Organisation de Coopération et de Développement Économiques
Organisation for Economic Co-operation and Development

06-Nov-2014

English - Or. English

DIRECTORATE FOR FINANCIAL AND ENTERPRISE AFFAIRS
COMPETITION COMMITTEE

ANNEX TO THE SUMMARY RECORD OF THE 121st MEETING OF THE COMPETITION COMMITTEE HELD ON 18-19 JUNE 2014

-- Summary Record of the Discussion on Airline Competition --

This document prepared by the OECD Secretariat is a detailed summary of the discussion held during the 121st meeting of the OECD Competition Committee on 18-19 June 2014.

More documents related to this discussion can be found at www.oecd.org/daf/competition/airlinecompetition.htm

JT03365718

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SUMMARY OF DISCUSSION

by the Secretariat

The Committee Chair, Frederic Jenny, pointed first to the high number of contributions (33 in total) received for this roundtable, which highlighted the great importance of the airline competition topic. He then introduced the four expert panellists: Professor Severin Borenstein, E.T. Grether professor of business administration and public policy at the Haas School of Business; Mr. John Balfour a legal practitioner from Clyde & Co; Professor Pablo Mendes de Leon, professor of air and space law at Leiden University and Mr. Brian Pearce, IATA's chief economist.

The Chair also presented the four main topics for discussion. The first topic would pertain to liberalisation and de-regulation of the airline industry and to the evolution of its regulatory frameworks (Section 1). The discussion would then move on to structural and behavioural factors affecting competition among airlines (Section 2). The third and most central part of the discussion would address anti-trust issues and competition enforcement, including market definition, merger control, horizontal agreements and unilateral conduct (Section 3). Last, time permitting, delegates would be invited to discuss challenges ahead and evolutions to come in airline competition, focusing notably on the impact of state intervention in the airline sector (Section 4).

Before starting the roundtable discussions, the Chair invited the OECD Secretariat to present its Background Note.

The Secretariat first indicated that the Background Note focused on civil air transportation of passengers. After highlighting the importance of the air transport sector, it was noted that although liberalisation has indeed injected market dynamics, its impact should not be overstated. Liberalisation has not occurred everywhere and even where it has occurred, the sector is still heavily regulated at two levels. At international level, traffic rights still depend on bilateral air service agreements, which often include nationality conditions. At national level, a trend towards re-regulation can be observed, especially where market distortions cannot be addressed through anti-trust enforcement.

Two of the most driving industry features were mentioned. The first one is the entry of low cost carrier into markets which has undoubtedly brought important benefits to consumers and stimulated competition. Today, however, we are witnessing a phenomenon of hybridisation of business models, blurring the traditional distinction between full service or legacy carriers and low cost carriers. While competition law-makers and enforcers tend to focus on LCC entry in their decisions, hybridisation may need to be increasingly taken into account. The second feature is the emergence of alliances as the main way adopted by airlines to do business together. Alliances make sense economically and legally, essentially by allowing airlines to pursue synergies while retaining their nationality. Three recent trends that characterise and influence airline alliances today were highlighted: stratification, equity-based alliances and the emergence of Gulf carriers.

Regarding competition enforcement in the airline industry, it was observed that unilateral conduct cases are rare. It is unclear whether this scarcity is due to detection difficulties or to uncertain legal tests. It

is critical however to address these questions, especially in the airline industry where dominance may be unavoidable on certain routes.

Regarding horizontal agreements in the airline sector, alliances play a major role. A variety of anti-trust enforcement mechanisms are used across jurisdictions to assess airline alliances, ranging from merger control used e.g. in Brazil or India, to anti-trust immunity with the US DOT or to airlines' self-assessment in the EU. Two risks stem from this inconsistency: on the one hand, a risk of enforcement tool shopping; on the other hand, a risk of efficiency loss in competition enforcement as well as in the benefits expected from the alliance. Finally the Secretariat highlighted some open questions around the substantive analysis of alliances. First, recent studies cast doubt as to whether alliances have generated efficiencies at all and, if so, for whom. Second, has alliance competition to some extent replaced airline competition? Competition cases suggest that enforcers are increasingly relying on the latter. Last, more emphasis should maybe be put on the impact of network effects and multi-market contact and on the risk of co-ordinated effects. The growing importance and complexity of airline alliances make competition authorities' role ever more important in ensuring consumer welfare.

1. Today's de-regulated environment in which airlines operate and compete

1.1 De-regulation and liberalisation processes

The Chair thanked the Secretariat for the introduction and gave the floor to Mr. Balfour.

Mr. Balfour introduced the regulatory framework for international civil aviation, which is based on the Chicago Convention. Its key provision establishes that each state has complete and exclusive sovereignty over the airspace above its territory. As a result, bilateral agreements have been entered into by states throughout the world. Traditionally these agreements have been very restrictive, aiming to protect national carriers. Recently, however, more liberal agreements have been signed. Bilateral agreements often provide that operations may be withheld or withdrawn if an airline is not substantially owned and effectively controlled by local nationals. This explains why airlines have preferred to enter into alliances as opposed to acquisitions.

Mr. Balfour then went on to discuss the EU framework. Air transport was initially exempted from the scope of the Treaty of Rome. Following the US de-regulation, two changes took place in the EU. First, the European Court of Justice held in the *Nouvelles Frontières* decision that competition rules applied to air transport. Second, Council voting requirements on air transport issues changed from unanimity to qualified majority. As a consequence, three legislated packages were adopted. These led to a free internal market where air transport access and fares were completely liberalised. Common rules on airline licensing were also established. This put an end to national monopolies and allowed airlines to establish themselves and/or to acquire other airlines in other Member States.

Mr. Balfour also explained the necessity to control anti-competitive behaviours in a liberalised sector. Airline-specific rules in the EU notably concern state aid for which there is an exceptional regulation enabling the European Commission to intervene against state aid given by third countries to their airlines. Mr. Balfour concluded by stating that liberalisation in the EU has been an enormous success and is being exported to other countries by agreements concluded by the EU.

The Chair thanked Mr. Balfour and asked Prof. Borenstein to discuss the US de-regulation process.

According to **Prof. Borenstein** the 1978 de-regulation in the US pertained only to domestic markets. Prior to de-regulation, prices were set by the government and airlines needed government authorisation to enter a route. Airlines competed on the number of flights per route, leg room, quality of aircraft and aggressive advertising. De-regulation lifted route access and price restrictions. This coincided with a

growth in open skies agreement between the United States and other countries. There has however been almost no movement towards cabotage, except within the EU.

Prof. Borenstein then discussed industry characteristics and de-regulation highlights. The industry has witnessed a lot of market entries and exits and real fares have substantially declined (though they are now rising again). Over the history of airline de-regulation, on domestic service alone, air carriers have lost more than US $50 billion. Routes have also become more concentrated and airport dominance has generally increased. Legacy airlines, which had costs 30% to 40% above those of low cost carriers, have slowly managed to diminish this gap and have retained a dominant share of the industry. Recently important mergers have also taken place, decreasing the number of airlines.

Prof. Borenstein further highlighted two issues. First, early research has found that route and airport concentration leads to higher fares and gives real market power to airlines. The model of contestability, which is that threat of entry keeps routes as competitive as actual entry, is widely rejected. Second, economies of density (flying more passengers between two points) tend to be quite important and feed into the economies of the hub model. Economies of network and scope, on the other hand, have not been established. In addition, three trends have been witnessed since the 1980s: expansion and contraction of hub networks, steadily increasing load factors and expansion of low cost carriers.

Prof. Borenstein then tried to reconcile declining real prices with concerns about market power and losses in the industry. He notably pointed to the fact that the airlines losing most money have high costs and that overall airlines have been doing quite well recently. He also showed that if fare prices have gone down and costs have remained constant, load factors have increased. Finally, he highlighted that average price premiums due to hub dominance effects have steadily declined.

Prof. Borenstein explained that when airlines think about their ability to raise prices, they look at share gap, which is a measure of how effectively an airline can maintain loyalty of local passengers. Corporate programmes have an important impact on this because they require a share of a company's business. Share gap has been particularly high since the 1990s. The remaining challenge in the US pertains to loyalty effects. Prof. Borenstein insisted that the ability to deal with such loyalty effects will determine whether fares will stabilise or keep increasing. This is in part due to the fact that loyalty programmes have two effects when there are a small number of airlines in the market. They raise barriers to entry and divide markets because airlines know that poaching customers at the hub of another airline will be particularly difficult.

The Chair thanked Prof. Borenstein and invited Prof. Mendes de Leon to discuss de-regulation in the rest of the world.

According to **Prof. Mendes de Leon**, traditional aviation regimes are formed by bilateral agreements. More liberal regimes started emerging through open skies agreements, which were initiated by the US in 1992. These open skies agreements have also been adopted in other parts of the world.

Prof. Mendes de Leon then discussed current industry dynamics and evolutions. Code sharing agreements, which started in the US in the late 1980s, have become common place. The three major alliances tend to be dominated by EU and US carriers, but still regroup carriers from all parts of the world. Some airlines have started investing into other carriers to get access to foreign markets. This is raising a lot of attention from European and other competition authorities. Franchising has also taken place. Finally, particularly in South America and East Asia, airlines are establishing daughter companies.

According to prof. Mendes de Leon, while previously civil aviation authorities had a prominent position and competition had a relatively modest role to play with respect to these industry developments,

this is changing. The problem is that there is no global competition regime or authority enforcing it, which makes dealing with cross-border alliances, investments and other airline practices complicated. Cross-border competition enforcement relies on the effects doctrine, positive comity and agreements between competition authorities. Consequently, the markets that are most affected will determine which competition authorities are competent to examine a specific case. A recent example of airlines facing investigations by multiple competition authorities concerns the air freight cartel case.

Prof. Mendes de Leon also highlighted the airline behaviours that can affect competition, including state aid which has been mentioned in relation to Middle Eastern carriers.

Prof. Mendes de Leon concluded with a few observations: thanks to de-regulation, airlines have more room to act in accordance with commercial realities. With less state interference competition authorities also have more room to act. Conflicts may arise regarding legal regimes and authorities; and regional approaches are gaining importance. The International Civil Aviation Organization (ICAO) is also examining issues in the airline sector quite deeply, whereas airline services are excluded from the scope of the WTO's mandate.

1.2 The impact of de-regulation and liberalisation: industry and country perspectives

The Chair turned to Mr. Pearce to provide perspectives from the industry and IATA.

Mr. Pearce indicated that he would offer a global perspective, highlighting key features and trends of the commercial industry. First, he stressed the overall importance of the air transport sector for the economy. In the last 20 years, city connections have doubled, supply chains have been globalised and production has been fragmented. About one third of world trade by value is carried by air transport. Second, consumers have captured a lot of the value generated by air transport services. Costs have also fallen substantially over the last six decades: while this decline has paused over the last decade, in particular due to increased energy costs, prices have reflected these falling costs.

Mr. Pearce explained that the industry had not offered good value for investors. Since de-regulation, net profit margins worldwide have averaged 0.2% after debt interest and tax per year. According to Mr. Pearce, the passing off of cost decline to consumers and the lack of value for investors suggest that power has not been exploited by airlines. Over the last two decades, return on invested capital has been below the weighted average cost of capital. The industry is thus making economic losses. Mr. Pearce gave four suggestions as to why economic losses have been persistent. First, there may be some market power in other parts of the air transport value chain. Second, there could be excess capacity because capital markets are not working perfectly. Third, a lot of the costs that airlines are facing are common and joint, and recouping these costs can be difficult. Fourth, structurally, a financially sustainable equilibrium might not be possible.

Mr. Pearce concluded with two observations: first, except where governments bar entry through restrictive air service agreements, entry into the airline industry is relatively easy; and second, the industry is marked by significant failures and exits, including of low cost airlines. Mr. Pearce believes that these two features show that there is some contestability in airline markets.

The Chair expressed some doubts on how to reconcile the interventions of Prof. Borenstein and Mr. Pearce on the issue of contestability. According to Mr. Pearce, entry is relatively easy, there is mobility of capital and exit happens, which would lead to think that the contestability hypothesis is verified. The Chair invited Prof. Borenstein to comment on this.

Prof. Borenstein explained that in the US and most probably in Europe, entry is accompanied by large drops in air fares, which would be evidence against the concept of contestability. In the US, data has upheld the fact that without actual entry, prices tend to increase.

After having heard about the European, the US and the regional and global views from the experts, the Chair invited delegations to share their national views on the process and consequences of liberalisation. The Chair first turned to Indonesia which so far has only had a limited experience with liberalisation.

The delegate from **Indonesia** first gave an overview of the Indonesian airline industry, which started with one state-owned airline in 1950. With de-regulation, the number of airlines increased from 7 in 1999 to 27 in 2004. Now there are 17 private companies, mainly low cost, connecting 454 routes and 297 airports.

The delegate then offered his view on competition issues arising in the airline industry in Indonesia. One of them concerns price fixing, which is considered very harmful for consumers by the competition authority and is thus prohibited by law. Indonesia's contribution discusses two related cases, including the privilege INACA had between 1997 and 2002 to fix tariffs for economy class flights on domestic routes. The KPPU suggested that the privilege be withdrawn.

The Chair asked the Indonesian delegate to explain what happened after the KKPU issued the recommendation to liberalise prices.

The Indonesian delegate explained that the government of Indonesia was about to put the relevant clause in Indonesia competition laws. The KPPU also suggested cancelling a government policy accommodating synergies between state-owned companies. This suggestion is being considered by the president. More generally, many cases are being brought to the KPPU's attention and there is much room in Indonesia to make the airline industry more competitive.

The Chair explained that before moving to the next topic, Austria would present their experience with liberalisation and the impact it has had on competition dynamics.

The delegate from **Austria** explained that with liberalisation, competition and demand increased while fares decreased. Life became more difficult for airlines, which started entering into mergers and alliances. In Austria, the most important merger took place in 2009 and involved national carrier Austrian Airlines and Lufthansa, followed by a merger of the two most important low cost carriers, Air Berlin and Fly Niki, in 2010. The decline in ticket prices also affected travel agencies as airlines reduced or eliminated commissions raising the question as to whether this was in line with competition law. Liberalisation also affected airports: Some cases involved non-discrimination issues between low cost and full service carriers. Liberalisation therefore changed the whole industry, not just competition.

The Austrian delegate then discussed competition-related issues that the competition authority is currently dealing with. This includes monitoring prices, notably on the Vienna-Brussels route. In 2013 a new provision was introduced in the Austrian Cartel Act enabling the authority to continuously monitor industries and products. The authority does not have investigative powers in this field and must therefore rely on public data.

The Austrian delegate also raised the need for a level playing field, which has become more apparent with liberalisation. The Austrian competition authority was consulted regarding the introduction of the 'fair competition' clause in bilateral agreements. The issue arose due to airlines, notably Emirates, receiving state aid. The aim of the 'fair competition' clause was to introduce a mechanism to suspend landing rights when there was a suspicion of unfair competition. It was a difficult clause to draft and an even more

difficult one to negotiate. It would seem that there are discussions at the European level to formulate a model for such a clause.

The Chair indicated that issues of international co-operation and competition between subsidised and non-subsidised airlines would be addressed in more depth later in the discussion.

2. Factors affecting airline competition

The Chair introduced the second part of the discussion by highlighting that airline competition could be affected by both structural and behavioural factors or obstacles, as revealed by a number of country contributions.

2.1 Structural factors affecting competition

The Chair observed that a number of contributions pointed to structural barriers, in particular congested airports and slot allocation issues. For example, in Japan, a mechanism promoting new comers was initiated by the transport authority; while in Korea, the KFTC suggested measures to make the slot allocation system more competitive. To start the discussion, the Chair gave the floor to Japan.

The delegate from **Japan** started his presentation with a brief overview of the de-regulation process in Japan and its effects. Until 1990 when the de-regulation of the sector started, the airline industry in Japan used to be heavily regulated, with three airlines segmenting markets among them. Since then, various steps were taken and in 1998, two new airlines entered the market for the first time in 35 years.

The Japanese delegate also discussed one of the biggest barriers to entry in the industry: landing slots at Haneda Airport. Because of the important concentration of people and business activity in Tokyo, routes between Tokyo and other major cities are the most profitable. As a result, there is strong excess in demand for slots at Haneda airport. Slots are controlled by the Ministry of Land, Infrastructure, Transports and Tourism (MLIT) which tended to favour incumbents, creating barriers to entry. Following de-regulation, the MLIT wished to promote entry and started giving preferential treatment to new entrants in the allocation of slots at Haneda airport. This helped entrants obtain slots and enter profitable markets. In 2001, two of the incumbents, JAL and JAS, merged. In response to the concerns expressed by the JFTC, the merging parties offered remedies including returning slots to the MLIT. The MLIT promised, on that occasion, to re-allocate these slots so as to promote competition by allowing latecomer air carriers to use them. As a result of these measures, the JFTC approved the merger.

The Chair turned to Korea where the KFTC also tried to improve the slot allocation system.

The delegate from **Korea** explained the recommendations made by the KFTC to the presidential council regarding entry de-regulation. The KFTC's efforts to render the domestic airline industry more competitive were two-fold: taking measures against anti-competitive business practices and de-regulation. The delegate concentrated on the de-regulation aspects. Price and entry regulations had been continuously eased since the 1990s. Yet this had not been sufficient to enable low cost carriers to compete with existing major airlines. In 2010, the KFTC submitted a report suggesting entry de-regulation. Its first suggestion related to aircraft slot adjustment. Slots are allocated in accordance with criteria developed by the Korean slot schedule committee. At the time of the proposal only two airlines were allowed to participate in this committee, which led to slot adjustments unfavourable to low cost carriers. The KFTC proposed to enable new companies, including low cost carriers, to participate in this committee. The second suggestion concerned the strategic slot policy. This policy aims to generate better performance by retrieving slots from airlines and re-allocating them to new airlines. This policy was only in force at Incheon International airport. The KFTC suggested extending the policy to Jeju and Kimpo airports. The third suggestion related

to the registration criteria for small size airlines. All three proposals were accepted by the presidential council.

The Chair thanked the Korean delegate for this interesting report regarding the capacity of a competition authority to positively influence slot allocation processes. To contrast this view, the Chair gave the floor to Iceland, whose contribution suggested that efforts by the competition authority to influence this process had not been very successful.

The delegate from **Iceland** acknowledged that the authority had been facing difficulties regarding the allocation of slots. Slot issues can be explained by the geographical situation of the country. Iceland is quite small and is in the middle of an air route between Europe and North America. This makes it desirable for airlines to operate passenger flights to and from Iceland using the same aircraft for flights between the two continents within the same day. To enable this, airlines must be allocated suitable time slots. There is only one international airport in Iceland: Keflavik airport, which is a co-ordinated airport with grandfather rights. Over 90% of the most important slots at peak hours have been allocated to Iceland Air, the incumbent and dominant carrier in Iceland. Despite numerous applications by new competitors, they were not allocated the necessary time slots. Iceland Air has priority in the allocation of pre-existing slots but also in the allocation of new slots, which is the main problem. From explanations given by the slot co-ordinator, there seems to be a lack of understanding of the importance of competition in this matter. Iceland's competition authority views the arrangement of slot allocation as detrimental; it therefore advised the aviation authority to review this arrangement (especially the categorisation of Keflavik airport as a co-ordinated airport) in 2008, 2009 and 2011. More recently, a similar request was made to review existing regulations to ensure that competition issues are considered when allocating slots. The case is currently before the court.

2.2 Behavioural factors affecting competition

The Chair then turned to behavioural factors affecting competition, two of which were selected for purposes of this roundtable: loyalty programmes and certain pricing techniques.

2.2.1 Loyalty

The Chair gave the floor to New Zealand and asked why the court and the authority disagree on whether a loyalty programme could create a barrier to entry.

The delegate from **New Zealand** explained that the decision made by the court on this issue resulted from a strict adherence to market definition, whereas the Competition Commission did not distinguished between markets for leisure customers and business customers. When the discussion came to the question of barriers to entry, the Commission argued that for business passengers loyalty programmes may constitute a barrier to entry. In contrast, the Court found that loyalty programmes were not a barrier to enter the market for airline services more generally. The delegate noted, however, that is case dated back to 2003 and was fact specific, so it would unlikely bind future decisions.

The Chair turned to Peru where frequent flyer programmes were found not to significantly decrease competition on domestic routes.

The delegate from **Peru** pointed out that barriers to entry were relevant in domestic markets. Several studies showed that frequent flyer programmes could hinder competition: they induce differentiated prices, create switching costs and induce costs for potential entrants. Yet, when airlines representatives were interviewed during a market consultation, they explained that with regards to domestic flights, the impact of frequent flyer programmes was limited, because miles accumulated on domestic flights had little effect on the ability to obtain a reward.

The Chair recalled that the danger of frequent flyer programmes was raised by Prof. Borenstein in his initial presentation, notably on the important distinction between corporate discount programmes and regular frequent flyer programmes.

According to **Prof. Borenstein** sophistication of loyalty programmes has changed substantially over time. In the 1980s and 1990s frequent flyer programmes were not as aggressively used as an exclusionary tool (as they are today).

2.2.2 Pricing techniques

The Chair noted from the country contributions that there seems to be a fair amount of price discrimination in the airline industry. The Chair asked Mr. Pearce to offer his views, particularly on the link between price discrimination and market power.

Mr. Pearce acknowledged that price discrimination could normally be a sign that market power is being exploited. Yet, two cost-related features of the airline economics can explain price discrimination. First, about 50% or more costs in the airline industry are joint or common costs. With competition driving prices down, it is difficult to cover these costs. Second, while there is a clear incentive to go for larger size aircrafts and low frequencies due to economies of scale, passengers, especially business ones, tend to have a strong preference for frequency. In a market where entry is free, this should result in a multi-tier fare structure to cover costs. Mr. Pearce therefore concluded that price discrimination was not necessarily reflective of market power.

According to Mr. Pearce, the emergence of ancillary costs can be explained along the same lines. Following de-regulation, the mechanisms enabling a multi-tier fare structure disappeared. Low cost carriers entered and conditions such as "Saturday night stop over" disappeared. This may have pushed the industry down. Un-bundling and selling ancillary services may have emerged as a response to this, since there is willingness from customers to pay for added benefits. Price segmentation has therefore been led by preferences or the economics of the industry, which in principle can lead to an economically efficient outcome. It has become a means to cover all of the costs. This must be understood in light of the little evidence of economic profits being made in the industry.

Prof. Borenstein disagreed with most of Mr Pearce's explanations, but he agreed with the policy response: this is standard price discrimination and it does reflect some degree of market power. Yet, the airline industry is never going to be an industry without market power. Bundling was initially a response to regulation and quality of service competition. Unbundling therefore seemed quite natural. The issue is whether firms are doing this in an efficient way. Is competition forcing them to be efficient? Losses may not necessarily be a sign of competition.

The Chair linked this discussion to the issue of drip pricing, which is partially linked to unbundling but also to the way prices are presented to consumers. Both the UK and Australia contributed to this question.

The delegate from the **UK** explained that both drip pricing and partitioned pricing can raise similar issues for customers, including search and purchasing errors: had customers had the information required at the right moment in the purchasing process, they may have acted differently. Drip pricing may therefore lead to consumer harm. The starting point to deal with these pricing techniques is consumer protection law. In the UK, there is the unfair trading regulation and the air service regulation. The ideal solution would be to have prices shown up-front in a menu-like way with all compulsory and non-compulsory price components listed. In the UK, the pricing regulator (the Civil Aviation Authority) publishes a comparison of charges compulsorily included in prices. This has been helpful in enabling fare comparison. The CMA's

contribution identifies various factors to take into account when considering enforcement action against airlines' pricing techniques.

The delegate from **Australia** emphasised their main concern: consumers get attracted by headline prices while discovering as they progress through the booking process that the price is much higher than expected, including additional mandatory and optional elements, with some 'options' pre-selected. Australia has also used consumer laws to address the problem. A particular provision provides that if a firm advertises only part of the price, then it must also advertise the single minimum price. In its contribution, Australia described action taken under this provision. Very recently a case regarding headline prices that did not include a booking fee was also filed against Jet Star and Virgin, under the misleading and deceptive conduct provision contained in consumer law.

3. Competition issues in the airline industry and anti-trust enforcement

3.1 Market definition

The Chair explained that the first issue to be discussed regarding anti-trust enforcement in the airline sector, is one on which agreement is rare, namely market definition. Some contributions suggest that relevant markets should be defined based on origin and destination, some believe a distinction should be drawn between scheduled flights and chartered flights, whereas others think that this distinction is blurring and finally there is New Zealand who tends not to concentrate heavily on defining markets at all. BIAC expressed concerns with regards to the confusion that disparities in market definitions are creating. The Chair asked Australia first to present its two-tier approach to market definition.

The delegate from **Australia** explained that the Australian competition authority uses a purposive market definition: market definition is a tool rather than an end in itself. This requires the identification of substitution constraints relevant to the conduct under consideration. In relation to airlines, this involves consideration of both route-specific and network effects. This approach is relevant for normal competition analysis as well as for the specific authorisation regime (for consideration of both benefits and detriments) to exempt conducts such as alliances. Just last year, the authority examined an alliance between two airlines with both route specific effects and network effects on trans-Tasman routes. Benefits and detriments were analysed at both levels.

The Chair asked Prof. Borenstein why he seemed to have suggested that network effects were not that important in the airline industry.

Prof. Borenstein clarified that network effects are important, notably on the cost side, but there is no reason why airlines should do network-wide bundling to get that advantage. On the loyalty side, network effects are definitely important but mostly for anti-competitive reasons.

The Chair invited New Zeeland to explain why in its view too much emphasis should not be put on market definition.

The delegate from **New Zealand** explained that they have only recently dismissed the primacy of market definition and revised their merger guidelines, to focus more on the closeness of competition.

Following New Zealand's brief explanation the Chair turned to BIAC.

The delegate from **BIAC** explained that confusion concerning market definition can be evidenced by merger cases. When Delta/Northwest, United/Continental and Southwest/Air Tran mergers were reviewed in the US, the position was that low cost carriers should be included in the relevant markets for scheduled passenger flights and that one-stop routes and non-stop routes should be treated as being in different

markets. In the American Airlines/US Airways merger, the low cost carriers were excluded from the relevant markets, whereas non-stop routes and one-stop routes were considered to be in the same market. At the same time, the European Commission took an origin and destination approach in the Delta/Northwest, United/Continental and American Airlines/US Airways mergers. Inconsistencies are an important issue, especially in the airline industry where mergers are rare, whereas alliances and code-sharing agreements are more common. While some of the airline alliances and agreements require formal approval, as in the United States, in many jurisdictions such agreements are left to self-assessment. Self-assessment is highly dependent on how markets are defined and airlines sometimes may find it confusing. This stems from a lack of real guidance and from standards that can prove quite difficult to adapt in the context of a code-sharing agreement or an alliance. Differences among competition agencies' approaches make this assessment process all the more complicated. More uniformed guidance on the part of the competition authorities could prove helpful in preventing anti-competitive horizontal agreements.

Prof. Borenstein disagreed with BIAC's intervention by saying that the last thing authorities should be doing is giving this kind of guidance. Market definition is a rigid concept for a very fluid competitive setting. Firms are constantly innovating. It would be wrong to define a rigid standard to abide by. The United States took a major step forward with the 2010 merger guidelines in recognising that market definition is often more of an impediment to understanding a market. Prof. Borenstein was pleased to hear that New Zealand was moving in the same direction. According to him, what really matters is actual competition, the elasticity of demand a firm faces and the ability to raise prices above competitive levels.

The delegate from **BIAC** reacted by stating that, in their view, more guidance is better than no guidance. They support a system of universal compliance rather than one where companies are encouraged to take risks, letting the enforcers sort things out.

The Chair observed that business models in the airline industry change quite often. This evolution can make the principles on which market definition is based a bit more unstable, but should not prevent authorities from providing some guidance.

3.2 Airline merger control

The Chair underlined that airlines could do business together through different means: through mergers, but also more often through alliances. From the contributions, it appeared that depending on the country and on the type or level of airline co-operation, the competition assessment may differ. The Chair proposed to start with a discussion of the classical merger case: the LAN/TAM merger, and invited the delegates to discuss how industry specificities were taken into account in competition assessment.

3.2.1 Airline mergers and acquisitions (majority or full)

The delegate from **Chile** explained that in January 2011 a Chilean consumer association filed an inquiry before the Competition Tribunal about the LAN/TAM merger. The merger was subsequently approved by the Competition Tribunal and confirmed by the Chile's Supreme Court, the Constitutional Court as well as by the Brazilian anti-trust authority. LAN is the largest airline in Chile, whereas TAM is one of the most important Brazilian airlines and almost the only one flying to Chile. In assessing the merger, the Competition Tribunal studied: i) competition among airlines in South America, ii) overlapping passenger routes, iii) non-overlapping passenger routes and iv) the market for international air cargo. The Tribunal took industry specificities into account in the definition of relevant markets, in analysing barriers to entry and in designing remedies. Network effects, economies of density, frequent flyer programmes, alliances and hubs all had an impact on market definition. Regarding barriers to entry, entry and exit points to and from South America were taken into account. As a result, one of the remedies required the release of slots at major airports. Code-sharing agreements were also perceived as a potential barrier. The Tribunal

demanded that LAN and TAM extend their frequent flyer programmes to other airlines and that they enter into inter-lining agreements with other airlines on certain routes. LAN and TAM were also asked to resign from at least one of the global alliances they belonged to. In the end the merger was approved but subject to extensive structural and behavioural remedies because of the industry specificities.

The Chair asked the Chilean delegate about the different opinions expressed by the judges of the Competition Tribunal on this matter.

The delegate from **Chile** explained that one judge concurred in the approval but rejected two remedies because, in his view, they were not connected to the effects of the operation or were not discussed during the merger process. Another judge rejected the merger because he considered that the concentration of LAN with its closest South American competitor would offer the merged entity too much market power.

The Chair turned to Australia which examined failing firm defences. In one merger case the defence was accepted. In another, which was not a merger, it was not. The Chair asked Australia about the diverging outcomes on the failing firm defence in the two cases.

The delegate from **Australia** specified that the two matters referred to by the Chair are the Qantas/Emirates alliance and the Virgin/Tiger acquisition. In the alliance case, the defence was refused but the alliance was conditionally authorised due to efficiency benefits. In the Virgin/Tiger case, even though Australia does not have a formal failing firm defence, the fact that Tiger was facing financial difficulties had an important impact on the analysis. The Australian delegate provided further background to better understanding the Virgin/Tiger case. Initially, Australia had a regulated industry and only two main airlines, Ansett and Qantas. Virgin, a low cost carrier, entered in 2000 and became the second airline after Ansett failed. After acquiring Impulse Airlines, Qantas launched Jetstar as a low cost carrier, adopting a dual FSC-LCC model. Virgin subsequently began a "game change" strategy to become a FSC and Tiger, a subsidiary of the Singaporean airline, entered in 2007 as a low cost carrier. Tiger never made any operating profit; it incurred substantial losses and was suspended by the aviation safety regulator from flying for a few months in 2011. In 2012, Virgin applied to acquire 60% of Tiger. The acquisition was important as it would leave the domestic industry with only two airlines, both with a dual full service and low cost strategy. This raised unilateral and co-ordinated effects concerns. The real question, however, was whether Target could stay in the market absent Virgin's acquisition. The answer was that absent the acquisition, Tiger's planes would be relocated to other parts of Tiger's operations in Asia. As a result the merger was cleared on failing firm grounds.

3.2.2 Mergers across business models

The Chair introduced the second topic regarding mergers and asked the UK to discuss the impact of differences in business models on the assessment of mergers in light of the *Ryan Air/Aer Lingus* minority acquisition case.

The delegate from the **UK** explained that although Ryanair and Aer Lingus are not at opposite ends of the business model spectrum, they do differ: Ryanair is a low cost carrier, whereas Aer Lingus is as a value carrier, serving more central airports, operating both short- and long-haul flights. The merger analysis was carried out on an origin-destination pairing basis. On most routes, these airlines were the only two in operation. Both airlines carried similar types of passengers, monitored each other's behaviour and targeted each other in their respective marketing materials. The authority concluded that both airlines competed head to head. The difference in business model did not have a substantial impact on the analysis.

3.2.3 Remedies

Remedies are another important issue with respect to mergers, especially in the airline industry. The Chair invited the United States to discuss the *American Airlines/US Airways* merger. In particular, the Chair asked why the merger was not blocked if the US, as per their contribution, considered that the settlement did not and could not remedy the specific harm arising from the merger.

The delegate from the **US** emphasised the fact that, as explained in the US paper, it was literally impossible to precisely remedy the specific harm alleged in the complaint. Due to the nature of airlines networks, it was not possible to divest route to replace existing competition between the merging parties. Behavioural remedies, while theoretically possible, would be extremely burdensome and difficult to monitor. Under US law, it is not necessary that the remedy precisely replicate the form of the competition that would have been lost. The divestiture of significant assets at key airports to low cost carriers would result in the expansion of low cost carrier competition and in the delivery of substantial consumer benefits. These benefits compared favourably and could, in some ways, exceed the pro-competitive benefits that would have come from preserving competition between the two airlines.

Reacting to the delegate's answer, the Chair asked why the merger was not simply blocked in the first place, especially given that some expert commentators were supportive of this.

The US delegate reiterated that, in some ways, the remedies would enable for more competition than under the status quo. Had they not been comfortable with the benefits of the remedies, they would have been prepared to go to trial.

The Chair pursued the discussion on remedies by introducing the notion of carve-outs and highlighting a potential difference between Australia and Canada in the use of such a remedy in the airline sector. The Australian contribution suggested that while carve-outs may resolve competition concerns, they could also block the realisation of public benefits. Canada, on the other hand, recently imposed carve-outs in the *United/Air Canada* case. The Chair invited both delegations to present their analysis.

The delegate from **Canada** explained that *United/Air Canada* was a joint venture assessed as a merger, i.e. under merger control. The joint venture involved co-ordination and co-operation on pricing and capacity, frequent flyer programmes as well as revenue and cost sharing on US-Canada cross-border routes. The Canadian authority also reviewed three pre-existing agreements under provisions relating to competitors' collaboration. The review revealed that there was going to be a substantial lessening or prevention of competition on 19 routes. As the case was heading for trial, a settlement was reached, including carving out fourteen of these routes. As a result, the joint venture and the existing agreements could not be effective on these 14 routes. The consent agreement provided that, in case of a substantial change in the competitive landscape of any of these routes, a prohibition could be suspended or re-instated.

The Chair highlighted that another interesting aspect of this case is that the joint venture was assessed as a merger. He then turned to Australia to understand their position on carve-outs.

The delegate from **Australia** explained that they do not have a rigid position on carve-outs and discussed the cases that the Chair was referring to. These cases concerned airline alliances. In both cases, rather than imposing carve-outs, the alliance was accepted and conditions were imposed requiring them to maintain certain capacity levels on the concerned routes.

The Chair turned to the experts to nourish the debate.

According to **Prof. Borenstein**, carve-outs are often reflective of the fact that authorities concentrate on specific routes and concerns when reviewing mergers. Such an approach often lacks understanding of

the dynamic evolution and changes of the industry and how they can be affected by network mergers. Carve-outs address narrowly defined concerns while leaving open the broader evolution of the industry.

Turning to Mexico, the Chair explained that the *AeroMexico/Mexicana* merger was blocked due to insufficient remedies. He asked Mexico about the reasoning behind their decision.

The delegate from **Mexico** explained that in 2007 the authority rejected the merger for the second time. Some of the concerns identified pertained to slot allocations creating barriers to entry and the saturation degree of Mexico City airport. The remedies offered by Mexicana were rejected because they did not comprise any slot-related remedies and hence did not guarantee the entry of new competitors.

The Chair gave the floor to Prof. Borenstein who wished to comment.

Prof. Borenstein mentioned the *AeroMexico/Mexicana* and the *Air Canada/Canadian* cases. In both cases there was an issue of failing firm and nobody thought that there would be much competition left. In the most recent US mergers, the authority believed that markets would remain competitive. While Prof. Borenstein understood the US DOJ's decision, he pointed however to the difficulties involved in assessing the benefits for consumers.

New Zealand asked Canada if there was a concern for co-ordinated behaviour in the *United/Air Canada* case given that the joint venture was still in place on a number of routes.

Canada explained that, with the pre-existing agreements, there was already careful consideration for the exchange of confidential information. With the settlement, it is also possible to put monitoring in place to ensure that there is no exchange of confidential information.

3.3 Horizontal agreements

The Chair introduced the next part of the discussion, namely horizontal agreements between airlines: what do such agreements consist in and how are they assessed when they do not amount to mergers falling under merger control? The Chair turned to Mr. Pearce.

Mr. Pearce explained that although there are limited economies of scale in firm size, there is evidence for economies of density in the airline industry. In fact, business models can be understood as ways to generate traffic density. Low cost carriers use price to stimulate the leisure flow. Full service carriers use the hub-and-spoke model to concentrate flows of passengers. Because of the low density of traffic on many direct routes, Mr. Pearce believes that this second model will play an important role despite technological changes enabling airlines to fly more direct services on thinner routes. In conjunction with air service agreement restrictions, these industry specificities explain the movement towards alliances. More than other types of alliances, metal-neutral joint ventures can enable firms to generate sufficient flows of traffic and enable airlines to fly bigger aircrafts.

The Chair turned to Mr. Balfour asking whether mergers and alliances were assessed in a similar fashion.

Mr. Balfour outlined the differences between the Commission's assessment of mergers and of alliances. Regarding the competition assessment, the approach is essentially the same. The Commission might however be more rigorous when assessing a merger rather than an alliance. Regarding remedies, the approach is also quite similar. In both cases the most common remedy has been the release of slots accompanied by measures to ease entry. Equally questionable in both situations is the effectiveness of these remedies and whether they result in long term benefits. One difference is found in the outcomes: all alliances have been approved, whereas three airline merger cases led to the merger prohibition. Regarding

the procedure, the differences are more important. Mergers require a notification, the advantage of which is that it results is a definite long term decision. With alliances, since 2004, the procedure functions under self-assessment, which causes uncertainty. Timetables are also different: merger decisions take months, whereas alliance decisions can take years. This difference also creates further uncertainty.

Prof. Mendes de Leon reacted to Mr. Balfour's presentation by highlighting that one of the reasons for the approval of all these mergers may have been the will to promote European airlines in global markets. For example, *RyanAir/Aer Lingus* and *Aegean Airlines/Olympic Air* merger cases were smaller cases without a truly global dimension.

The Chair turned to the EU delegation regarding the characterisation of the differences between mergers and alliances and the EU's view on the uncertainties that the alliance regime may create.

The delegate from the **EU** confirmed that the differences and similarities between mergers and article 101 TFEU anti-trust assessments are mainly those highlighted by Mr. Balfour. The delegate suggested that for example, the *RyanAir/Aer Lingus* and *Aegean Airlines/Olympic Air* matters would still have led to a similar outcome had they been treated under the anti-trust rules and not the merger provisions.

The EU delegate then walked other delegates and the Chair through the process of analysing alliances. An alliance often takes the form of a joint venture, which, under EU law will be assessed either as a merger if it is a full function joint venture or under article 101 TFEU if it is not. Under article 101 the Commission would look at the parameters of co-operation and would concentrate on factors such as combined market shares, barriers to entry and the closeness of competition. The assessment would be carried out with regards to individual routes. Another important aspect of the Commission's practice relates to the assessment of efficiencies under article 101(3) TFEU. Efficiencies must be well demonstrated and must outweigh the negative effects of the alliance. The Commission notably takes into consideration better scheduling, economies of density and reduced double marginalisation.

Mr. Balfour stated that he agreed with the EU delegate's intervention.

To contrast the EU system, the Chair called on Israel, where there is a different spectrum of enforcement tools, combining e.g. an authorisation procedure, a block exemption and residuary cartel enforcement. This system may provide for more predictability and security. The Chair asked Israel's delegate to explain how the various tools function together.

The delegate from **Israel** explained that the system was changed several times. Currently there is i) an authorisation requirement, ii) a self-assessment block exemption for code-sharing agreements between Israeli companies and other airlines in cases where an open skies agreement applies, and iii) several block exemptions for particular types of agreements. This methodology was developed through the review of code-sharing agreements submitted by El Al. The methodology consisted in collecting extensive data, to create a competitive benchmark regarding price per kilometre, per seat or per passenger on routes similar to the one being assessed. This enabled comparison between concentrated routes and non-concentrated routes. It was notably applied to a seat swap agreement between El Al and Swiss.

The Chair then turned to Turkey to hear about two alliances mentioned in their contribution: one between Turkish Airlines, El Al, Egypt Air and Royal Jordanian Airline, the other between Air France, KLM, Northwest and Delta Airlines. What were the methodology and procedural context?

The delegate from **Turkey** noted first that the Turkish Competition Authority did not carry out a specific assessment for the Turkish Airlines and Star Alliance co-operation because it was not regarded as a threat to competition. Regarding the two alliances mentioned by the Chair, they were granted an exemption despite anti-competitive effects as they were supposed to lead to consumer benefits. In

particular, the second alliance's benefits included increased frequency of flights, wider networks and more comprehensive frequent flyer programmes. The fact that Turkish Airlines had a higher market share on routes overlapping with the joint venture was also important.

The Chair concluded on the discussions on horizontal agreements by observing that while the treatment of horizontal agreements may be procedurally different, it may not be so different from a substantive point of view. The situation of Israel is interesting as they seem to offer more guidance than other jurisdictions, which may make it more comfortable for airlines to know how they can operate together.

3.4 Unilateral conduct

To launch the discussion on unilateral conduct the Chair pointed to a few jurisdictions that had to address predatory pricing or conduct matters. He first invited Germany to talk about the *Germania* case. The case is interesting because of Lufthansa's pricing strategy and of the remedy imposed.

The delegate from **Germany** explained that this case dated back to 2002. Following Germania's entry on the Berlin-Frankfurt market, Lufthansa had substantially reduced prices exclusively on this route in an attempt to squeeze Germania out of the market. At the time the Bundeskartellamt had prohibited, under specific conditions, Lufthansa from offering a price below an amount corresponding to Germania's price plus 35 euros. This difference took into account services offered by Lufthansa but not offered by Germania. Moreover, should Germania have raised its prices above a defined level of 99 euros, Lufthansa would not have been obliged to raise its prices accordingly. The Higher Regional Court reduced the amount of minimum difference but confirmed the principle. The aim of the decision was to send a clear signal that the authority was decided to protect new entrants. The delegate further pointed to the difficulty to design remedies in unilateral conduct cases and to the specificities of German law.

The Chair asked Germany whether the allegation was that Lufthansa's prices were below some sort of variable costs.

The delegate from **Germany** explained that Lufthansa's price was below its average operating costs per passenger. The test at the time was to determine whether Lufthansa was competing on the merits or was applying a strategy to eliminate a rival and to fight a future entry.

The Chair turned to the US who has had experience of predatory conduct through capacity dumping. He called on the US to share their experience in this case and the characterisation of that kind of predatory conduct.

The delegate from the **US** explained that the case the Chair referred to dated back to early 2000 and involved American Airlines and its hub at Dallas Fort Worth. The division concluded that American had added excess capacity in order to drive a low cost carrier off its route. American knew that such a strategy would be very expensive in the short term. Yet, a successful low cost carrier hub at Dallas Fort Worth would have jeopardised a much larger amount of annual revenues. The division lost at the District Court and on appeal. The Court of Appeal confirmed the District Court's judgement but agreed that predation should not be treated with incredulity. The Court also rejected the District Court's holding that route-wide average variable cost is the only appropriate cost measure. The DOJ considers that this decision could be used as a precedent to argue, at least by inference, that incremental cost analysis is a correct measure in appropriate foreclosure cases and that multi-market recoupment is a viable legal theory.

The delegate from **Germany** informed the roundtable's participants that predatory pricing discussions were held this year by the ICN. The delegate drew attention to a situation briefly discussed in the ICN recommended practices: in certain limited circumstances even a not yet efficient competitor may exert a

competitive constraint. In such circumstances even pricing above certain measures of cost can harm and could be predatory.

To close the discussion on unilateral conduct, the Chair invited the experts to comment.

Mr. Balfour pointed out that there had been almost no investigation into cases of unilateral behaviour by airlines under article 102 TFEU.

Prof. Borenstein believes that the cases discussed point to the difficulty of prosecuting predation cases. Firms should be encouraged to compete aggressively, not be in fear of doing so. Yet courts should also recognise the potential role for prosecution of predation cases. He also re-emphasised that the ultimate anti-competitive impact of loyalty programmes is essentially one of predation, e.g. by threatening businesses of decreasing discounts at the network level.

4. Challenges ahead and evolutions to come

The Chair introduced the last topic which pertains to the absence of a level playing field in the air transport industry. From the contributions, the Chair observed that the playing field could be un-levelled in three ways: through direct state intervention, indirect acts of a regulatory nature and international confrontation of carriers and countries obeying different rules. Time permitting, delegations would be asked to share their views or experience with direct and indirect state intervention.

4.1 Direct state intervention

The Chair first turned to Japan which has recently bailed-out Japan Airlines (JAL) and had to consider some complicated trade-offs. The Chair asked Japan to address the way the decision was made and how negative impacts were dealt with.

The delegate from **Japan** listed the reasons behind JAL's financial difficulties. These included its business structure inflexibility such as excessive ownership of large aircraft and maintenance of unprofitable routes, organizational inflexibility that led to delays in decision making and the 2008 financial crisis. As a result JAL made a request to ETIC (a state-authorised corporation providing business revitalisation support) for revitalisation and filed an application to the court for corporate reorganization proceedings in 2010. The request was accepted by ETIC and the court commenced the corporate reorganization proceedings. The revitalisation process included measures such as financing, debt forgiveness, and preferential tax treatment, which led to an important restructuring of the business and its organisational structure.

While the Japanese delegate explained that the JFTC does not have any power with regard to state aid, he identified two dilemmas in deciding whether to rescue JAL. The first dilemma stands between distorting competition through a bail-out and taking the risk that an important competitor might exit the market and hence render the market more oligopolistic. The second one concerns the relationship between competition policies and other policies. (For further detail, the Japanese delegate referred to the presentation given at the WP2 meeting in February 2014 on JAL restructuring process and its impact.)

The Chair transitioned from Japan's intervention by highlighting how the impossibility of the JFTC to intervene when the bail-out was considered is reminiscent of the situation in South Africa. South African Airways (SAA) was indeed bailed-out without the authority being able to intervene. At the time of the bail-out, other airlines were facing financial difficulties, too. This begs the question of the decision process regarding money allocation and how it affects the level-playing field.

The delegate from **South Africa** explained that SAA was a state-owned enterprise. The airline received bail-out support in 2008, which immediately made them profitable for about three years, as well as in 2012. In 2012, a competitor, 1time airline, was forced out of the market. Both events put SAA back into profitability. Such a situation raised the question of the role of a competition authority. The South African delegate explained that in South Africa very little can be done in that regard. The authority used to argue that state-owned airlines are pressured to operate non-profitable routes to call for subsidies rather than bail-outs. The authority could also conduct studies and point to specific distortions.

The Chair gave the floor to **Prof. Mendes de Leon**, who noted that the EU was the only jurisdiction regulating state aid. He also observed that, in the EU, some routes were identified as public service obligation routes, enabling airlines to receive subsidies.

To contrast with the intervention by South Africa, the Chair introduced the situation of Malév. Malév was forced by the Commission to redistribute (illegal) state aid received from the Hungarian government, provoking its failure. Malév was soon after replaced in the market by low cost airlines. The Chair invited the EU to comment on Malév and react to Prof. Mendes de Leon's intervention.

The delegate from the **EU** confirmed that the EU is amongst the very few jurisdictions to have state aid rules. The system is based on a general prohibition of state aid with some exceptions, including for failing firms. This exception is subject to various conditions. It requires that the company submit a credible restructuring plan. In doing so, airlines are sometimes inspired by low cost carriers. Companies must also participate to up to 50% of the cost of the bail-out. This compensatory measure is seen as the "price to pay" for the distortion of competition that a subsidy will create. The final condition is that a company cannot receive aid twice within a ten-year period. These rules have been applied several times in the airline industry. Generally aids were prohibited when bankruptcy would not have impacted the connectivity of the area thanks to new entry. This may have been the case in the Malév decision.

The Chair called on Hungary to hear more about the Malév case. He pointed to the fact that the Hungarian contribution says nothing about attempts made by Malév to change its business model. The Chair asked whether there was any structural reason for the airline's financial difficulties and wondered why it did not change its business model to remain profitable?

According to the delegate from **Hungary**, there are three ways to generate more revenues than costs in the airline industry: be big enough like Lufthansa, be efficient enough like Ryan Air or be special enough like Aer Lingus. Malév was none of these three options. In that sense it was not the Commission's decision that made it bankrupt but its own structural difficulties.

The Hungarian delegate highlighted that, following Malév's bankruptcy, other airlines took over Malév's market shares. In 2012, the first year following the bankruptcy and one affected by economic difficulties in Europe, the overall traffic in Hungary and at the airport dropped less than 5%. Since 2012, Wizz Air, the incumbent low cost airline, has increased its capacity by 100%. There is also an on-going study to examine qualitatively and quantitatively the consequences of Malév's disappearance. Generally this case shows how the lack of state intervention can enable the development of the real benefits of market liberalisation.

4.2 Indirect state intervention

To discuss indirect state intervention, the Chair introduced the last two interventions. Egypt would talk about the preferential treatment of Egypt Air, how it affected the playing field and what a competition authority could do about it. Then BIAC would address various issues that affect the level playing field in the industry.

The delegate from **Egypt** explained that Egypt used to have a long history of state intervention. This long history prompted the competition authority to conduct two studies, one on domestic markets and one on regional markets.

The delegate explained that their recent study identified five barriers. The first one pertains to the allocation of traffic rights and route permits, for which a considerable preference is given to Egypt Air, the state-owned flag carrier. The second one is that, in practice, private companies must obtain approval from Egypt Air to fly regional flights from Cairo airport (Egypt's most important airport), which constitutes an unjustified restriction aimed to protect Egypt Air from any competition. This approval obligation could also result from bilateral air service agreements and the fact that Egypt Air takes part in them. The remaining barriers relate to Egypt Air's preferential fuel price and payment conditions, its brand image and its highly skilled workforce.

Following the studies, some recommendations were made. These recommendations included eliminating regulatory barriers as well as the preference given to Egypt Air. The Egyptian delegate highlighted some positive steps towards enhancing competition, including reducing nationality requirements.

The Chair finally gave the floor to BIAC.

The delegate from **BIAC** explained that there were still many flag carriers and state-owned enterprises in the airline, airport and other related facilities sectors. The presence of these companies has an impact on the creation of a level playing field as it often creates a temptation for states to subsidise these airlines. Some subsidies may be perfectly reasonable and justified. But if subsidies are used outside of these limited situations, they may deter entry and can drive airlines out of markets. Regarding Egypt, BIAC's delegate highlighted that they seem to have done a very thorough job and hoped that they would be able to push for these recommendations to be implemented.

The Chair closed the discussion by thanking the delegates, the Secretariat, the experts and all 33 contributors.