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Book Review — Digitized Version

[Book Review of] Button, Kenneth,..., Flying into the future: air transport policy in the European Union: Cheltenham (UK), Elgar, 1998

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REZENSIONEN – BOOK REVIEWS

Button, Kenneth, Kingsley Haynes, and Roger Stough, *Flying into the Future. Air Transport Policy in the European Union*. Cheltenham (UK) and Northampton/Mass. 1998. Edward Elgar. XII, 199 pp.

The current decade has brought profound changes in the way air transport works. Not only has the institutional framework within which EU air transport takes place altered fundamentally since the liberalization of its air transport markets, but also the airlines have responded (and are still responding) to these institutional changes by ongoing reorganizing the operation of their industry, which – again as a repercussion – has led to new questions about the need to further accommodate the institutional setting of this transport sector by a new policy shift. Against this background, the book of Kenneth Button, Kingsley Hayes, and Roger Stough explores the organization of air transport in the European Union. It analyzes the nature of the industries supplying air transport services, the institutional structure within which the airlines operate, and the impediments to an increased efficiency in the provision of air transport. The authors not only consider the economics of European air transport but also legal, political, technical, and geographical issues.

Chapters 1 and 2 are devoted to the economics of the airline industry, at both the level of cost structures and the institutional framework underlying the operations of airlines. At the beginning, the reader is given some impression of the growth and size of the European air transport markets as well as of trends regarding air transport in other parts of the world. In addition, an overview on the general factors influencing the development of EU air transport is given. The analysis then turns to the cost structures that underly market outcomes in the airline industry, devoting great attention to the various cost concepts such as economies of scale, scope and density, and their relevance for the operational characteristics of airlines' route networks. The authors point out that (although economies of scale are of minor importance in the airline industry) the existence of considerable economies of scope and density coupled with characteristics of the demand side of air transport may give carriers that operate large (hub and spoke-) networks of routes a competitive advantage vis-à-vis rivals. Indeed, the trend of world air transport has been toward more concentration in this industry although, however, some smaller airlines especially in the United States which operate rather simple (point to point-) route structures have managed to be among the most profitable of the industry. The authors conclude that because considerable economies of networking exist in this industry, airline markets are not perfectly contestable, which raises the question if there is a need for some form of reregulation in the form of government control over air fares.

Regarding the institutional framework for European air transport, the authors discuss in length the change in the views on economic regulation which influenced the policy shift from tight regulation of EU air transport markets to almost full liberalization and describe the historical pattern of this policy change as well as the market outcomes of liberalization. They point out that, although perfectly contestable markets are unlikely to be achieved in air transport, a high level of contestability is possible in the aviation industry. The experience with the liberalized EU air transport markets show that consumers have greatly benefited from removing traditional regulation especially on those routes where the number of competitors has risen after the deregulation of market entry conditions. Many routes, however, have remained monopolies or at least duopolies with no entry occurring after liberalization, either because multiple services are simply not technically sustainable or institutional impediments still limit market entry.

The liberalization of EU air transport markets has been a gradual process, which has lasted for more than a decade. In contrast to this, the US government took a "big bang" approach for the deregulation of the US domestic air transport market. In Chapter 3, the authors discuss the pros and cons of gradualism versus the shock strategy of reform. As they state, the choice between the two alternatives is inevitably influenced by the social discount rate the reformers take into account: A big bang approach has high initial costs of disruption to an industry and possibly consumers, but a rapid move to a higher level of economic welfare, whereas gradualism has fewer initial adverse implications, but the benefits of change take longer to materialize. However, as they point out, a comparison of the US-style deregulation vis-à-vis the EU-style liberalization must always consider the specific characteristics of the different operational environments within which the carriers operate (e.g., the geographical dispersion of traffic, the role of nonscheduled operators, and intermodal competition). However, in my view the discussion of the latter point has shortcomings, especially in that the authors limit their treatment of this aspect to a pure description of the different conditions for air transport in both regions, but do not provide a strong link of reasoning between different environments on the one side and the different approaches of liberalization taken by the EU and the US government on the other. So after I read this chapter, I was still left with the question in which way specific conditions of the supply of air transport services do influence the optimal policy choice.

Chapter 4 is devoted to infrastructure as a necessary prerequisite for air transport to take place. It is argued that the institutional framework for the provision of infrastructure services may have profound effects on the development of air transport markets. The emphasis lies on congestion at major European airports and air traffic control systems, but also includes ground surface access. It is shown that a lack of adequate infrastructure facilities and also inefficient mechanisms to allocate existing infrastructure capacity among users may be a major impediment to competition between airlines and also to the future growth of air transport at all.

The next two chapters (5 and 6) look at a topic which is currently of important concern of EU air transport policy, namely the formation of airline alliances. Especially the formation of global alliances involving carriers from several continents, which coordinate schedules and fares, has risen political concerns about the consequences for the long-term perspectives of competition in air transport, and about the need to accommodate this trend by policy action to prevent inefficient outcomes. As the authors clearly state, alliances may generate positive and negative effects on the marketplace, as they allow carriers to exploit the full potential of economies of scope and density and therefore to lower costs of providing air services, but also may help airlines to circumvent legal restrictions on their activities and may give them market power by raising barriers to entry for non-alliance affiliated air service providers. The authors claim that, although currently available information reveals that the main international alliances have not, in the short term, resulted in any social net welfare loss, a clear understanding of the longer-term effects is still lacking, especially with regard to the structural effects the formation of airline alliances may have on regional air transport links.

Chapter 7 explores the issue of the stability of liberalized EU air transport markets. This is an aspect which has not yet attracted much attention in the literature although it was of considerable media interest in the light of significant losses of the world's leading airlines in the early 1990s and also seems to underly the pragmatic approach of the EU's merger policy regarding this sector. In order to fill the gap and to answer the question if policy action is needed to prevent market instability, the book employs the theory of the core. It is argued that airline markets show conditions which this theory would predict as to lead to natural market instability and therefore to inefficient market outcomes. These conditions can (as the authors state) also explain the current efforts of airlines to coordinate their operations as efficiency-enhancing. However,

because (albeit with a different direction of correlation) several of those conditions are also consistent with collusion for rent-seeking purposes, it is difficult to judge airlines' route, schedule and pricing cooperations either as efforts to cure market failure, or as a reflection of efforts to create market power. Hence, given the state-of-the-art knowledge about the functioning of airline markets, the question cannot yet be answered what the best policy response to those actions by the airlines would be, as the longer-term stability necessary for an emerging market equilibrium is not yet fully understood (p. 169).

At the end of the book (Chapter 8) the authors ask if last decade's EU air transport policy has been a success. Their answer is: Although EU-style liberalization has brought benefits for those engaged in the industry as well for their customers, EU aviation policy is still far from being complete, especially with regards to the management of infrastructure services, competition policy, and external relations.

The book presents a comprehensive and clear overview on the current status of EU air transport policy. It highlights the changes in aviation the policy shift of the last decade has generated, and also points to open policy questions. Although it does not present any new statistical or econometric analysis (except a rough examination if those conditions exist in the air transport industry which would perhaps result in an empty core problem), this is not a real shortcoming, as the authors' main intentions were not directed to presenting new quantitative analysis when writing the book. Instead, their aim was to show the complexity of policy questions that evolve in a liberalized air transport marketplace as the industry's players adjust to the removal of traditional regulation. This aim has its own merits, as it seems that the fundamental forces that drive the air transport industry are often not well understood in the public policy debate. Therefore, it is not a drawback that readers are left with more open questions than answers after they have studied this book, but pointing to these questions makes the book worthwhile to read. Especially the discussion of a perhaps natural instability of airline markets may pave the way for further research of an aspect of airline markets which, although it may be of particular importance for the future formulation of EU competition policy for this sector, has received too little attention in the academic discussion. I enjoyed reading the book, and in my opinion it may be valuable to read for all those that are engaged or interested in this industry, for which it may serve as a valuable starting point for future research on the questions raised in this book.

Hartmut Wolf

Halpern, Laszlo, and Charles Wyplosz (eds.), Hungary: Towards A Market Economy. Cambridge, U. K. 1998. Cambridge University Press. XX, 399 pp.

Antal-Mokos, Zoltan, Privatisation, Politics, and Economic Performance in Hungary. Cambridge, U. K. 1998. Cambridge University Press. XVI, 231 pp.

The transition process has had a relatively long and unique history in Hungary. In contrast to many other East European economies, the acceptance of a coexistence between, and experimentation with, different organizational arrangements provided Hungary with initial conditions perceived to be conducive to rapid and successful transition in the wake of political changes in the late 1980s. These favorable conditions were complemented with the presence of, *inter alia*, a developed human capital base, extensive external linkages with non-socialist economies in the West and elsewhere, and a traditionally export-oriented productive base essential for the development of a small open economy.

The experience of the economy in the 1990s has, however, invalidated much of these presumptions. Difficulties have been manifold and pervasive. Relative to other broad-