



ICAO Global Symposium on Air Transport Liberalization  
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# Air Service Development for Developing Countries

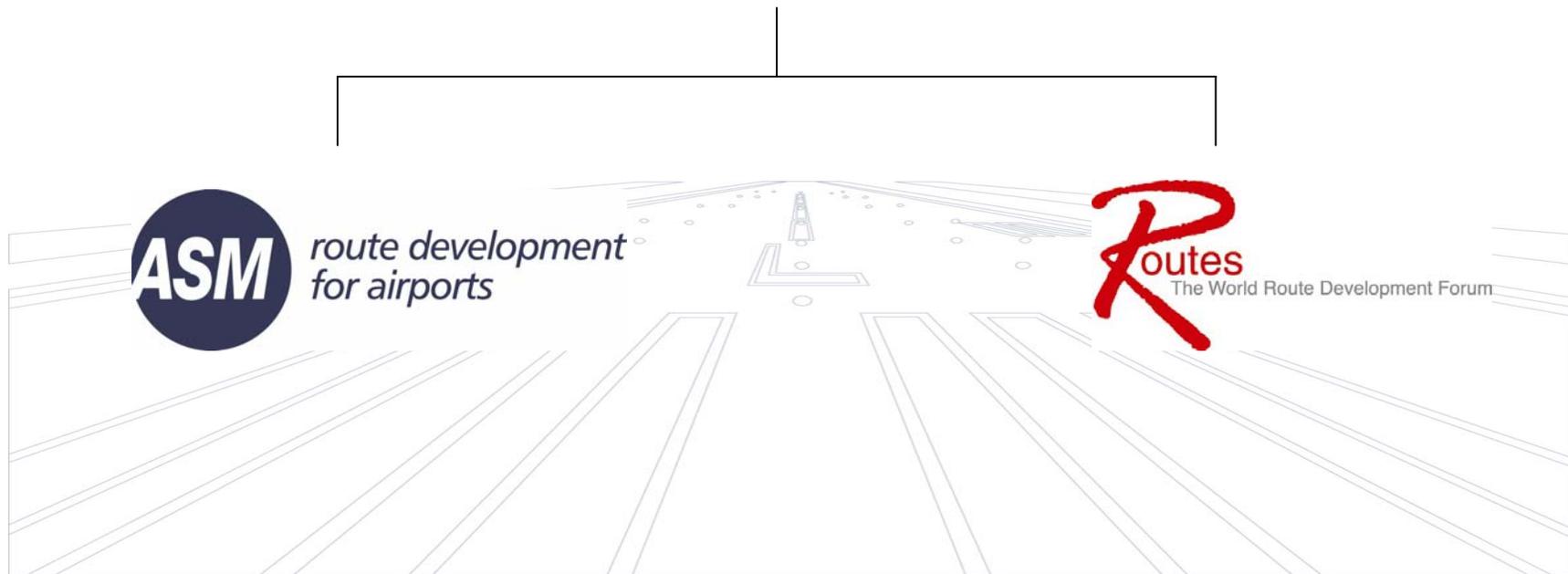


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# Corporate Structure

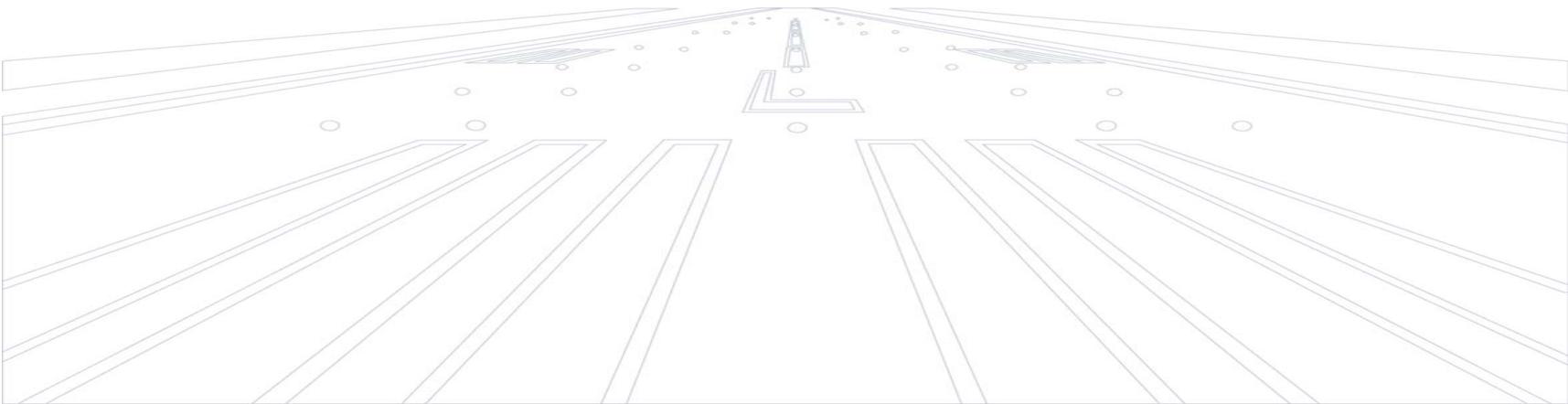


The Route Development Group

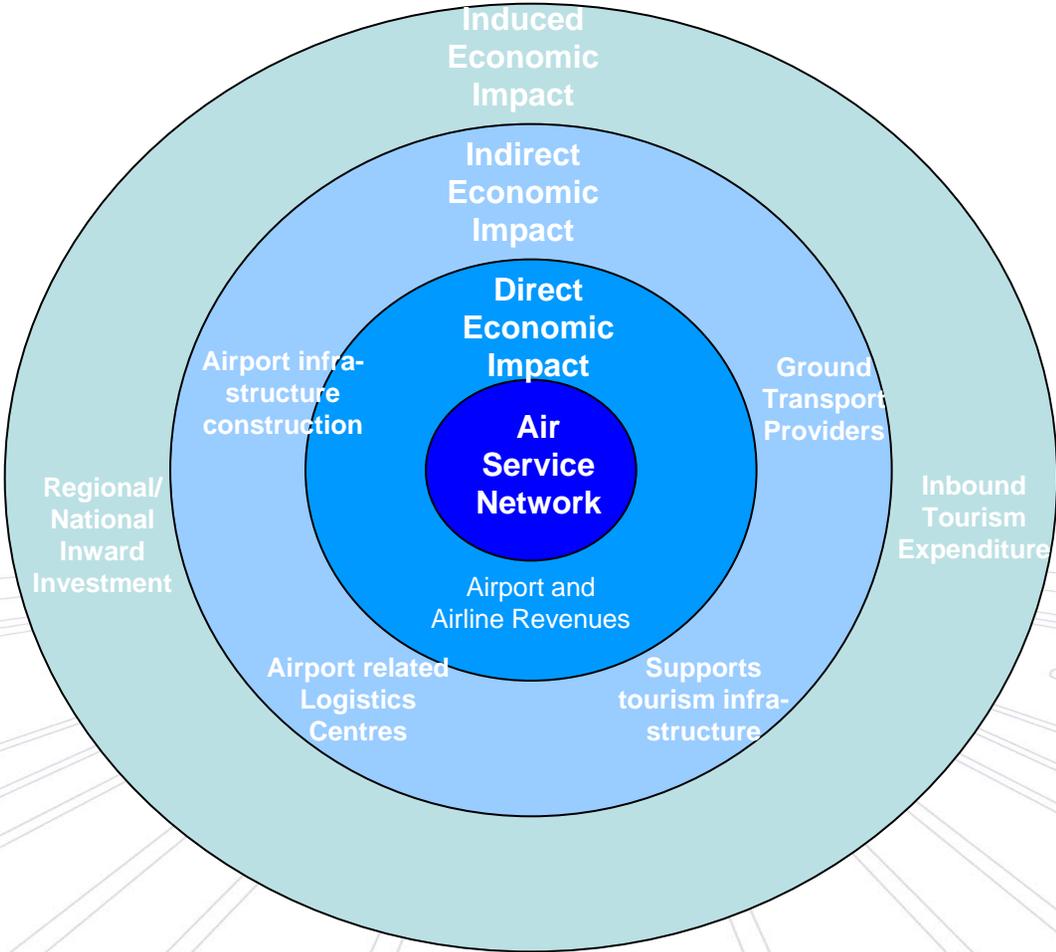


# Why the interest in Air Service Development – or What are 2,000 people doing in the room next door ?

- Who drives Air Service Development ?
- Air Service Development – Getting the Basics Right
- A Practical Initiative – The ICAO/WTO ESTDR initiative



# Air Service and Economic Development



# Air Service Development

## Driven by airlines or other stakeholders?

Previously controlled by airlines, but the “monopoly” on decision-making has changed.

Key drivers are now:

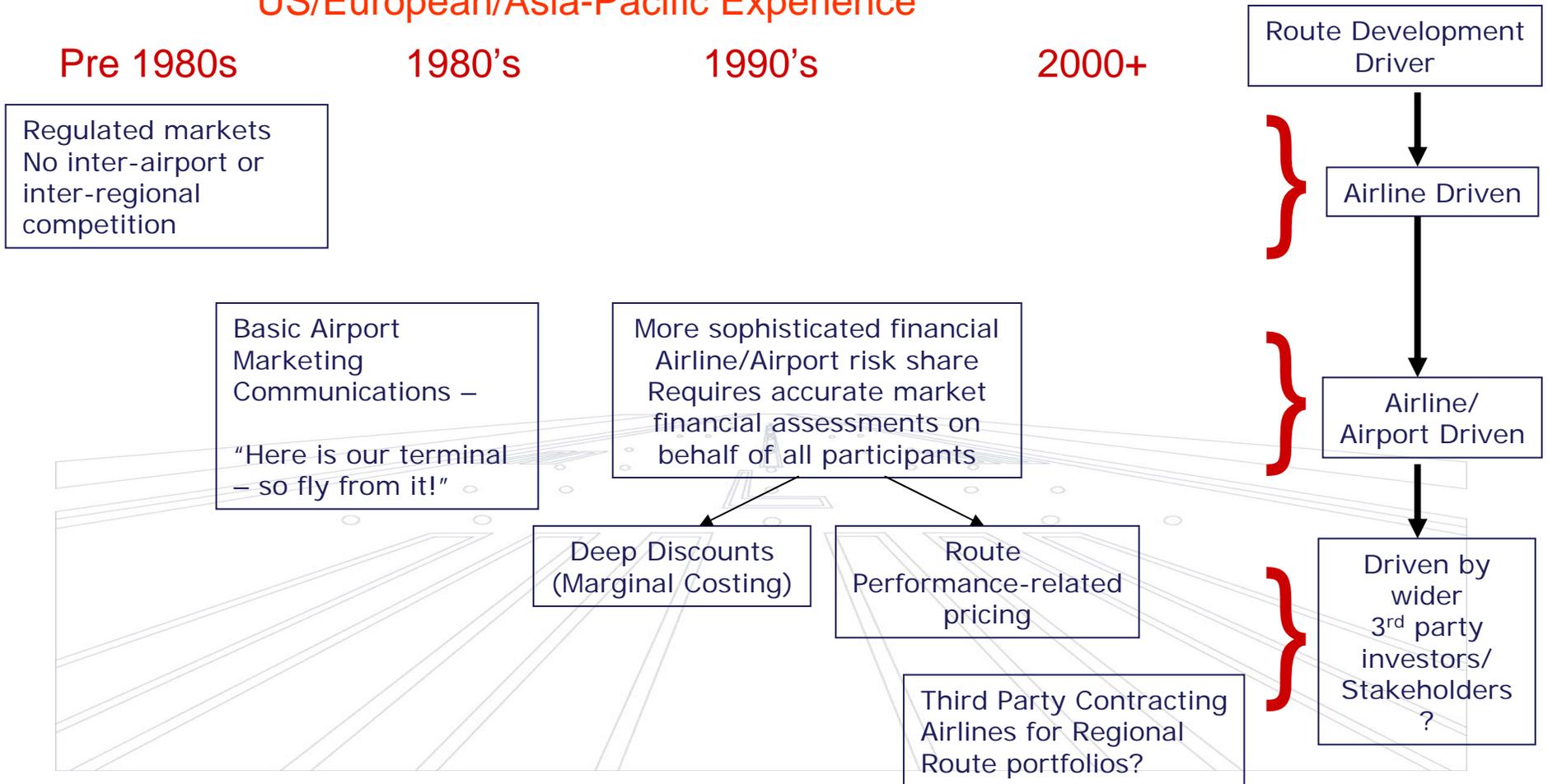
- Wider stakeholder participation
- Airline financial performance and availability of expansion capital
- More aggressive competition between cities/region on an international basis
- Further de-regulation of markets

# Wider Stakeholder Participation – The Axis of 6



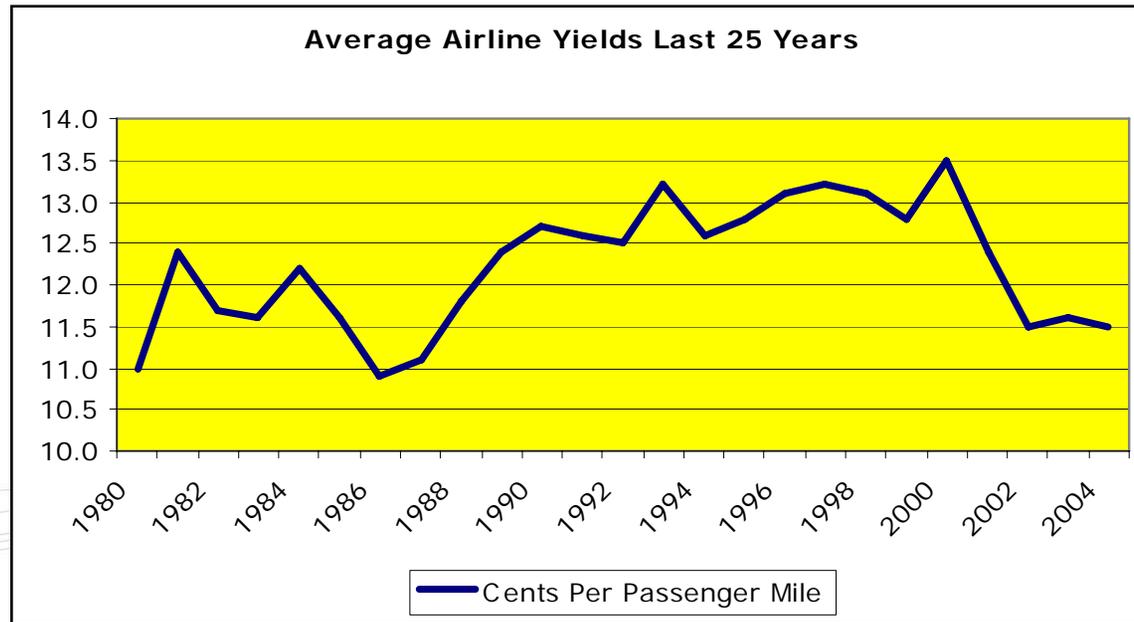
# Route Development – driven by airlines or other stakeholders?

## US/European/Asia-Pacific Experience



# Current Airline Financial Performance is Perilous.....

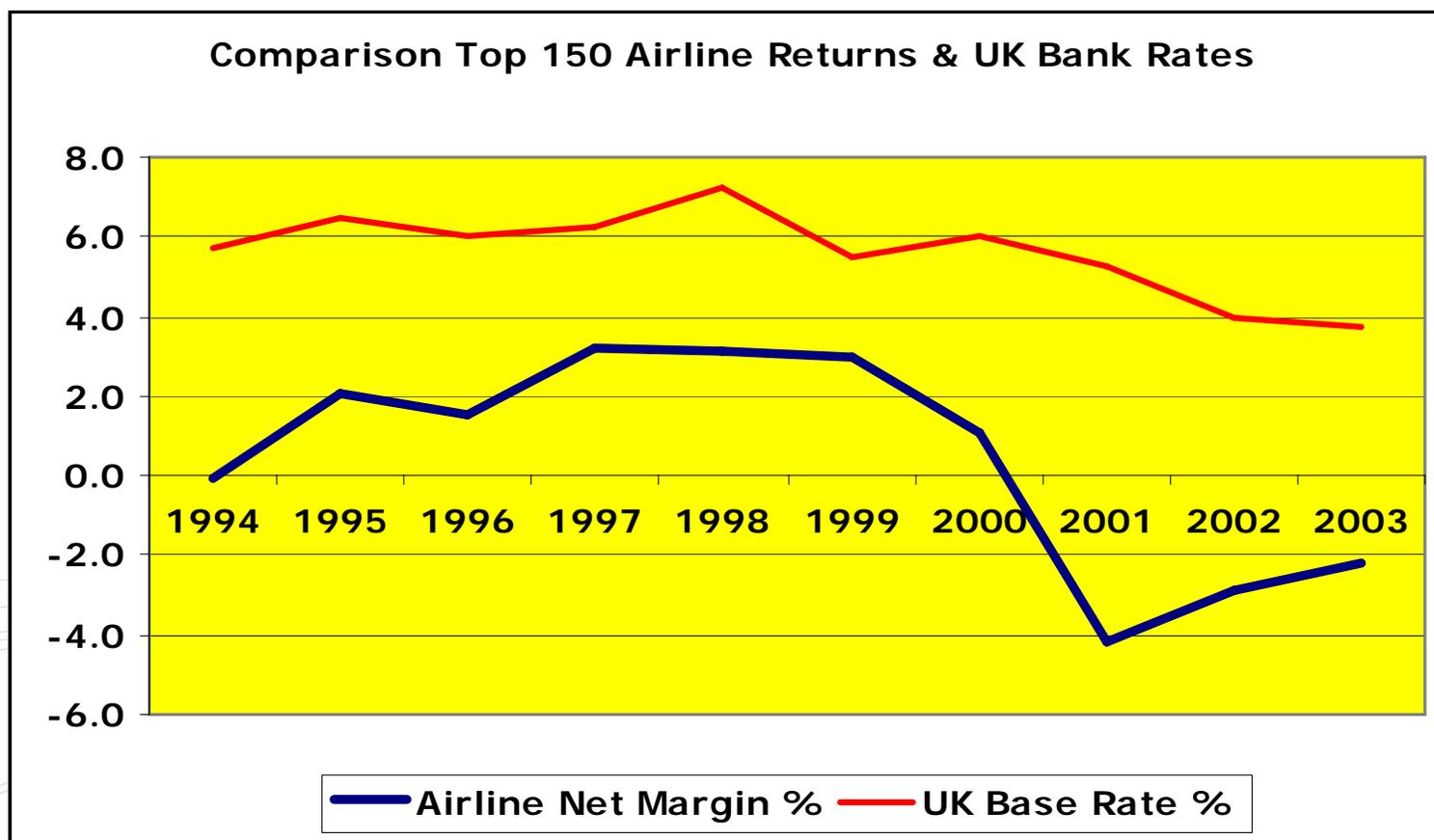
## Average Yields Are Falling...



Average yields per passenger mile are currently at the same levels reported in the 1980's

Source: AeroEcon

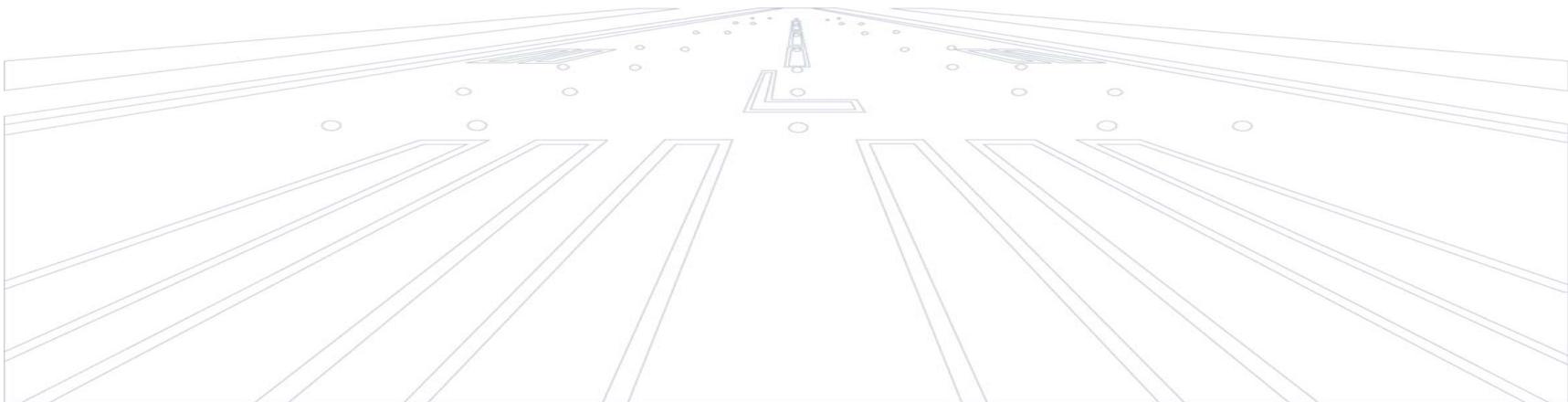
# Historical Airline Financial Performance is Not Much Better.....



UK base interest rates for the last 10 years have provided greater returns than the top 150 airlines

# Aggressive Competition between Cities/Regions

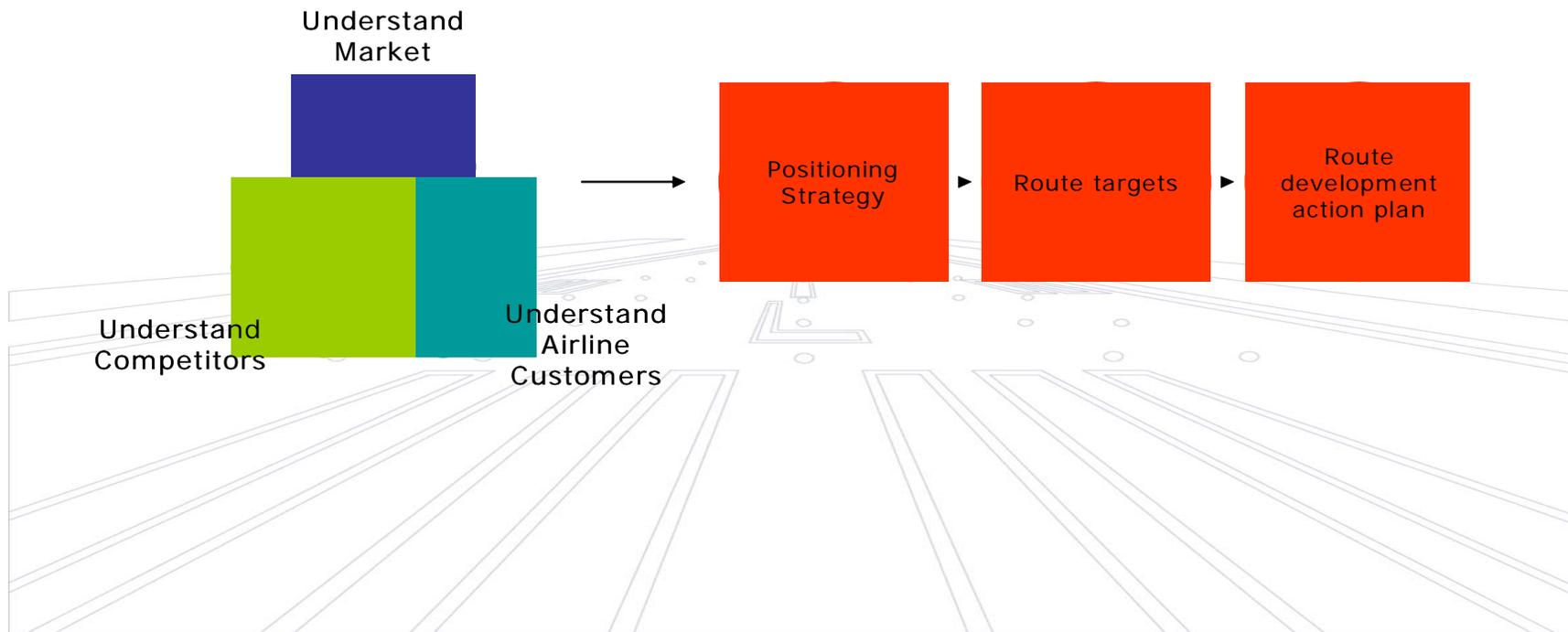
- Airport Privatisations generate an immediate need for shareholder value
- Airports adopting more aggressive marketing approaches
- Tourism seen as key driver of economic growth – particularly in developing countries



# Route Development – Best Practice for Stakeholders

## The Route Development Process

Route development strategy...



# Understanding The Market

## Quantitative

- Market Size
- Market Price Elasticity
- Market Forecast
- Route Financial Viability (including up to date airline operating economics )
- Quantitative Surveys
- Government Statistics
- Specialist data

## Qualitative:

- Existing and Future Trade Links
- Tourism Info.
- Tour Operators/Travel Agents
- Market Intelligence

# Understanding the Market - More Accurate Traffic Assessments



# Understanding the Market – Accurate Passenger Flow Information

- Can be difficult to obtain
- Can be contradictory
- Can be expensive
- But airlines need it to make informed decisions!!
- Data Sources include:
  - MIDT
  - PTM
  - BSP
  - Immigration and Visitor Registration Data
  - Airport Passenger Surveys
  - Government/CAA aviation statistics

# Understanding The Market

Source	+	-
MIDT	Accuracy	Cost Increasing lack of market coverage Complexity of manipulation
BSP	Accuracy	Cost Increasing lack of market coverage "Clouding" of true O&D patterns
PTM data	Accuracy Relatively cheap acquisition cost	Potential contractual difficulty in data acquisition
Passenger Survey Data	Relatively cheap acquisition and processing costs	Less accurate because of reliance on sampling techniques

# Understanding Airlines

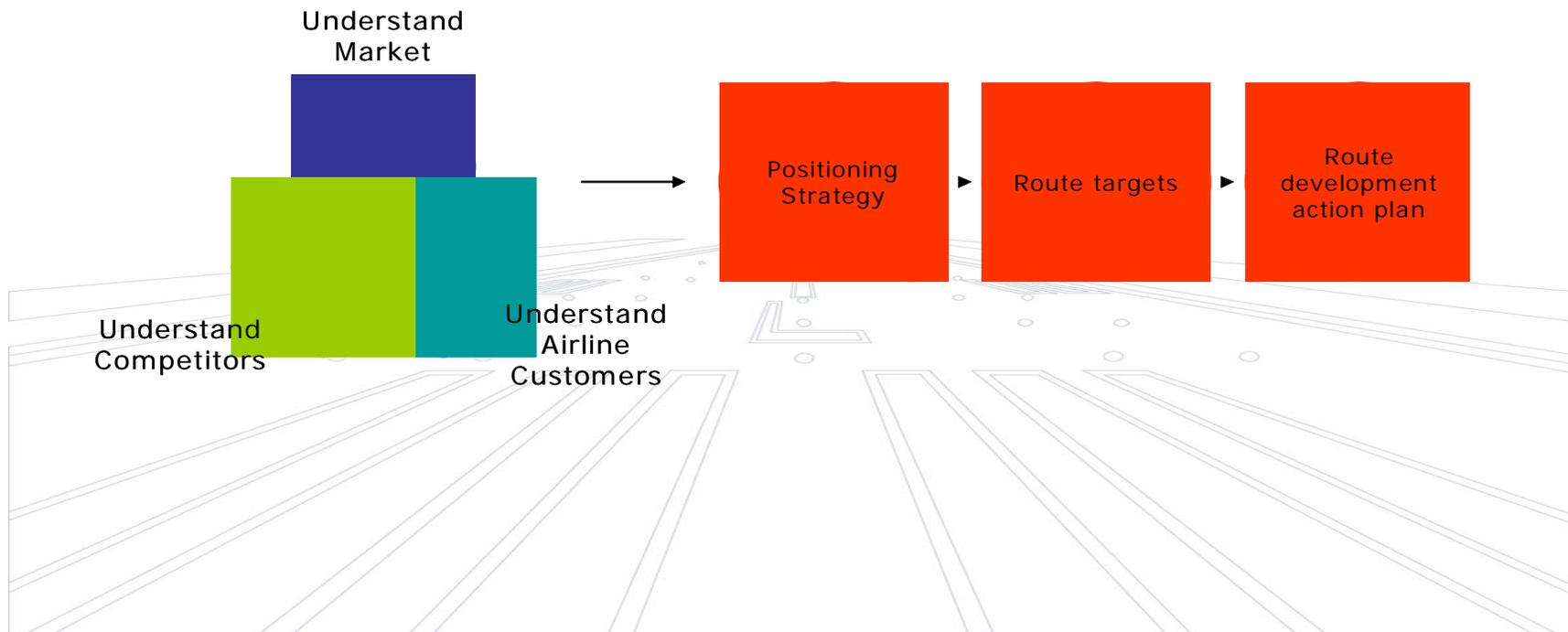
- Background – Previous / Current Interest
- Profile – Fleet, Alliances
- Route Development Strategy – Expanding / Consolidating
- Route Network – Frequency, Capacity, Hubs, Code shares
- Current Performance – Pax. Growth, Financial, PLF
- Key Personnel – Structure (Cargo, Scheduled, Sales, Commercial), Relationships, Age, Career, Ambitions,
- Decision Making Process – Key People, Meetings, Global, Regional, Local
- Culture – Open / Closed, Aggressive

Things change regularly – keep up to date !

# Route Development – Best Practice for Stakeholders

## The Route Development Process

Route development strategy...



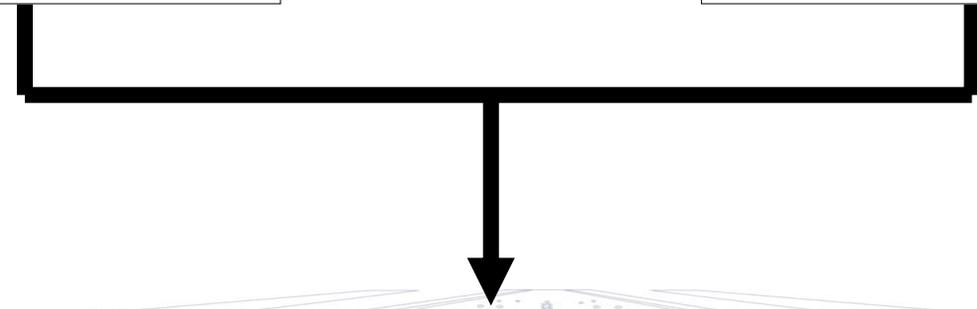
# Pro-Active Route Development – Does it Work ?

- Airports Company of South Africa set up a corporate marketing structure in 2001 which has delivered system wide growth in airline customers and passengers over the last four years.
- Costa Rica Ministry of Tourism and San Jose Airport adopted a mutually supportive marketing strategy in 2002. Out of 10 identified airline targets, 8 were delivered in the subsequent 18 month period
- Air Service Development is too important to leave to airlines !!!!

# A Practical Initiative – Action, Not Words

“International”  
EAS programme

International Tourism  
Development Route



ESTDR – Essential Service and Tourism  
Development Route Scheme

# ESTDR – Key Objectives

ESTDR have 2 main objectives:

- assure lifeline provision of air services for remote or peripheral destinations
- facilitate and drive economic development
  - develop tourism

States that are considered to be in most need of the introduction of ESTDR schemes are the group of 50 classed as Least Developed Countries (LDCs), Small Island Developing States (SIDS), and LandLocked Developing Countries (LLDCs)

# Example of other Schemes in Operation

There is 'patchy' usage of similar schemes across the world:

- PSO schemes in France, Greece, Ireland, Portugal, Spain
- Regional Route Development Funds in parts of the UK
- USA: Essential Air Service schemes to subsidise services between remote communities and hubs. There are also:
  - 'travel banks' funded by corporations
  - marketing funds typically through visitor and conventions bureau
- Caribbean airports: subsidies, revenue guarantees and subsidised fuel
- Africa: Egypt, Tunisia and Morocco provide route support for charter flights

*Route support schemes are all 'bespoke' and lacking consistency*

# Understanding of the principles of ESTDR

ESTDR are a form of essential air service scheme ...

“a mechanism whereby support, in the form of a financial subsidy and/or an exclusive concession, can be provided to airlines for the provision of certain services of a public service nature...”[\[1\]](#).

Historically, support has taken the form of:

- Generic direct subsidy
- Indirect subsidy
- *The experience of EU member states is that targeted assistance has been extremely beneficial in allowing critical lifeline routes to remain viable, thereby protecting the interests of some of Europe's peripheral communities.*

[\[1\]](#) A Study of an Essential Service and Tourism Development Route Scheme, ICAO / WTO 2005

# Key Issues Regarding Route Support Schemes

The experience of Route Support Schemes have challenged all 'stakeholders':

- Do they distort the market?
- How can they be well managed?
- Do they work?

*Persistent difficulties with these issues prompted the ICAO / WTO initiative – levelling the playing field*

# Understanding the criteria and designing a blueprint for an ESTDR scheme - the two key tests

## Test 1: Demonstration of need - does the community or region need air service?

- air service is needed because the region and/or airport is very remote
- vital economic sectors cannot remain viable without air service
- social or political reasons
- “development area” receiving tourism funding development

*If the airport or region meets one or some of these criteria, it is anticipated that the process then moves to the next test and then to the implementation steps described below.*

# Understanding the criteria and designing a blueprint for an ESTDR scheme - the two key tests

## Test 2: Economic Justification

Route economics will be scrutinised to see if:

- air service is not immediately viable
- but, with a realistic level of support it can be viable in the medium term.

Aircraft	A 319-100	737-200	A 320-200	727-200
Seats	124	108	150	149
ASKs	114,824	100,008	138,900	137,974
DOC (\$) per trip				
Fuel	2,033	2,491	2,142	4,118
Airframe Maintenance	429	1,214	460	3,936
Engine Maintenance	306	650	339	990
Line Maintenance	125	562	132	1,496
Flight Crew	672	672	672	940
Navigation	335	311	352	375
Landing Fees	490	401	562	661
<b>Total DOCs (\$) per Trip</b>	<b>4,390</b>	<b>6,301</b>	<b>4,659</b>	<b>12,516</b>
DOC (\$) Per Seat	35.40	58.34	31.06	84.00
DOC (¢) per ASK	3.8	6.3	3.4	9.1

# Potential ESTDR Scheme Structure

Once the key tests have been passed, the emphasis moves to one of structuring the scheme. Passing the test and structuring the scheme have a degree of iteration.

- route selection – including demonstration of need
- service level specification
- carrier selection
- contract duration
- subsidy payments
- sources of financing
- supplementary options
- regulatory arrangements

# Potential Route Selection

Scheme framework is not rigid ... it is the prerogative of Government to define candidate routes. 'Need' will be viewed in terms of:

- Lifeline provisions: if the route is not supported, no one will fly it
- Cultural contacts: air service is essential to link ethnic communities
- Supporting vital economic sectors: without adequate air service certain industries (such as tourism) will be adversely affected

*Economic development is likely to carry greater weight in the selection of routes.*

# Service Level Specification

ICAO / WTO study emphasized flexible approach in setting service level. The level of frequency and capacity has a circular relationship with traffic, revenues and cost.

- The traffic levels will be a function of the following:
  - Existing market – clear evidence of this will come from airport data, travel surveys or other research
  - Stimulated or 'directed market' some tourism flows will be generated simply because air services are made available
  - Schedule/frequency: some traffic will be sensitive to the days and times of flights; others will be sensitive to price

# Carrier Selection

Requirement to “...design the appropriate institutional mechanism as a means to allocate a targeted subsidy [so that] market distortion and unfair competition are minimized.” The normal method is likely to be an auction:

- Ensuring market protection and/or support is required. Usually this would be undertaken through publicising the route opportunity

- Screening for eligibility according to air service agreements

*Depending upon the outcome of these stages, there will be a design process for the receipt of tenders from eligible airlines.*

# Carrier Selection

The tender criteria should be driven by an assessment of the needs of the LDC and the degree of likely competitiveness. Criteria will include:

- Specification of routes and/or groups of routes for which support / market protection is required
- Level of support required
- Market protection required
- Extent of tourism development produced
- Airline financial viability
- Business plan
- Codesharing with partner airlines
- Other, ad hoc, factors
- Whether 'solus status' is required

*There will be a requirement to design a weighted ranking of these factors to allow for a quantified evaluation of competing bids.*

# Contract duration

Two broad options and a sliding scale between them.

- short term contract with the airline – has advantage of allowing competition onto the route or eliminating subsidies but discourages investment
- long term contract - advantage of allowing the airline time to develop the route and make the necessary investment.

Challenge to develop a framework for changing economic and market conditions and airline management and operating performance

*The trade-off, therefore, is between not providing a sufficiently attractive proposition (in the case of the short term contract) and creating a long-term protected monopoly, which would be bad for the consumer and possibly for overall market development.*

# Finance Sources ?

- Applicant regional/central government
- Key source market governments
- Development Agencies
- A PPP based on the "Axis of 6"
  
- Is it 'competitive' with other state expenditure? If so, what is the cost-benefit analysis (CBA) procedure?
  
- Would the Government need external domestic or international support?

*These factors require a deep understanding of the sources of international funding and finance aid.*

# Taking the ESTDR scheme forwards ?

- Air Service Development Plan needs to be identified as a catalyst for overall regional/national economic development
- Need complete synergy between Air Service Development and regional/national tourism strategy
- International Development Agencies and Banks – review the focus on supporting infra-structure rather than accessibility ?
- Development agencies in major tourism source markets (North America/Europe/Asia-Pacific) to assess financial participation
- Inclusion of ESTDR clauses in future bi-laterals
- Most of all – ICAO/WTO need to inaugurate the scheme quickly with a trial - who is willing to meet the challenge ??

Thank you !

