (July/Aug. 2002) (The International Civil Aviation Organization recorded that following the events of September 11, 2001, total passenger traffic decreased by 3.9 percent over the previous year and international freight tonnes kilometers by approximately 5 percent).

122. Abeyratne, *supra* note 102, at 31 (citing Yann Cochennec, *What goes up. . . Aircraft orders and deliveries slid dramatically in 2002, but 2003 will be even tougher*, INTERAVIA BUS. & TECH., Jan. 1, 2003).

123. *Id.* (citing Peter Morrell & Fariba Alamdari, The Impact of 11 September on the Aviation Industry: Traffic, Capacity, Employment and Restructuring 7 (Int'l Labour Office Working Paper No. 181, 2001), *available at* http://www.ilo.org/public/english/dialogue/sector/techmeet/tmica02/tmica-wp181.pdf (last visited Sept. 13, 2006)).

124. *See* Ruwantissa I.R. Abeyratne, *International Responsibility in Preventing the Spread of Communicable Diseases through Air Carriage - The SARS Crisis*, 30 TRANSP. L.J. 53 (2002).

125. 2001 Annual Review, *supra* note 127, at 12.

126. Abeyratne, *supra* note 102, at 31 (citing Cochennec, *supra* note 122).

127. *Id.* at 29, 30.

ance and security costs.[128]

These setbacks notwithstanding, current trends dictate that the world economy will remain moderately stable and healthy in the near future, despite a slowdown in economic growth.[129] In the short term, inflation may hold steady and inflation rates will probably decrease gradually.[130] The continuing upward trend in fuel prices is likely to increase airline fixed costs, and aviation will increasingly be defined in trade terms, whilst being a strong candidate for trade liberalization with a firm focus on services.[131] In the years ahead, individual airlines will be compelled to remain competitive. They will need to flow with the tide of emergent and future commercial trends such as privatization, the use of information technology, and removing infrastructure constraints and governmental restraints.

Air travel has several determinants in regard to demand. Primarily, it is determined by income levels and demographics and the cost of air travel.[132] With regard to the cost of air travel, world energy demand, supply, and prices are key factors which drive both the profitability of the air carrier and the cost factor involving the use of travel offered by the carrier to the consumer.[133]

All the above indicators incontrovertibly point to one central driver of future air transport competition, which will help the increasing influence of global alliances and partnerships between carriers to be a key element in industry strategic development where more groups of airlines will provide direction and focus. Airline management, geared towards competition, will be called upon to improve coordination, and provide integration and stability to the air transport industry, calculated to result in the inevitable corollary of cost reduction.

The outsourcing of non-core activities will continue among airlines, encouraging fledgling carriers to emerge in a liberalized market. Larger airlines will seek franchising and code sharing agreements with other airlines to the furthest extent possible, and will not disregard the importance of creating low cost subsidiaries, while also looking to consolidate their services with other carriers. In the process, existing distinctions between scheduled and nonscheduled (charter) carriers will be minimalized. In

128. *Id.* at 31 (citing 2001 Annual Review, *supra* note 127, at 24).

129. Annual Review 2003, *supra* note 121, at 4.

130. Abeyratne, *supra* note 102.

131. PAT HANLON, GLOBAL AIRLINES: COMPETITION IN A TRANSNATIONAL INDUSTRY 22-24 (Butterworth-Heinemann 1996); WTO, International Trade in Air Transport: Recent Developments and Policy Issues, in World Trade Report 2005: Exploring the Links Between Trade, Standards and the WTO 213, 221 (2005), *available at* http://www.wto.org/english/res_e/booksp_e/anrep_e/wtr05-3b_e.pdf (last visited September 6, 2007) [hereinafter *World Trade Report 2005*].

132. Hanlon, *supra* note 131, at 12.

133. Abeyratne, *supra* note 102, at 32 (citing Hanlon, *supra* note 131, at 22).

terms of service distribution, airlines will invest in e-commerce, concentrating as much as possible on selling their services directly online.

The growth in commercial air services has continued to outstrip the available capacity at more and more airports.[134] Although many airports with congestion problems are located in Europe, a growing number of airports in other regions are reaching capacity limits.[135] Moreover, because of the interconnected operations of the international air transport system, capacity constraints at some airports impact other airports.[136] This is becoming an increasing challenge to the continued growth of air transport and is having an impact on further liberalization with respect to market access, requiring, in some instances, airports to enter into alliances with one another.[137]

Governments, airlines, and airports have each developed measures to overcome or ameliorate situations of insufficient airport capacity.[138] Many States have either expanded existing airports, built new ones, paved new runways or added terminals.[139] However, environmental, economic, political, and physical constraints have, in some instances, prevented physical expansions to increase airport capacity.[140] At least one inter-governmental body and a regional body have taken action to improve air traffic control systems designed to increase the capacity of air traffic management at airports.[141] Airports and air carriers have been able to enhance airport capacity by improved facilitation at existing facilities,[142] despite increased security requirements after the events of September 11, 2001, which have limited capacity enhancements in this area.[143]

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134. *See World Trade Report 2005*, *supra* note 137, at 223.

135. *Id.*

136. *See* Hanlon, *supra* note 131, at 140-41.

137. *Id.* at 148.

138. Abeyratne, *supra* note 102, at 34.

139. As was noted by the WTO:

> A number of high growth international ports, such as Hong Kong, China (1998), Osaka (1994), Kuala Lumpur (1998) and Shanghai (2002) have built new airports to deal with the [capacity] problem . . . London's Heathrow airport is particularly notable for the capacity constraint problem. After decades of struggling to deal with congestion, the authorities have decided to build a new terminal and a short runway.

World Trade Report 2005, *supra* note 137, at 223.

World Trade Report 2005, *supra* note 137, at 223.

140. *Id.*

141. For example, in April 2001, the Federal Aviation Administration (FAA) announced a set of initiatives in its Operational Evolution Plan, which is designed to increase capacity within the United States national air space. *See Air Traffic Control: Role of FAA's Modernization Program in Reducing Delays and Congestion: Testimony Before the Subcommittee of Aviation, Committee of Commerce, Science, and Transportation, U.S. Senate*, GAO-01-725, 5 (2001) (statement of Gerald L. Dillingham, Director of Physical Infrastructure Issues).

142. Annual Review of Civil Aviation 2003, *supra* note 121, at 10.

143. Abeyratne, *supra* note 102.

Revenue and investment management is a key concept, which has pervaded the air transport industry, particularly in the wake of trends in privatization of airports and air navigation services.[144] Both airports and air navigation services need to consider issues involved in privatization in order to manage their revenues and investments. Along with the burgeoning need for an increase in airport capacity, to accommodate the demand for increasing air transport capacity, comes the issue of proper fiscal management of income derived by airports and air navigation services providers. Intrinsic to the issue of revenue and investment management are considerations of cost pricing, liability, and duties imposed upon a privatized entity. These aspects have to be managed if successful revenue and investment management are to be accomplished.[145] Intrinsically, an examination of appropriate cost pricing and revenue allocation will be a significant item on the agenda of both airport and air navigation service providers in the near future.[146]

The preeminent regulatory challenge confronting air transport is to update policies, guidelines and other regulatory instruments to address changes in the aviation environment. Competition, when coupled with liberalization of air services taking place on an international scale, inevitably calls for a more open and free approach.[147] However, it is not prudent to consider air transport services as being just another normal economic activity. The overarching objective of ICAO, as contained in Article 44 of the Convention on International Civil Aviation, is for ICAO to foster the planning and development of international air transport so as to meet the needs of the people for safe, regular, efficient, and economical air transport.[148] This is a most fundamental challenge, which not only draws the inference that air transport is a public utility,[149] but also issues a challenge to ICAO, its Contracting States, and their carriers to ensure the provision of a safe service satisfying fixed standards of continuity, regularity, capacity, and pricing.

The inherent characteristics of air transport, of being a public utility[150] on the one hand and of being confronted with the danger of over regulation on the other, admit of the need for a delicate balance between

144. Gunnar Finnsson, Move to Privatization of Airports Requires Careful Consideration of Numerous Factors, 48 INT'L CIVIL AVIATION J. 18 (Jan./Feb. 1993).

145. Abeyratne, *supra* note 102.

146. *Id.*

147. *Id.* at 33.

148. Chicago Convention, *supra* note 104, at art. 44.

149. Int'l Civil Aviation Org. [ICAO], Policy and Guidance Material on the Economic Regulation of International Air Transport, at 1-18, ICAO Doc. 9857 (2nd ed.1999) [hereinafter *ICAO Economic Policy Guidance Material*], *available at* http://icaodsu.openface.ca/documentItemView.ch2?ID=7951.

150. Abeyratne, *supra* note 102.

untrammelled competition and suffocative regulation. While the first approach may give rise to the usual free market inhibitors such as airport, airway, and runway congestion, the other approach may ground to a halt the services that may provide air transport commensurate with the demand.

In order to face the exponential growth of the air transport industry, it is inevitable that competition and liberalization should be given serious consideration as a current and future trend in the aviation field. What is needed foremost, in order to improve international cooperation toward achieving a well meshed and overall competitive policy, is to consider the various possible options available. One of the options to promote competition and facilitate trade in air transport lies indisputably in combating and eliminating anti-competitive practices. State responsibility toward achieving this goal is a key factor.[151] One way of ensuring collective State action in this regard, might be for States to enter into understandings or agreements toward combating restrictive trade practices, either bilaterally or plurilaterally. Along with a plurilateral framework of competitive policy, there also should be a concomitant bilateral structure of individual agreement between States to stringently monitor anticompetitive conduct. This can only be achieved with a robust and effective international legislative structure.[152] The important role played by public international law in this regard cannot be denied.[153]

As for liberalization of air transport, there has so far been no indication that any State favors total liberalization, calculated to open out its domestic market.[154] Strategic alliances between airlines, whether through mergers or other arrangements, will be viewed with caution and objectivity by individual airlines and States. This will act to preclude the total overrunning of local interests. It is this consideration that would make liberalized ownership and control criteria less attractive to local entrepreneurs who would not encourage foreign ownership to encroach on local control airlines have of their own markets.

The two integral areas that will carry the sustainability of air carriers and assurance of air services in the years to come will be regulatory control and economic strategy. From an economic perspective, it is inevitable that competition will be between airline alliances rather than individual carriers.[155] Markets will be unstable, and in the case of individual airlines, only those who go back to basics to offer the consumer a

151. *Id.* at 34-35.

152. *Id.*

153. Abeyratne, *supra* note 102.

154. *Id.*

155. Abeyratne, *supra* note 84, at *37.

service as value for money will survive.[156] Ethical and moral consideration of economics, in terms of strategic airline management that provides for quality customer service, will play a major role in airline sustenance and will be the bottom line for the years to come.[157]

From a trading perspective, both States and carriers must share equal responsibility to ensure continuity of air transport services.[158] The uniqueness of the operation of air transport services as a trading practice lies in the symbiosis required for its sustenance between States and carriers.[159] This peculiar relationship requires that a certain responsibility devolves upon States to ensure the prosperity of its air transport industry and to prevent the industry from collapsing.[160] Although air transport may be heavily privatized in some instances, particularly in the developed world, it does not take away the overall regulatory supervisory role of the State and its obligation to support its carriers.[161]

From a regulatory perspective, the challenges faced in the economic field are to update and promote ICAO policies and guidelines to meet the demands of a changing environment, and to seek a balance between promoting economic growth in the industry, advancing civil aviation, and strengthening security measures and facilitation. In order to address these challenges, all players involved need to seek a harmonious relationship between a liberalized economic regulatory framework and proper safety, security, social, and labor standards.

Economic activity in air transport, particularly in the movement of aircraft between States, should be viewed in the context of sustainable development, where environmental protection would play a key role. Although air transport does not pose catastrophic environmental consequences on a short-term basis,[162] it has become opportune to address trade in air transport and its effect on global environmental welfare as a composite whole, rather than within a fragmented framework. The economic aspects of environmental protection, particularly in the areas of noise charges and emissions trading as a market based option, is an inevitable challenge, particularly when it concerns global consensus on criteria for levying such charges and their quantification.

A compelling feature in any investment policy concerning air transport must include policies encouraging foreign investment in civil avia-

156. *Id.*
157. *Id.*
158. *Id.*
159. *Id.*
160. *Id.*
161. *Id.*
162. Dave Southgate, *Aircraft Noise – A Broad-Area Issue*, ICAO Environmental Report 38 (2007), *available at* http://www.icao.int/icao/en/env/pubs/Env_Report_07.pdf.

tion, including investment in airports and general aviation. Airline ownership and control provisions in local legislation and bilateral air services agreements must be relaxed to encourage foreign equity in the air transport industry. A moderate rental policy should also be adopted by the State to preclude undue burden on the airports. The supply of seat and freight capacity must be realistic and consistent with demand, compelling a reduction in aircraft orders.

Despite the past forecast of a substantial loss to the air transport industry in the five years ending in 2005, ICAO forecasted that scheduled passenger traffic would grow by 5.2 percent in 2006.[163] This brings to bear the need for investment, to ensure that the necessary air transport services will be available to the public, while also making sure that over-investment in aircraft capacity is avoided at all cost.

IV. Investing in Airports

Airports, particularly in developing nations, have attracted significant private sector investment in the past 20 years, in spite of the grave financial risks involved.[164] However, in the 1990s, a growing trend emerged, which increasingly encouraged governments to turn to the private sector for assistance in strengthening and stabilizing efficiencies in the provision of airport infrastructure services.[165] Other interests in the private sector were spurred on by its expertise in raising revenues and eradicating mismanagement and neglect that had alienated assets under governmental control.[166] The overall objective of governments when leaning toward the private sector was to salvage assets, provide a more efficient service, and obviate governmental interference in tariff and investment policy decisions.[167] At present, the trend toward private investment in airports is facilitated by the globalization and liberalization of the world economies, which have resulted in the ownership and management of airports to undergo significant changes.[168] Of course, each model of privatization and investment in airports and their infrastructure have different variants which are applied diversely to suit individual business and political models.[169]

It is noteworthy, that at its incipient stage, international civil aviation

163. *The World of Civil Aviation 2003-2006, supra* note 21, at 84.

164. Ruwantissa Abeyratne, *Towards a SAARC Common Aviation Policy*, Asian Law, March, 2005 [hereinafter *Towards*].

165. *Id.*

166. *Id.*

167. *Id.*

168. *Id.*

169. *Id.*

relegated to the airport the status of a terminus,[170] much the same as a bus terminus of that time, assigning it as the focal geographical point at which people gathered to embark on a plane for a journey by air, or disembark after an air journey.[171] However, airports are now complex industrial enterprises.[172] Quite apart from the essential airside support given by airports to landing and departing aircraft, there are commercial facilities provided for both passengers and the public within the terminal building by concessionaires who are specialists in their own fields of business.[173] The airport authorities collect concession fees (non-aeronautical revenues) from the concessionaires. In numerous airports around the world, the income derived from such resources is significant, often exceeding traditional income derived through the provision of airport and air navigation services (aeronautical revenues) to incoming and outgoing aircraft.[174]

The paradigm shift which changed the nature of an airport from being a place where a person enplaned to travel to another country, to also being a complex entrepreneurial enterprise, has compelled governments to view airports as being of significant commercial potential.[175] The conventional practice of investment by States in airports is becoming increasingly unpopular and difficult because of pressure to finance other more pressing and high-priority services, e.g., public health, education, and social services.[176] From an economic perspective, it is incontrovertible that most States that have privatized their infrastructure have stood to gain financially, particularly when the revenue from privatization is injected to the government coffers.[177] Cases-in-point are airports under the British Airports Authority, the largest group of privatized airports in the United Kingdom and Australia.[178] In the case of the United Kingdom, several airports have been subject to long-term leases for up front payments.[179] The role of government at the post-privatization stage is substantially different from the role played when an airport is under government control. After privatization, governments are no longer responsible for management and development of airports.[180] Management of facilities of the air-

170. *See* ICAO, CIRCULAR 3-AT/1: AIRPORT ECONOMICS 9 (1948) (Giving an early definition of airports).

171. *Towards, supra* note 170.

172. RIGAS DOGANIS, THE AIRPORT BUSINESS 7 (Routeledge 1992).

173. *Towards, supra* note 170.

174. *Id.*

175. *Id.*

176. *Id.*

177. *Id.*

178. *Id.*

179. Tulsi Kesharwani, *Privatization of Aviation Infrastructure*, ASIAN INSTITUTE OF TRANSPORT DEVELOPMENT: NEW DELHI, at 160 (2002).

180. *Towards, supra* note 170.

port is transferred to the new administration, as well as the collection of airport charges and other revenues.[181]

Usually, apart from the basic advantage of attracting more finances to the government treasury, there are three reasons that impel a government to open an airport for public issue: lack of government funds to expand airport capacity to meet the demands of air transport, increase of efficiency of the airport and its services through private sector involvement, and the opening of a wider choice for airlines operating into the airport in terms of hub operations.[182]

The United Nations introduced a global perspective on privatization by endorsing the practice, particularly by a General Assembly Resolution in 1992,[183] which, while recognizing the sovereign right of each State to decide on the development of its private and public sectors, notes that "the private sector plays a positive role in mobilizing resources and promoting economic growth and sustainable development."[184] The Resolution goes on to urge all concerned to support "national efforts of countries in implementing privatization, de-monopolization, administrative deregulation and other relevant policies in the context of their economic regions and the opening of their economies."[185]

Privatization of an airport brings to bear a certain focus on the changed status of the airport, particularly in terms of ownership and management, and the inevitable corollaries of legal liabilities and fiscal responsibility, which change hands.

V. Conclusion

A compelling feature in any investment policy concerning air transport must include policies encouraging foreign investment in civil aviation, including investment in airports and general aviation. Airline ownership and control provisions in local legislation and bilateral air services agreements must be relaxed to encourage foreign equity in the air transport industry, and a moderate rental policy should be adopted by the State to preclude undue burden on the airports. The supply of seat and freight capacity must be realistic and consistent with demand, compelling a reduction in aircraft orders.

Despite the forecast of a substantial loss to the air transport industry in the five years ending in 2005,[186] ICAO forecasted that scheduled pas-

181. *Id.*
182. *Id.*
183. G.A. Res. 47/171, U.N. Doc. A/RES/47/171 (Dec. 22, 1992).
184. *Id.*
185. *Id.*
186. ICAO, *World Air Passenger Traffic to Rebound Strongly in 2004 and Continue to Grow*

senger traffic will grow by 5.2 percent in 2006.[187] This brings to bear the need for investment, to ensure that the necessary air transport services will be available to the public, while also making sure that overinvestment in aircraft capacity is avoided at all cost.

Investment in air transport will also have a beneficial effect on the robust synergy between aviation and tourism, particularly because of the overarching dependence by the tourism industry on aviation for the carriage of tourists to their destinations. The growing interdependence between the two industries has resulted in a significant increase in the combined contribution of aviation and tourism to the gross domestic product, generating employment and investment opportunities.

The World Bank has reported that a robust global investment climate is central to growth and poverty reduction. In this regard, the preeminent goal of governments should be to create opportunities for the private sector for investment, while simultaneously creating expansion and employment within the State sector. In other words, the goal should be to create a sound investment environment for everyone so that society as a whole will benefit. Of course, this is easier said than done, as developing nations have their own internal concerns and pressing needs brought to bear by both social and natural factors. It calls for a certain symbiosis between the developed and developing world, as well as an enduring commitment from the international community to assist the developing world in three main areas: removing distortions in developed countries that harm the investment climates of developing countries, providing increased and effective assistance, and sharing knowledge and experience. These three areas of contribution from the international community have to be applied to the basic axiom that economic development requires adequate and effective transportation. Each country has a theoretically optimum amount of transport capacity. Transportation plays a multifaceted role in the pursuit of development objectives of a nation as well as the need to maintain international communication networks. Air transport enables goods and passengers to be transferred between and within production and consumption centres. Therefore, it could be argued that investment is vital to air transport.

in 2005 and 2006, available at http://www.airportsinternational.co.uk/pdfs/nr.pdf (last visited Sept. 16, 2007).

187. *Id.*