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No Alternative To IATA

An Interview with Mr Knut Hammarskjöld,
Director-General of IATA, Geneva

IATA is usually thought to be the guarantor of an economically sensible development of international air traffic. What is the justification for such a reputation?

IATA is a trade association of international airlines from 86 nations, with the basic objective: to provide the means of collaboration among air transport enterprises; to promote safe, regular and economic air transport for the benefit of the peoples of the world; and to foster air commerce and study the problems connected therewith.

The IATA Secretariat thus provides the means for the Member airlines to coordinate and rationalise their individual company or national policies by mutual agreement. It cannot *per se* "guarantee the economically sensible development of air traffic", but does provide the essential research organisation, international forum and negotiating machinery without which an integrated and co-ordinated global air transport system would not be possible.

What is your opinion on the reproach that IATA is a monopolistic institution?

Allegations that IATA is a "monopoly" or "cartel" are simply not valid, and are refuted by the facts. IATA is a voluntary, non-exclusive, non-political and democratic organisation. Membership is automatically open to any operating company which has been licensed to provide scheduled air service by a government eligible for membership in the International Civil Aviation Organization (a UN specialised agency).

All active Members of IATA have an equal vote, and decisions by the Traffic Conferences must be reached by unanimous agreement of all the Members. This implies that an individual Member can block any decision which it dislikes, and achieve its own objectives. In practice, most agreements are compromises which are only possible by a high sense of responsibility on the part of the negotiating delegates. Like any international agreements, however, the final results may sometimes take a long time and require much effort. IATA is not a supra-national

authority with either the power to refuse membership or to impose arbitrary or "monopolistic" decisions on a worldwide industry representing many different national interests and policies.

Price Agreements

Price policies of an organisation like IATA usually raise suspicion. What is the procedure for negotiating rates at the Passenger Traffic Conferences of IATA?

IATA's work begins only after the individual governments have promulgated a formal exchange of traffic and other rights, under bilateral air transport agreements, and have licensed specific airlines to perform such services.

In view of the complexity of the interlinking airline networks around the world and the price levels concerned it would obviously be impracticable to negotiate agreements on a short-term basis. In order to provide both a stable marketing plan for travel agents throughout the world and also to give the airlines a viable

basis for economic planning, the fares and rates levels are thus normally agreed for a period of two years.

Composite Traffic Conferences for Passenger fares and for Cargo rates are called in alternate years, in autumn and spring respectively. At these Traffic Conferences, all existing fares and rates must be either revalidated for a further period, cancelled, or amended in accordance with the individual Member airlines' marketing philosophies and traffic projections—and under unanimous agreement. Prior to each Conference, each Member airline submits proposals for the agenda on any aspect of the fares agreements which will affect its own operations, and documentation frequently runs into several thousand proposals. The IATA Secretariat is responsible for arranging and processing the negotiating sessions, working groups and committee meetings which are necessary to allow the Member airlines' delegates to reach the final agreements.

In practice, the global agreements are built up through hard negotiation of a series of inter-related regional or area agreements until the full worldwide fares structure has been completed. The resulting packages of normal and special fares are delicately balanced to cover all segments of the business and vacation travel markets and are closely interlocked to meet not only the regional but also the long-haul and interline traffic requirements.

Cooperation with Governments

To what extent can governments interfere with the price policies and generally with the activities of IATA?

The governments have the ultimate control over the IATA Member airlines' pricing policies. Before they can become

effective, the agreements negotiated at the Traffic Conferences are required to be filed for a statutory period with the interested governments for approval or rejection.

It is clear that no airline will come to the Conference table to negotiate a fares policy which is in conflict with its own national government's interests or objectives, and for which subsequent approval is unlikely to be forthcoming.

This is demonstrated by the fact that about 95 p.c. of all fares agreements negotiated under the IATA machinery do receive the necessary government approvals. The governments' protection of the consumer interests is evidenced by both the pre-Conference discussions with the national airlines and by the 5 p.c. rejection level. It is noteworthy that rejection of any component of a fares package by a single government authority can negate formal acceptance of the whole agreement for the whole area concerned.

Both the governments and the airlines who are parties to the fares agreements insist that IATA should police the agreements adopted, in order to ensure compliance by all concerned. Infringements can lead to disciplinary action against the offending airline or travel agent.

Costs and Revenues

Price increases are usually motivated by costs rising more rapidly than revenues. How would you describe the recent development of costs and revenues in the case of IATA Members?

In the year 1969 the world's scheduled airlines experienced a deteriorating financial position, despite growing traffic volumes. Due to inflationary trends, operating expenses increased by 15.3 p.c. compared

with a growth of only 13.6 p.c. in operating revenues.

Although world airline operating revenues were up from \$ 14,000 mn to \$ 15,900 mn in 1969, the operating profit fell from \$ 754 mn (5.4 p.c.) to \$ 627 mn (3.9 p.c.). Net profit, after deduction of non-operating items such as interest, taxes, etc. but including subsidies, dropped from an estimated \$ 430 mn (3.1 p.c.) to \$ 335 mn (2.1 p.c.) in 1969.

The airlines continue to be faced with a financial squeeze resulting from declining revenue yields and rising unit costs. Average revenue yields per ton-kilometer performed worldwide fell in 1969 by 1.1 p.c. to 31.91 cents, following a greater decline the previous year. This was accompanied by an increase in unit operating costs per ton-kilometer performed of 0.4 p.c. to 30.65 cents. There are indications that these adverse airline financial trends have continued through 1970.

There are several reasons for the continuing and rather disappointing airline financial trends. First, average unit operating costs are increasing because the cost savings resulting from the introduction of more productive aircraft continue to be more than offset by the inflationary trends in the costs of labour, materials and almost every service purchased by the industry. This includes the rapid increases in airport and en-route air navigation charges, and the cost of delays due to ATC slowdowns and airport and airways congestion which are adding to airline operating expenses. At the same time the airlines are facing a continuing downward trend in revenue yields due to the influence of a growing proportion of traffic moving at lower promotional or special discount fares and rates.

This declining trend in profitability comes at a critical time when the industry is faced with heavy capital demands. An analysis of the future capital financing situation indicates that IATA Member airlines as a whole are expected to incur expenditures between 1970 and 1974 of some \$30,000 mn in new capital investment on aircraft and spare parts and other fixed assets including ground equipment. They will also need an additional \$6,000 mn for the repayment of past loans.

Heavy Capital Requirements

Will the industry be able to meet these heavy capital requirements?

The industry's ability to meet these heavy capital requirements will depend very largely on future airline financial health, which is not only a source of internally generated capital, but also acts as an attracting force for external capital by demonstrating the security of investment for lenders as well as the prospect of a sufficiently attractive return for equity holders. With deteriorating financial health expected over the next few years, internal sources are expected to provide a smaller share of total capital requirements. External sources of capital, mostly loans, should therefore become relatively more important.

However, the worldwide demand for capital continues to exceed supply and interest rates are likely to remain high. Even if the financial health of the airlines improves there may still be difficulties in raising the large amounts of capital needed to finance the industry's growth. The best industry economic performance achieved in the past may not be good enough. The airline industry needs a satisfactory and consistent level of profitability and

a reasonable rate of return to be able to raise the necessary capital without government support.

A financially healthy airline industry will thus depend essentially on the inter-relationship of revenue yields, load factors and unit costs. The airlines individually and collectively will therefore have to exercise strict discipline in the fields of tariff policy and capacity provision in order to achieve adequate economic health. Support of governments to this end will be needed, but unsatisfactory airline profitability prospects will probably also require direct government participation in the form of loans and equity capital if the industry is to develop on a sound economic basis.

Chaos as a Result of "Free Market"

Would a "free market" for air traffic be a realistic alternative to IATA?

Definitely not. On international routes the results would probably be chaos and the disappearance of any semblance of an integrated global system allowing advance through bookings and interlining at common standards of service and scheduling.

Some critics of the IATA pricing structure believe that a "free market" would lead to a considerable decrease in air fares, but this is not necessarily true. There are examples of free markets where rates have gone up, for example in the tanker charter business. UN data on charters from important oil centers to Europe and the UK show tanker rates increasing by 27 p.c. between 1963 and 1969, a period characterised by the introduction of larger and more efficient vessels. Monthly data for 1969 show variations of over 100 p.c. in these rates, largely due to

seasonal supply and demand. Price increases and fluctuations of this order would not be acceptable to air passengers or shippers.

In a "free market" there would also be a danger that the larger airlines, with their vast resources and huge fleets, might drive the smaller or developing carriers out of business unless some form of restraint or control were to be exercised by national authorities. In practice, each nation jealously guards its own air space and commercial rights and the question of fares and rates is an important factor in every bilateral air negotiation. There are few routes in the world where traffic concerns only two countries and virtually every fare is related to and dependent upon every other.

Multilateral agreements are therefore essential. In the absence of some central negotiating machinery, each government would be driven into a perpetual series of bilateral negotiations with scores of other countries over each adjustment in a fare or change in the form of a baggage check. It was, in fact, this philosophy which led the ICAO nations in 1946 to delegate the responsibility for such negotiations to the newly-formed IATA, while still retaining the right of approval or rejection of the resulting agreements. It is this IATA system which has made it possible for an individual passenger to purchase a single ticket for a complex international journey involving many airlines and countries against a single payment, in any currency, with guaranteed reservations, standards of service and scheduling.

If the IATA negotiating machinery ceased to exist tomorrow, the national authorities would probably be forced to set up some similar organisation within six months.