DEPARTMENT OF TRANSPORT

AIRLIFT STRATEGY 2006

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1. INTRODUCTION

1.1 Purpose

This document presents a five year South African Airlift Strategy (Strategy) for the regulation of air transport in support of the Tourism Growth Strategy.

The Strategy was developed based on aviation policy directives and as a specific response to the Accelerated and Shared Growth Initiative of South Africa (ASGI-SA) and as directed by Cabinet. The Draft Strategy also addresses issues raised by the Department of Environmental Affairs and Tourism (DEAT) and South Africa Tourism (SAT), whilst also responding to the air freight requirements as envisaged in the National Freight Logistics Strategy, approved by Cabinet in 2005.

It is recognised that the Strategy at this stage focuses mainly on the air transport needs of the trade and tourism sectors and does not necessarily address the requirements of all Government Departments. The effectiveness of the Strategy will, however, depend on ongoing research regarding market developments worldwide as well as the identification and incorporation of additional or revised governmental requirements.

1.2 Mission

The White Paper on National Transport Policy (1996) defines South Africa's mission for air transport as follows:

"To maintain a competitive civil aviation environment which ensures safety in accordance with international standards and enables the provision of services in a reliable and efficient manner at improving levels of service and cost while contributing to the social and economic development of South Africa and the region."

This Mission was reconfirmed during the recent policy review project and incorporated into the draft White Paper on National Civil Aviation Policy, 2006.

In keeping with the above, the mission for air transport in particular with respect to the Tourism Growth Strategy is to ensure an enabling environment, which responds effectively to the needs of domestic and international users and air service providers.

1.3 Goals

The Strategy is aimed at:

- Locating the South African Civil Aviation Industry's growth within government's overall policy framework with specific focus on government initiatives such as ASGI-SA;

- Contributing towards sustainable economic growth and job creation with emphasis on the ASGI-SA initiative.
- Ensuring the sustainable growth of the South African Civil Aviation Industry, with emphasis on introduction of new entrants to the market, and expansion of existing markets;
- Creating an enabling framework which allows both consumers and service providers reasonable flexibility and choice;
- Enhancing the prospects for South Africa as a preferred air travel destination;
- Aligning air transport with other national strategies through the common criteria of the "National Interest" through inter-departmental participation with specific reference to the National Foreign Policy, National Tourism Strategy, National Trade and Industry Strategy as well as general infrastructure requirements of South Africa;
- Improving institutional coordination and alignment between all relevant stakeholders, as per the Tourism Sector Plan; and
- Address airline competition and pricing to reduce total cost of travel to South Africa.

2. LEGAL MANDATES

The following instruments represent the legal mandate for the regulation of air transport services:

2.1 The Constitution of the Republic of South Africa, 1996.

2.2 The Convention on International Civil Aviation (Chicago Convention) of 1944 regulates international civil aviation worldwide.

2.3 Aviation Act, No 74 of 1962 gave effect to South Africa's legal adoption of the Chicago Convention.

2.4 Civil Aviation Policy guides South Africa's participation in the rapidly changing aviation market. The International Civil Aviation Policy of 1992 was developed with the primary purpose of guiding South Africa's participation in the rapidly changing international aviation market. Both the current domestic and international air transport policies were revisited during 1996 and were re-confirmed, with minor additions, through the White Paper on National Transport Policy (1996). This Policy is currently under review and a *draft White Paper on National Civil Aviation Policy, 2006,* will be published for public comments in the near future.

The main principles of the current and proposed revised policy are to encourage effective competition, to safeguard national interests and to encourage South African participation in the market. This policy recognises that the national interests of the country and the interests of the suppliers and consumers respectively may not coincide. The policy thus represents a trade-off between these various interests. In theory, therefore, the interests of the "national carrier(s)" should not be a prime factor determining South Africa's negotiating approach.

The policy is aimed at encouraging competition through the implementation of the Yamoussoukro Decision, multiple designation of airlines, double disapproval tariff system, liberal capacity and frequency regime, promotion of all international airports as entry points in South Africa and that third and fourth freedom traffic rights (direct air services) will form the basis for negotiating the exchange of traffic rights.

2.5 Air Services Licensing Act (Act No. 115 of 1990):

The Air Services Licensing Act, 1990, regulates access to the domestic air services market based on airlines' ability to operate safe, secure and reliable air services. No economic regulation is applicable for entry into the domestic market.

2.6 International Air Services Act (Act No. 60 of 1993)

The fundamental objectives of the current Policy were embodied in the International Air Services Act, 1993 (Act). This Act will be amended to give effect to the *draft White Paper on National Civil Aviation Policy, 2006, once* approved by Government.

The International Air Services Council (Council) has been established in terms of this Act and is responsible for the licensing of South African airlines serving international destinations.

In giving effect to the stated national priorities as defined in the Policy, the Council has to perform its duties in terms of Section 3(3) "*... in a manner which in its opinion is calculated-*

(a) to promote trade with, and tourism to and from, the Republic;
(b) to promote competition between persons who operate international air services;
(c) not to unjustifiably prefer any licensee over another;
(d) to promote a high standard of safety in the operation of international air services;
(e) to promote the development and interests of the local international air services industry;
(f) to promote the interests and needs of users or potential users of air services in the Republic.".

The Act empowers the Minister to enter into air services agreements with other States, subject to the approval of the President. Arrangements that may be included in bilateral air services agreements are specified in broad terms. No specific requirements regarding the granting of 5th freedom rights[1] and "Open Skies" arrangements are prescribed. Foreign airlines

[1] Definitions contained in Annexure H

wishing to fly to South Africa must obtain a foreign operator's permit (FOP) from the Chairperson of the Council.

2.7 National Freight Logistics Strategy

Cabinet approved the National Freight Logistics Strategy in 2005. The Department of Transport has subsequently commissioned the development of an *airfreight logistics strategy* responding to the airfreight requirements as envisaged in the National Freight Logistics Strategy. This *Airlift Strategy* focuses mainly on passenger and freight air services whilst the *Airfreight Logistics Strategy* will in particular focus on infrastructure issues.

2.8 Bilateral Air Services Agreements

Bilateral air services agreements are negotiated on an equal basis between equal partners, reflecting the mutually agreed best-fit between the national interest of the negotiating partners. The bilateral system therefore, has the flexibility to accommodate the policies of a wide range of states of different sizes and at different stages of economic development, with airlines of varying strengths and capabilities.

Since 1992, South Africa has embarked on the review and modernisation of all bilateral air services arrangements in terms of the International Aviation Policy. This process was accelerated since 1994 following the establishment of a democratic government and subsequent worldwide support for the country's transformation agenda.

South Africa has to date concluded bilateral air services agreements with one hundred and four (104) States in all regions of the world. Twenty-five (25) of the hundred and four agreements (104) provide for the designation of a single airline per side. Forty-four make provision for the approval of applicable tariffs by both sides. Seventy-nine (79) agreements provide for the multiple designation of airlines by each side. Only fifty-nine agreements provide for the double disapproval tariff regime. This liberal system requires the disapproval of both contracting parties to prevent introduction of a tariff.

2.9 Multilateral and Regional Agreements:

2.9.1 World Trade Organisation (WTO):

Since the 1990's, regional air transport liberalisation initiatives have enjoyed preference over the World Trade Organisation (WTO) multilateral approach.

A number of developed countries support the exchange of traffic rights and air transport liberalisation through the WTO framework, claiming that the bilateral system created under the Chicago Convention has become inadequate. The majority of states, however, do not support this view and limited the GATS Annex on Air Transport to what are termed soft rights and exclude traffic rights ("hard rights"). This approach is also endorsed and encouraged by ICAO[2].

2.9.2 Yamoussoukro Decision

In 1999, African States formally adopted the Yamoussoukro Decision (YD) for the liberalisation of intra-African air transport services Article 10 of the Abuja Treaty.

In general there is reluctance from some African States to implement YD. During May 2005, the African Ministers responsible for air transport in Africa met at Sun City and initiated a process towards the accelerated implementation of the YD. A further Ministerial meeting was held in May 2006 hosted by Gabon to review progress made towards implementation of the YD. The outcome of this meeting as well as the high level meeting of African Airlines held in Tunis on 29 and 30 May 2006 assist in respect of Yamoussoukro Decision implementation.

South Africa has opted to implement the spirit of YD on a bilateral level with willing partners as an interim measure, pending full implementation of the YD across Africa. The DOT has also embarked on the development of an approach aimed at accelerating the implementation of YD. This will include an econometric study to quantify the economic cost of regulatory constraints, including benefits that could be reaped as a direct result of the implementation of the Yamoussoukro Decision. This will guide South Africa's approach towards YD when engaging with the African Union, NEPAD and bilateral counterparts in Africa.

2.9.3 South African Development Community (SADC) Protocol:

SADC member states signed the Protocol on Transport, Communications and Meteorology in 1996. The main aim of this Protocol is the establishment of transport and communications systems which are efficient, cost-effective, predictable, environmentally sustainable and meeting the needs of the users. In particular, the Protocol focuses on the elimination of hindrances and impediments to the movement of persons, goods and services.

The SADC Protocol's sub-regional initiatives on liberalisation of intra-Africa air transport services are aligned with the principles of the Yamoussoukro Decision.

[2] ICAO – International Civil Aviation Organisation

3. AVIATION ENVIRONMENT

3.1 Global Passenger Market Growth:

Air transport is a significant contributor to economic growth and job creation worldwide. Its economic impact exceeds US$ 2.9 trillion or 8% of global GDP and generates 29 million jobs within the following categories[3]:

- Around 5 million are directly employed;
- There are 5.8 million indirect jobs through purchases of goods and services from companies in its supply chains;
- 2.7 million are induced jobs through spending by industry employees; and
- Another 6.7 million direct and 8.8 million indirect jobs are the result of air transport's catalytic impact on tourism.

Growth through Tourism

"Perhaps the major contribution that air services can make to economic development services in Africa is through developing and promoting international tourism".

"Tourism facilitates poverty reduction by generating economic growth, providing employment opportunities and increasing tax collection, and by fostering the development and conservation of protected areas and the environment".

"Economies with high growth during the last decade (eg: Mauritius, Tunisia, Egypt, Ghana) have tended to be those where the tourist sector is key to economic activity."

- Oxford Economic Forecasting, *The Contribution of Air Transport to Sustainable Development in Africa*, 2003

The International Air Transport Association (IATA) projects that international air travel will experience an annual growth rate of 5.6% between 2005 and 2009. This is lower than the average growth rate of 6.5% per annum seen during the buoyant 1990s. Growth is expected to be strongest in Asia and the Middle East, in line with strong regional economic growth, and lower in the more mature North American and European markets.

IATA also projects that air travel to and from South Africa will, for the five years to the year 2010, grow at an average annual rate of 5%. The highest annual average growth rates between 6.6% - 6.8% are forecast on Europe-Middle East, Middle East – Asia Pacific and within Asia-pacific. The lowest growth of 4.2% and 4.6% are respectively forecast within Latin America/ Caribbean and North America to Latin America (IATA, 2005).

Routes between Europe and Africa have largely developed on the basis of historic political and economic ties, rather than by recent economic growth. Nevertheless, Africa's economic performance remains closely linked to trade with Europe and the potential for tourism-led development. European originating demand, in particular for leisure flows, has the most potential to spur growth in air passenger traffic levels between the two regions. As investment in tourism infrastructure and economic governance improve in African countries, so will the attractiveness of African destinations for European travellers. In

[3] Oxford Economic Forecasting / Air Transport Action Group, (OEF/ATAG) 2005, Economic and Social Benefits of Air Transport

addition, NEPAD infrastructure development initiatives will accelerate the improvement of aviation infrastructure in Africa and thereby facilitate the expected increased passenger and cargo movements on intra-African routes.

On a country-pair basis, IATA projects that the SA-UK route will register an average growth rate of 4.8% over the period 2005 to 2009. The entire Africa region enjoys only about three percent of the international air travel market and is projected to register an overall average annual growth rate of about 5,7% over the period 2005 to 2009. (IATA Forecasts – 2005 – 2009)

3.2 Contribution to the South African Economy:

The aviation sector is a vital component of the South African economy. However, due to historic reasons, the sector's contribution to the economy has been constrained. Likewise, tourism has played a relatively small role in the South African economy prior to 1994. However, in the last 12 years, the aviation and tourism sectors' contribution to the economy has increased substantially, growing from approximately 1 million tourist arrivals in 1990 to over 7 million in 2005.

Tourism generates in excess of R 48 billion in revenue from foreign tourists each year and, since 2000, has been growing volumes at rates averaging between 4% and 6%.[4]

Tourism is a major contributor to job creation in South Africa – the only priority sector that has grown both its Gross Domestic Product (GDP) and employment contribution to the economy. At current levels, tourism supports 540,000 direct jobs, and a further 670,000 indirect jobs. Based on this performance, growth of tourism arrivals contributes one new direct job for every 12 new tourists. Alternatively, every additional air frequency serving South Africa will support the creation of 1100 new jobs in the year that service is introduced.[5] In the light hereof, the important role of South African and foreign airlines to transport these tourists to South Africa should not be underestimated. It, however, also highlights the importance of providing sufficient air transport capacity to all key tourism markets.

3.3 Airlines providing airlift:

3.3.1 SA Airlines:

Based on ownership, South African airlines can be categorised as Government-owned or privately-owned (including listed companies).

[4] SA Tourism – Aviation and Tourism Growth, 11 April 2006
[5] This assumes 1 new weekly flight for a year by a B747-400 aircraft with 340 seats at an average seat occupancy rate of 75%.

- **Government owned:**

  Government owns South African Airways (SAA) and SA Express (SAX). Whilst these airlines are powerful tools for achieving governmental goals, they also pose unique challenges in respect of the regulatory framework and competition environment (details reflected in paragraph 3.4). SAA is the dominant South African airline in respect of both the domestic and international air services markets.

- **Privately owned South African airlines:**

  Privately owned South African airlines providing scheduled air services include Comair/Kulula.com, Nationwide, Interair, 1Time, Airlink, Airlink Regional and Pelican Air Services.

3.3.2 Foreign airlines serving South Africa since 2000:

The total number of foreign airlines serving South Africa appears to be gradually increasing as indicated below. The table, however, does not reflect the changing face of operators. For instance, during 2002, 12 new airlines entered the South African market whilst 6 operators left the market. Similarly, in 2003, 4 new airlines entered the market, balanced by 4 airlines exiting the market, keeping the total at 67. In some instances airlines withdrew due to strategic changes to their networks, in other cases airlines were liquidated (e.g. Swissair and Khalifa Airways (Algeria)).

Table 1: Foreign airlines serving South Africa

	Foreign Scheduled Airlines:	Passenger/ cargo combined - actual operations:	Code Sharing – marketing airline only	Dedicated Cargo Services:
2000	61	49	6	10
2001	61	44	8	14
2002	67	46	9	16
2003	67	47	8	15
2004	71	51	9	14
2005	75	54	9	17

3.4 Concept of "National Airline"

3.4.1 Defining "national airline" or "flag carrier"

Conventionally, "national airline" also known as "national carrier", refers to "**state owned airline**". This concept, which is as old as commercial aviation itself, is a direct result of the high cost of capital associated with this industry, leaving governments as the only entities able and willing to source the vast amounts of capital required for the establishment of airlines. Such airlines are normally named after the founding state, e.g. South African Airways, Air Namibia, etc, displaying corporate logos based on the national colours.

This concept was also firmly entrenched in the Chicago Convention of 1944, although not to the exclusion of private ownership of airlines.

The term 'flag carrier' is normally used to refer to the national, state-owned airline of a country. With the steady movement towards privatisation in the airline sector, and a concentration on commercial stability of airlines, some major national airlines, such British Airways, have distanced themselves from their national identity. Others, such as Air Canada, have simply appropriated the national symbol of the Maple Leaf for their own commercial purposes: 'The Maple Leaf on the tail of an Air Canada plane is not a symbol of our national identity. It is a corporate logo.' [6]

The term 'national carrier' is currently used to refer to the airlines of particular states, regardless of ownership. This is mainly due to the liberalisation of air services agreements for the designation of one or more airlines registered in a particular country. For instance, in the case of the RSA-Namibia Agreement, SAA,BA/Comair and SA Express are all designated as national (ie South African-based) airlines, authorised to operate air services. This more technical use of the term is sometimes confused in popular literature with the older, conventional definition of a single state-owned airline.

3.4.2 Integration of a conventional national state-owned carrier into the economy

Developments in the international experience of national airlines have been complicated with the promotion and implementation of privatisation in the airline sector, and the growth internationally of competition on international routes, more or less coincident with the rise of a large number of independent states after 1960 as colonial empires collapsed. At least two, potentially conflicting trends developed: on the one hand, the introduction of liberalisation and increased competition between international carriers and the opening of domestic markets in developed countries to larger numbers of airlines occurred on the back of economic growth and development in the north. On the other hand, newly emergent independent states remained committed to developing national airlines both as elements of national pride, but essentially as strategic assets to encourage incorporation into the global economy from areas that were not considered commercially viable, or of any other interest, to international carriers other than those of the former

[6] Ward, as quoted in "The Canadian Experience with Deregulation, May 15, 2005, E Lacobucci, University of Toronto, M Trebilcock, University of Toronto and R Winter, University of British Columbia

colonial powers (eg Air France into West and Central Africa, or BA into East and Southern Africa).

More recently, forceful arguments promoted through the so-called Washington Consensus, attempted to drive privatisation and liberalisation of air services deeper from the developed north into the developing world as a whole. A common suggestion was that the rise of an increasing number of privately-owned, commercially driven airlines in both domestic and international markets presented government regulators, in countries with their own state-owned airlines, with a potential conflict of interest between securing the greater good of the consuming public against protection of state carriers.

South Africa falls between the two extremes of experiences. On the one hand, the maturity of the economy has encouraged and in turn been influenced by the opening up of the domestic market to multiple airlines of different sizes and shapes. The negotiation of bilateral air service agreements with other nations has ensured that today we have unprecedented numbers of airlines flying to and from South Africa. However, our geographic location, associated with the nature of the global interactions that our developmental state has incorporated into our domestic agenda, emphasises that, strategically, a national carrier (however the ownership structure may be structured) can still be a major catalyst for our further integration with the international community. Currently, the frequency of flights to and from South Africa by non-South African carriers is often determined by current seasonal demands, rather than the need for daily or regular commuter traffic. However, South Africa's growth and development, and the role it plays on the continent, cannot be determined by seasons or irregular demand, and we must retain our own capacity for international and regional integration. The international airline environment is dynamic and policies need to take all factors into consideration.

It is apparent from the above evidence that there is nothing inherently contradictory between state ownership on the one hand and efficient operation and commercial viability on the other. Within the context of a properly structured regulatory and legislative environment, state owned airlines can continue to operate effectively without necessarily taking advantage of unfair competition. Of course it is possible, but it is not inevitable, and government should ensure that the national carrier, in operating in line with clearly defined national strategic objectives, does not impinge on the ability of privately owned entities to operate fairly either.

3.5 Role of National Airlines in the Civil Aviation Market:

National airlines (state owned and/or private) are important for the building of tourism destinations. For the majority of destinations that have emerged in the last ten years, the national airlines (state owned and/or private) of such countries have been a key feature of their success.

A case study conducted in respect of QANTAS and Thai International suggested two possible approaches to ensuring that emerging destinations achieve alignment between their tourism strategies and their national carriers (state owned and/or private). These approaches are:

- **Indirect Regulation and Facilitation: Case Study – QANTAS**:
  Australia developed a competitive approach to air services, and privatised QANTAS against these objectives through:

  - Three-year pre-privatisation period where the regulatory environment was liberalised to allow it to "get fit", i.e., to effectively face major competitors in the global market;

  - Privatisation was used to enable major re-investment and fleet expansion with private sector capital; and

  - Created an environment in which QANTAS was encouraged to work in close alignment with the tourism industry.

- **Direct State Involvement: Case Study – Thai International:**

  The Thai Government developed Thai International with the explicit mandate to:

  - Develop and expand company business to become a world-class airline;

  - Promote Thailand as gateway into the Asia-Pacific region;

  - Support Thailand's tourism industry; and

  - Maximise profit in order to raise funds for human resource development and equipment necessary to achieve the above objectives.

The following illustrates the strategic importance of the national airlines towards the building of destinations: