International Transport Forum

Assessing the Prospects for an E.U.-ASEAN Air Transport Agreement

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OECD

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THE INTERNATIONAL TRANSPORT FORUM

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Table of contents

Tables

Figures

1. Introduction

In February 2014, transport officials from the European Union (E.U.) and the Association of Southeast Asian Nations (ASEAN) met on the sidelines of the Singapore Airshow to discuss a possible comprehensive air transport agreement between both sides. At the meeting's conclusion, the ASEAN states invited the European Commission to launch the internal processes necessary to secure a mandate to commence negotiations on an agreement. In particular, ASEAN welcomed Vice President of the European Commission and Commissioner for Transport Siim Kallas' statement that he would propose to the Commission to seek authorization from the Council of the European Union to start negotiations (E.U.-ASEAN Joint Declaration, 2014).

The economic potential of a "bloc-to-bloc" agreement is obvious: it would be the first accord to lay out an "open skies" or "open aviation area" arrangement between two major regional trading blocs. This could significantly liberalize traffic rights and market access for both regions' airlines into each other's respective territories, along with numerous other potential benefits. Indeed, with 28 and 10 countries respectively and a massive combined population of 1.1 billion, the E.U. and ASEAN economies stand to benefit greatly from an ambitiously-crafted agreement.

Air traffic between the two regions has nearly doubled in the last 15 years to more than 10 million passengers in 2012 (E.U.-ASEAN Joint Declaration, 2014). At the same time, a significant amount of traffic in the E.U.-ASEAN market has been captured by airlines from third countries, particularly the "sixth freedom" carriers like Emirates, Etihad, Qatar Airways and Turkish Airlines. Thus, a major impetus for the proposed E.U.-ASEAN agreement is the desire on both sides to stem this loss of traffic to the sixth freedom carriers.

This paper assesses if the proposed agreement can realistically counter the sixth freedom carriers' market power. At the same time, the asymmetries between the E.U.'s common aviation market and the incomplete ASEAN Single Aviation Market (ASAM) will be analyzed to illustrate both sides' unequal bargaining positions.

2. Envisioning the E.U.- ASEAN "open skies" market

Unlimited Third and Fourth Freedom Rights?

While actual negotiations have not started, it is nonetheless possible to predict the features of any meaningful accord. One critical liberalizing feature would be the complete relaxation of third and fourth freedom rights on a bloc-to-bloc basis. Hence, market access in the form of direct, non-stop flights between the two regions operated by airlines designated by both sides could become unlimited in capacity, frequency and aircraft type. This is the basic philosophy behind all modern "open skies" aviation agreements, and should form the backbone of the proposed E.U.-ASEAN agreement.

An "open skies" regime with unlimited third and fourth freedom rights and capacity for both regions' airlines could go some way toward winning back some of the traffic lost to sixth freedom rivals. Hence, major hub-to-hub operations between Singapore, Bangkok and Kuala Lumpur (on the ASEAN side) and London, Paris, Frankfurt, Amsterdam and Rome (on the E.U. side) will likely benefit from increased operations and market competition.

Here, it should be noted that currently, not all the bilateral agreements between the E.U. and ASEAN states have been fully liberalized. The proposed comprehensive agreement will undoubtedly seek to overcome this problem – indeed, with full relaxations, the ASEAN carriers will enjoy unlimited rights and capacity into all the E.U. countries, including those such as France, Greece and Italy that still maintain capacity restrictions bilaterally. The E.U. carriers will similarly enjoy reciprocal unlimited access into ASEAN points.

To date, the European Commission has concluded "horizontal" agreements with only 4 out of the 10 ASEAN states (Indonesia, Malaysia, Singapore and Vietnam) to allow for the automatic designation of all E.U. carriers to enjoy the traffic rights between individual E.U. states and these ASEAN states (European Commission, 2013). Four other ASEAN member states - Brunei, Cambodia, the Philippines and Thailand - have agreed to E.U. designation in a more limited way, i.e. through amendments of bilateral agreements with individual E.U. states. The two remaining ASEAN states, Laos and Myanmar, have not yet entered into any agreement for E.U. designation. The table below shows the status of such agreements:

Table 1. **Status of E.U. designation agreements with ASEAN member states**

E.U. designation agreed under a horizontal agreement		E.U. designation agreed bilaterally with E.U. Member State	
	Total no. of bilateral agreements amended		No. of bilateral agreements amended
Singapore	22	Thailand	7
Malaysia	19	Philippines	4
Indonesia	19	Brunei	2
Vietnam	17	Cambodia	1

Source: European Commission, Bilateral Air Services Agreements brought into legal conformity since the Court of Justice of the EU judgments of 5 November 2002,
http://ec.europa.eu/transport/modes/air/international_aviation/external_aviation_policy/doc/table_-_asa_brought_into_legal_conformity_since_ecj_judgments-_january_2013.pdf

In essence, E.U. designation allows carriers such as Lufthansa (and for that matter, all E.U. airlines) to be designated to fly between, say, Paris and Singapore even though they are not French carriers. However, actual traffic capacity remains governed by the relevant bilateral agreements. If these have finite entitlements (e.g. the France-Singapore agreement), the E.U. carriers will have to share that limited capacity between themselves following E.U. Regulation 847/2004. Of course, a comprehensive E.U.-ASEAN agreement will overcome this problem and eliminate capacity constraints altogether.

Table 2. **Direct operations by E.U. and ASEAN carriers between the two regions**

Carrier (Region)	Originating Points/Hubs	Destination Points	Total Weekly Seats	% of Total Capacity
Thai Airways (ASEAN)	Bangkok	Brussels, Copenhagen, Frankfurt, London Heathrow, Madrid, Milan, Munich, Oslo, Paris, Rome, Stockholm, Zurich	64,410	26.1
Singapore Airlines (ASEAN)	Singapore	Amsterdam, Athens, Barcelona, Copenhagen, Frankfurt, London Heathrow, Manchester (via Munich), Milan, Munich, Paris, Rome, Zurich	61,792	25.0
Malaysia Airlines (ASEAN)	Kuala Lumpur	London Heathrow, Frankfurt Paris, Amsterdam	27,516	11.2
KLM (E.U.)	Amsterdam	Bali (via Singapore), Bangkok, Kuala Lumpur, Jakarta (via Kuala Lumpur), Manila (via Taipei), Singapore	15,620	6.3
Vietnam Airlines (ASEAN)	Hanoi, Ho Chi Minh City	London Heathrow, Frankfurt, Paris	13,508	5.5
Air France (E.U.)	Paris	Bangkok, Ho Chi Minh City, Kuala Lumpur, Singapore	13,394	5.4
Lufthansa (E.U.)	Frankfurt	Bangkok, Jakarta (via Kuala Lumpur), Kuala Lumpur, Singapore	11,648	4.7
British Airways (E.U.)	London Heathrow	Bangkok, Singapore	11,284	4.6
Finnair (E.U.)	Helsinki	Bangkok, Singapore, Hanoi, Krabi, Phuket	9,992	4.0
SWISS (E.U.)	Zurich	Bangkok, Singapore	6,132	2.5
Austrian (E.U.)	Vienna	Bangkok	4,312	1.7
Norwegian (E.U.)	Stockholm, Oslo	Bangkok	3,492	1.4
Garuda Indonesia (ASEAN)	Jakarta	Amsterdam	3,140	1.3
Condor (E.U.)	Frankfurt	Bangkok, Phuket	498	0.2
		TOTAL	**246,738**	100.0

Source: Airline websites and Centre for Aviation (CAPA) and Innovata, at http://centreforaviation.com/analysis/emirates-etihad--qatar-continue-to-pursue-rapid-expansion-in-southeast-asia-western-europe-market-120471

Note: Weekly capacity is for week of 4-10 November 2013. The figures reflect direct flights on the respective airlines' own metal (aircraft) only; codeshare operations on other carriers are excluded. Fifth freedom operations by non-E.U. and non-ASEAN carriers are excluded; SWISS and Norwegian taken as E.U. carriers.

Table 3 illustrates the points serviced in both regions by the Middle Eastern and Turkish sixth freedom carriers, while Table 4 sets out these carriers' weekly capacity into ASEAN.

Table 3. **One-stop operations by sixth freedom carriers between the E.U. and ASEAN**

Carrier	**Originating Hub**	**Destination Points**		
		E.U.		**ASEAN**
Emirates	Dubai	Amsterdam Athens Barcelona Birmingham Brussels Copenhagen Dublin Dusseldorf Frankfurt Geneva Glasgow Hamburg Larnaca Lisbon London Lyon	Madrid Malta Manchester Milan Munich Newcastle Nice Oslo Paris Prague Rome Stockholm Venice Vienna Warsaw Zurich **Total: 32**	Bangkok Ho Chi Minh City Jakarta Kuala Lumpur Manila Phuket Singapore **Total: 7**
Qatar	Doha	Athens Barcelona Berlin Brussels Bucharest (via Sofia) Budapest (via Zagreb) Copenhagen Edinburgh Frankfurt Geneva Larnaca London Madrid	Manchester Milan Munich Oslo Paris Rome Sofia Stockholm Venice Vienna Warsaw Zagreb Zurich **Total: 26**	Bali (via Singapore) Bangkok Clark, Manila Hanoi (via Bangkok) Ho Chi Minh City Kuala Lumpur Jakarta Manila Phnom Penh (via Ho Chi Minh) Phuket (via Kuala Lumpur) Singapore Yangon **Total: 12**
Etihad	Abu Dhabi	Amsterdam Brussels Athens Berlin Dublin Dusseldorf Larnaca London	Frankfurt Geneva Manchester Milan Munich Paris Rome Zurich **Total: 16**	Bangkok Ho Chi Minh City Jakarta Kuala Lumpur Phuket Manila Singapore **Total: 7**
Turkish Airlines	Istanbul	A total of **74** points in the E.U.		Bangkok Ho Chi Minh City (via Bangkok) Jakarta (via Singapore) Kuala Lumpur Singapore **Total: 5**

Source: Respective airlines' websites.

Note: E.U. points include those in Norway and Switzerland.Own elaboration of Ministry of Transport Statistics, 2014.

Table 4. **Middle Eastern and Turkish carriers' capacity into ASEAN, by weekly seats**

Carrier	November 2011	November 2012	November 2013	% growth over Nov 2011	No. of ASEAN destinations
Emirates	72,982	80,588	112,028	54	7
Qatar Airways	46,372	47,720	68,374	47	12
Etihad	29,202	38,812	48,314	65	7
Turkish	N.A.	N.A.	approx. 10,000	N.A.	5

Source: Centre for Aviation (CAPA) and Innovata, at http://centreforaviation.com/analysis/emirates-etihad--qatar-continue-to-pursue-rapid-expansion-in-southeast-asia-western-europe-market-120471 and http://centreforaviation.com/analysis/http://centreforaviation.com/analysis/turkish-airlines-narrowing-the-strategic-gulf-part-2-112353

Note: Seat capacity is for the first week in November 2011, November 2012 and November 2013.

It can be seen that the Middle Eastern and Turkish carriers' penetration into both regions, particularly in the E.U., is hugely impressive. Hence, they have tremendous capacity to compete for traffic in the E.U.-ASEAN market. Turkish Airlines alone has more than 70 destinations in the E.U., although its seat capacity into ASEAN lags behind the Middle Eastern carriers'. Of course, these sixth freedom carriers collect passenger "feed" from other regions such as Northeast Asia, North America and Africa as well. As such, their operations benefit from greater economies of scale in being able to funnel passengers from a variety of markets through their mid-point hubs. This is particularly important for filling up aircraft on the thinner routes involving smaller cities.

What this means is that an unlimited "open skies" regime between the E.U. and ASEAN may not help to justify their respective carriers' direct, non-stop flights between ASEAN and smaller non-hub E.U. cities such as Bordeaux, Oslo, Glasgow, Prague or Zagreb. The problem for these operations is not the lack of traffic rights but the absence of a sizeable market to fill up the aircraft. The same applies to direct flights between the E.U. and ASEAN cities such as Bali, Phuket, Manila, Ho Chi Minh City or Yangon. Due to superior geography and operating economics, the Middle Eastern and Turkish sixth-freedom carriers are better-positioned to exploit their "hub-and-spokes" advantage. Indeed, all the above cities are connected by one or more of the sixth freedom carriers through their respective hubs.

Consequently, an E.U-ASEAN comprehensive agreement with unlimited third and fourth freedom rights is likely to boost, if at all, only the hub-to-hub operations between the two regions. The thinner routes will remain difficult to fill. Even for the hub or trunk routes, there is unlikely to be a significant increase in actual traffic carried. With some exceptions, most direct E.U.-ASEAN routes already enjoy unlimited or near-unlimited capacity under the existing bilateral agreements. For instance, Singapore carriers have had unlimited rights into London Heathrow and all points in the U.K. since 2007; the real problem here is the lack of slots at Heathrow Airport which an E.U.-ASEAN agreement does not cure.

Elsewhere, unlimited or generous rights for ASEAN carriers to fly to the likes of Berlin, Brussels or Barcelona already exist, but are largely unutilized due to the lack of a market for regular and profitable operations. Similarly, the E.U. carriers have more than enough rights into points such as Kuala Lumpur, Hanoi, Phnom Penh and Jakarta but these have also proven to be unprofitable. Overall, unlimited capacity into points such as Paris and Manila that are still limited by the relevant bilateral agreements might be welcomed, but unlimited traffic rights alone will not help the E.U. and ASEAN carriers fill up their flights, particularly on the thinner routes.

A more significant strategy to grow the market would be to facilitate agreements between airlines from both sides that are immunized for joint venture, "metal-neutral" operations. These will allow hitherto competing players on a particular route to co-operate and engage in joint marketing and revenue-sharing. To illustrate, KLM and Garuda Indonesia could conceivably launch daily flights between Amsterdam and

Jakarta that see both carriers jointly marketing and operating those flights beyond simple code-sharing. Each carrier could take one of two daily flights, for instance, or half of the number of weekly flights. In this manner, the co-operating carriers would be “metal-neutral”, in that they become indifferent to which between them operates a particular segment, as long as both work toward marketing all seats that are cumulatively on offer. Overall, this represents a more viable strategy against rival sixth freedom carriers.

Naturally, such close co-operation (presumably along alliance lines) will invite competition or antitrust law scrutiny from regulators. Such “metal-neutral” operations have already received the blessings of regulators in the U.S., Japan, Korea and Singapore (for trans-Pacific flights, e.g. by Japan Airlines and All-Nippon Airways) and the U.S. and E.U. regulators for operations across the Atlantic. A comprehensive E.U.-ASEAN agreement could conceivably seek to facilitate such operations between the two regions and to lay down the necessary safeguards for protecting competition. It follows that in each case, regulators will still have to conduct robust economic analyses to determine the effect on competition. However, to the extent that strong competition is posed by the sixth freedom carriers in the E.U.-ASEAN market, approving such co-operation by airlines from both ends appears to be straightforward.

Fifth Freedom Rights and Ownership and Control Rules?

The proposed E.U.-ASEAN agreement should also go beyond liberalizing third and fourth freedoms flights (i.e. direct, non-stop flights) to relax fifth freedom operations as well. Thus, E.U. carriers could gain from having mid-point stops with traffic rights in the Middle East or India as well as beyond-ASEAN rights to Australia, New Zealand and the Pacific. For instance, E.U. carriers could stop over in Mumbai, India on an E.U.-Singapore-E.U. flight with unconstrained traffic pick-up rights in Mumbai in both directions, as well as similar rights in Singapore for an onward segment to Sydney, Australia and back. Conversely, ASEAN carriers could secure similar rights in Mumbai en route to the E.U. as well as beyond-E.U. rights to the Americas (e.g. Thai Airways on a Bangkok-Mumbai-Frankfurt-New York operation).

Such fifth freedom rights already exist in many of the current bilateral agreements, although their daily or weekly capacity may be restricted. Singapore Airlines, for instance, utilizes beyond-E.U. fifth freedom rights for its Singapore-Frankfurt-New York and Singapore-Barcelona-Sao Paolo operations. The E.U. carriers have similar traffic pick-up rights in ASEAN points for onward segments to Australia (e.g. British Airways’ London-Singapore-Sydney operations). The E.U.-ASEAN agreement’s aim should be to relax such operations to a greater or unlimited degree in order for its liberalizing impact to be meaningful. Of course, such operations must also be permitted by the respective agreements with the third countries concerned (i.e. India, Australia, the U.S. and Brazil in the above examples).

The exchange of full intra-regional fifth freedom rights within the E.U. and ASEAN should also be considered. Again, the bilateral agreements already provide for such operations, albeit with limited capacity on some routes. Hence, E.U. carriers like KLM have been operating to Bali via Singapore and Jakarta via Kuala Lumpur, in both cases with traffic pick-up rights in the mid-point ASEAN cities. Conversely, Singapore Airlines offers a Singapore-Munich-Manchester routing. Such fifth freedom operations should be freed up completely with capacity and pricing left to the market to dictate. Indeed, under the E.U.’s Regulation 1008/2008, E.U. carriers and, on the basis of reciprocity, air carriers of third countries, can freely set air fares and rates for intra-E.U. services. That said, given the fierce competition from the LCCs, few airlines from outside the E.U. have actually found it profitable to mount intra-E.U. operations.

The beyond-E.U. fifth freedom rights are likely to be more contentious, particularly because the lucrative trans-Atlantic market to the U.S. would be impacted. The E.U. airlines and their member states have tended to guard this market jealously, and ASEAN would conceivably have to offer a suitable quid pro quo or exchange. Here, the logical beyond-ASEAN market to barter would be Australia and New

Zealand. Yet, the E.U. carriers that have attempted this route in the past have mostly pulled out due to the high operating costs and severe competition. In fact, British Airways remains the only E.U. carrier still operating a fifth freedom flight to Australia (Sydney) via Singapore and even then, competition is stiff due to over-capacity in this sector. A bargain in some other form will likely have to be found in order to make fifth freedom liberalization work.

One possible avenue would be to negotiate a "package deal" involving more liberal investment opportunities in both sides' airlines. This would be similar to what the E.U. had negotiated with the U.S. and Canada, only that the U.S. still insisted on restricting foreign ownership of voting shares in U.S. airlines to no more than 25%. Here, the E.U. agreement with Canada would be more instructive – the liberalization of traffic rights is explicitly conditioned upon ownership limits in each side's airlines being progressively relaxed (E.U.-Canada Air Transport Agreement, 2009). Hence, when the national laws of both parties permit nationals of the other party to own and control up to 25 per cent of the voting interests of its airlines, unlimited third and fourth freedom rights for both sides' airlines shall be granted. When the relaxation on ownership and control goes up to 49 per cent, relaxations on fifth freedom rights shall apply.

Following this approach, the E.U. and ASEAN could phase in provisions allowing for either side to own up to 49% of shareholding in the other's carriers, with ownership allowed to be held region- or Community-wide. The relaxation of traffic rights could then be explicitly tied to such progressive relaxation on ownership. Practically, this will allow a consortium of E.U. airlines (possibly from within the same airline alliance group, e.g. Star, Oneworld or Skyteam) to hold 49% of interests in an allied ASEAN carrier. With the E.U. generally having more investment capital, the deal is likely to see more E.U. airlines and interests buying stakes in ASEAN airlines than the other way around.

What is notable about the E.U.-Canada agreement, though, is the fact that Canada previously limited foreign ownership of its airlines to 25% of voting shares and prohibited foreign control. As such, a progressive relaxation up to 49% could be traded in negotiations with the E.U. In the case of ASEAN, the complication is that the various member states have different ownership and control rules. Most already allow foreign ownership of local airlines up to 49%, in which case there would be nothing new to barter with the E.U. There is then the exceptional case of the Philippines, which maintains a lower threshold (40%) for foreign ownership of local airlines. This simply means that the ASEAN states will have to craft a consistent internal policy on airline ownership stakes first before they can negotiate effectively with the E.U.

Assuming ASEAN can agree on a common 49% cap for foreign ownership, this could conceivably be offered to the E.U. along the lines of the E.U.-Canada agreement. Alternatively, the E.U.-ASEAN agreement could simply provide for a 49% relaxation and leave it to the individual ASEAN states if they wish to adopt it. This could be a more realistic avenue as the relevant legal restriction in the Philippines is actually found in its Constitution and may be very difficult to amend.

For now, the E.U. and ASEAN should perhaps attempt to replicate what the E.U. has concluded with Canada, particularly in tying the relaxation of traffic rights (including eventually fifth freedom rights) to the progressive relaxation of ownership restrictions in the other party's airlines. Another model, albeit hugely imperfect, would be the draft fifth freedom deal that ASEAN has struck with China. While agreeing to trade unlimited third and fourth freedom rights, the Chinese were wary of giving up beyond-China fifth freedom rights to ASEAN airlines. China thus excluded its three major cities of Beijing, Shanghai and Guangzhou from the fifth freedom deal. Further, it offered a finite list of 10 points (mostly secondary cities) through which "beyond" fifth freedom rights could be exercised by ASEAN carriers. No "linkage" between traffic rights and ownership rules was made, which was probably wise given the complexities in doing so. However, capacity is limited to 14 weekly flights for each contracting state.

As for "internal" or "behind" fifth freedom rights (e.g. a Singapore carrier's Singapore-Bangkok-Shanghai operation, i.e. an ASEAN-ASEAN-China routing), the Chinese offered a list of 28 cities through which such operations can be mounted. Again, these are mainly secondary cities and the three major points of Beijing, Shanghai and Guangzhou are excluded. For both "internal" and "external" fifth freedom, the ASEAN states each offered a secondary point through which the Chinese carriers' operations can be routed. The result is a fifth freedom deal that is limited to secondary cities on both the Chinese and ASEAN sides.

Table 5 below reproduces the list of cities that are implicated in the deal. It is obvious that there are few realistic fifth freedom operations that can be mounted. A likely candidate route could be Singapore-Chongqing-Los Angeles, given Chongqing's size and huge catchment population. However, its geographical position in the interior of China means that the route will be circuitous and lengthy. Filling up the Chongqing-Los Angeles sector could thus turn out to be difficult.

The lesson here for the E.U. and ASEAN is that if a finite city "list" approach were to be taken, it must be ensured that the possible routings are commercially feasible, lest the agreement ends up being practicably worthless. If limits to fifth freedom have to be imposed at all, the better way would be to limit capacity only (e.g. no more than a maximum number of weekly flights or seats), rather than to add a further limitation on the cities through which the rights can be exercised.

Table 5. **Points Offered for the ASEAN-China Agreement's Draft Protocol 2 on Fifth Freedom Rights**

<table>
<tr><th></th><th>"External" Fifth Freedom
(e.g. ASEAN – China – Third Country or
China – ASEAN – Third Country)

Example: Malaysian carrier operating
Kota Kinabalu - Kunming – Delhi;
Chinese carrier operating
Xian – Chiang Mai - Sydney

[Weekly limit of 14 per country]</th><th>"Internal" Fifth Freedom
(e.g. ASEAN – ASEAN – China or
ASEAN – China – ASEAN or
China – ASEAN - ASEAN)

Example: Malaysian carrier operating
Kota Kinabalu - Chiang Mai - Kunming or
Kota Kinabalu - Haikou - Chiang Mai;
Chinese carrier operating
Xian – Chiang Mai - Singapore

[No weekly limit]</th></tr>
<tr><td>Brunei</td><td colspan="2">Bandar Seri Begawan</td></tr>
<tr><td>Cambodia</td><td colspan="2">Preah Sihanouk (Sihanoukville)</td></tr>
<tr><td>Indonesia</td><td colspan="2">Mataram (Lombok)</td></tr>
<tr><td>Lao PDR</td><td colspan="2">Luang Phabang</td></tr>
<tr><td>Malaysia</td><td colspan="2">Kota Kinabalu</td></tr>
<tr><td>Myanmar</td><td colspan="2">Any point except Yangon</td></tr>
<tr><td>Philippines</td><td colspan="2">Any point except Manila</td></tr>
<tr><td>Singapore</td><td colspan="2">Singapore</td></tr>
<tr><td>Thailand</td><td colspan="2">Chiang Mai</td></tr>
<tr><td>Vietnam</td><td colspan="2">Any point except Hanoi and Ho Chi Minh City</td></tr>
<tr><td>China</td><td>Nanning, Guilin, Kunming, Chengdu, Chongqing, Urumqi, Xian, Changsha, Zhengzhou, either Xiamen or Fuzhou

Total: 10</td><td>Nanning, Guilin, Kunming, Chengdu, Chongqing, Urumqi, Xian, Changsha, Zhengzhou, Xiamen, Fuzhou, Xishuangbanna, Wuhan, Shenyang, Dalian, Haikou, Sanya, Guiyang, Lanzhou, Xining, Yinchuan, Lhasa, Kashgar, Hohhot, Harbin, Changchun, Ningbo, Yanji

Total: 28</td></tr>
</table>

ASEAN Skies: Not Yet Truly Open

At this point, one should note the reality that the ASEAN states do not yet have a true single market among themselves comparable to the E.U.'s. Hence, ASEAN is nothing like the E.U., let alone a fully unified market like Canada or the U.S. For one thing, the ASEAN carriers do not enjoy the so-called "seventh freedom" that would allow them to fly between two points outside their home state (not even two points within ASEAN!).

As a result, a Singapore carrier cannot set up a base in Indonesia to fly to Thailand or to operate between domestic points in Indonesia, unless it adopts the traditional method of incorporating a subsidiary in Indonesia that is majority-owned and effectively controlled by Indonesians. Of course, such restrictions have been abolished in the E.U., where any E.U. airline can freely connect any number of E.U. points (even domestic ones) and can establish itself in any other E.U. member state without having to ensure that majority ownership and effective control reside in that state.

As for the more modest third, fourth and fifth freedom rights, the ASEAN Single Aviation Market (ASAM) project does attempt to liberalize these completely by way of several multilateral agreements. However, for these rights to take effect in an individual ASEAN member state, that state must explicitly accept the relevant multilateral agreements that spell them out. This is totally unlike the E.U. where the common market has automatic Community-wide application by force of law.

In ASEAN, the largest member state, Indonesia, has only recently on 30 May 2014 accepted the agreements that free up third, fourth and fifth freedom rights (and even then for its slot-constrained capital, Jakarta, only). For now, the other ASEAN states must still rely on their bilateral air services agreements with Indonesia that contain finite capacity entitlements to enable their airlines' operations into other Indonesian points.

The crux is that ASEAN's regional integration is not as developed as the E.U.'s. Critically, there is no supranational organ like the European Commission that can compel member states to place the regional interest above individual, national interests. The fact that the Commission can bring E.U. member states before the European Court of Justice (notably in the *Open Skies* cases) to extract compliance with a single market ambition is the precise reason why the E.U. common aviation market is relatively successful. Of course, aviation is only part of the larger E.U. project for regional integration, and that gives the common aviation market additional momentum. In ASEAN, the SAM project is wholly voluntary in that individual member states can accept liberalization commitments as and when they feel ready. As such, reluctant states can hold up the entire project if they do not see it as in their or their airlines' interests to accept.

As for ownership and control, the ASAM takes a leaf out of the E.U.'s book to provide for the possibility of a "Community Carrier". Hence, the ASAM makes it possible for an airline set up in Cambodia, for instance, to be majority-owned by ASEAN interests taken together (e.g. 20% Singapore, 20% Thai and 11% Cambodian stakes). In theory, there is no need for a Cambodian majority interest as long as effective regulatory control over the airline resides with the Cambodian authorities. While this provision exists on paper, no airline to date has actually been set up as a Community Carrier. This is because the ASEAN agreements provide that each individual member state retains the discretion to reject applications by such a carrier to fly to its points.

Not surprisingly, new airlines set up in ASEAN in recent years have continued to employ the traditional model with local (i.e. national) interests owning more than 50% of shareholding (the foreign investor typically holds 49%). This is still seen to be the preferred and more sustainable model. The recent examples of joint venture airlines of this type are low-cost carriers (LCCs) bearing a foreign parent's brand – Thai Lion Air, Malindo, Thai VietJet Air and Nok Scoot. These now join the more established LCCs like

Thai AirAsia, Indonesia AirAsia and Jetstar Asia, all of which are joint ventures featuring majority local/national ownership but using the foreign parents' brands.

Consequently, there is adherence in ASEAN to the "substantial ownership" requirement in that the foreign partner does not enjoy majority shareholding. That said, the related requirement of local "effective control" has taken on a much looser meaning. Most ASEAN member states gloss over the requirement and appear satisfied when their national is appointed as CEO. Whether effective control truly resides locally could be questionable since many of the joint venture airlines are run as integrated operations alongside their parent foreign carriers, using established common brands or identities as well as combined internet booking platforms. Relevant examples include the AirAsia, Jetstar, Tigerair and Lion Air operations.

In this regard, the ASEAN governments' relatively lenient attitude toward control has to be contrasted with the increasing attention that E.U. regulators are paying to airlines allegedly controlled by foreign minority shareholders, e.g. the Etihad equity stakes in various smaller European airlines. Even in liberal Hong Kong, the proposed establishment of Jetstar Hong Kong has elicited huge opposition from incumbent carriers such as Cathay Pacific and Hong Kong Airlines over the proposed new LCC's alleged control by the Jetstar/Qantas group in Australia. The more relaxed attitude toward control in ASEAN has actually allowed liberalization to grow roots, despite the governments' formal attitude toward foreign ownership stakes.

As a result of its unfinished single aviation market project, what is interesting about ASEAN's aviation relations is that it readily negotiates with third countries and blocs even as its own internal market is not yet truly "single". Consequently, an E.U.-ASEAN comprehensive agreement will practically mean that an ASEAN airline can fly to E.U. points only from its home national territory. Conversely, all E.U.-designated airlines will be able to connect any E.U. point to any ASEAN point, for the simple reason that the E.U. "backyard" is a unified one. This presents a significant market imbalance that disadvantages the ASEAN airlines in the long term. Moreover, E.U. airlines can now merge among themselves (the way Air France-KLM, British Airways-Iberia and Lufthansa-SWISS have done), but this is still impossible for the ASEAN airlines. Of course, all these market imbalances can only be corrected if the ASEAN States start to treat their own backyard as a true single market but this will take years to realize.

In this regard, it is clear that for the immediate future, an E.U.-ASEAN comprehensive agreement with open or unlimited capacity stands to benefit the E.U. airlines more in terms of market networks and penetration. Yet, the pragmatic ASEAN position is that it is unrealistic to wait for its own internal market to be forged first. This is why ASEAN had gone ahead to adopt an air transport agreement with China in 2010, despite all the market imbalance drawbacks described above. Hence, Chinese airlines can fly from all of China to all of ASEAN, while ASEAN airlines can fly to all of China only from points in their home states (Tan, 2010).

Fundamentally, apart from lacking a supranational mechanism to overcome national sovereignty and to prioritize the regional interest, the problem with ASEAN is that the individual member states' interests and levels of development are too disparate. The lack of a united negotiating stand is also partly why ASEAN could not convince the Chinese to allow fifth freedom rights through the major cities of Beijing, Shanghai and Guangzhou (as explained above). As a result, ASEAN's negotiations with the E.U. will likely be characterized by aero-political dynamics and asymmetries that are broadly similar to those encountered with China. Like with China, third and fourth freedom liberalization can probably be attained with minimal problems. However, fifth freedom rights and ownership and control issues will be much more complicated.

The challenge then is to make the proposed E.U.-ASEAN comprehensive agreement as meaningful as possible, despite the aero-political realities. Beyond third and fourth freedom relaxations, the negotiators should attempt to negotiate a "package" deal entailing liberalization for fifth freedom operations, joint venture and alliance arrangements as well as mutual investments in and control over their airlines. Both sides should also seek to promote deeper co-operation in other challenging issues such as harmonization of safety and security standards and even regulatory oversight over passenger rights, competition law and carbon emissions.

3. Conclusion

Ultimately, even if all these goals were progressively met in the proposed E.U.-ASEAN comprehensive agreement, there is probably not too much that the agreement alone can do to stem the loss of traffic to sixth freedom carriers. Overall, the two blocs should not allow their proposed comprehensive agreement to be defined only by the desire to neutralize the sixth freedom carriers. Other liberalizing steps and areas of co-operation that promise mutual benefit should be pursued in order to bring two dynamic regions that are separated by the tyranny of distance a whole lot closer, particularly in terms of market philosophy, trading relations and people-to-people exchanges.

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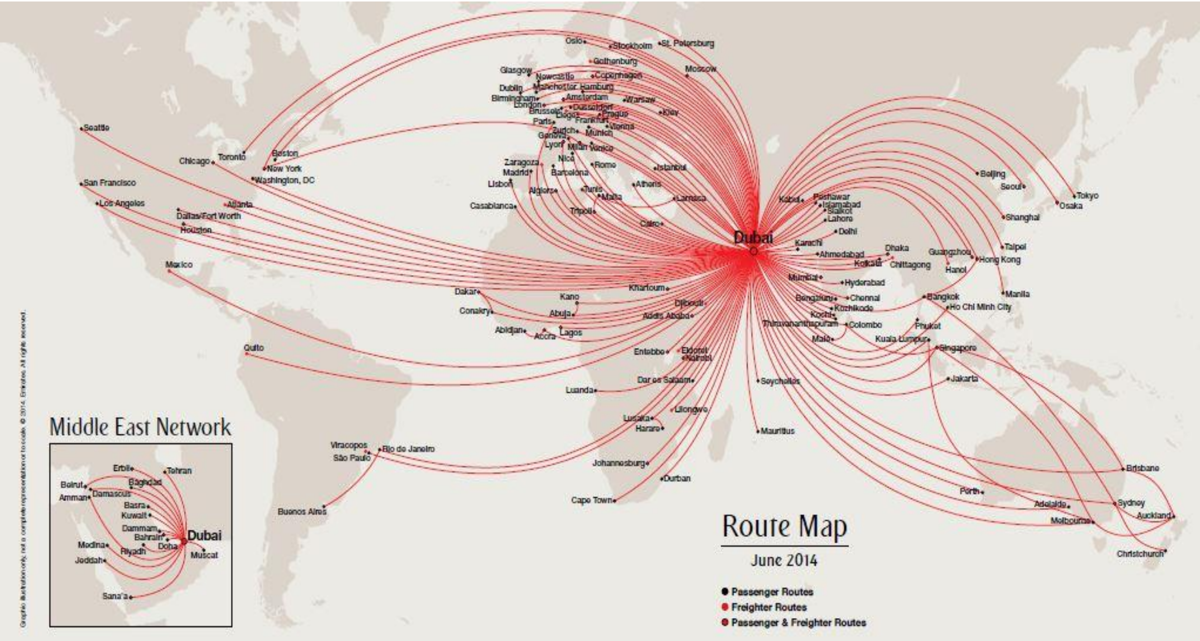
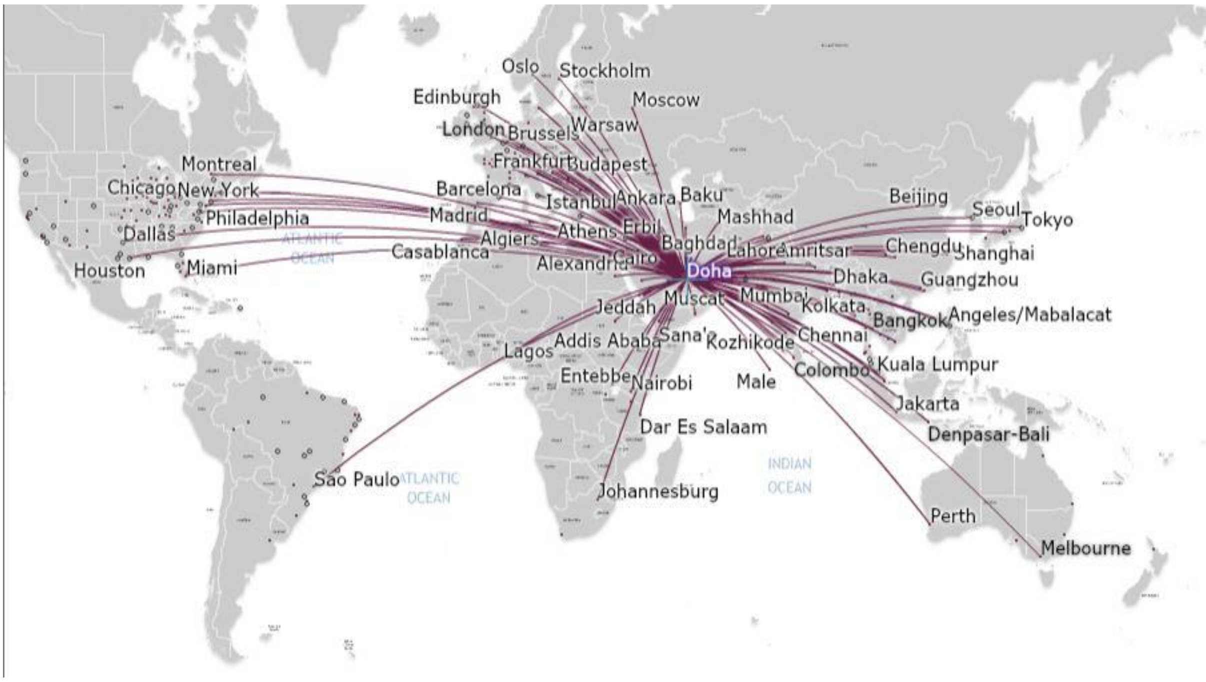
Annex I. Network maps of leading sixth freedom carriers in the Middle East and Asia

Figure 1. **EMIRATES**



Source: Emirate's website

Figure 2. **QATAR AIRWAYS**

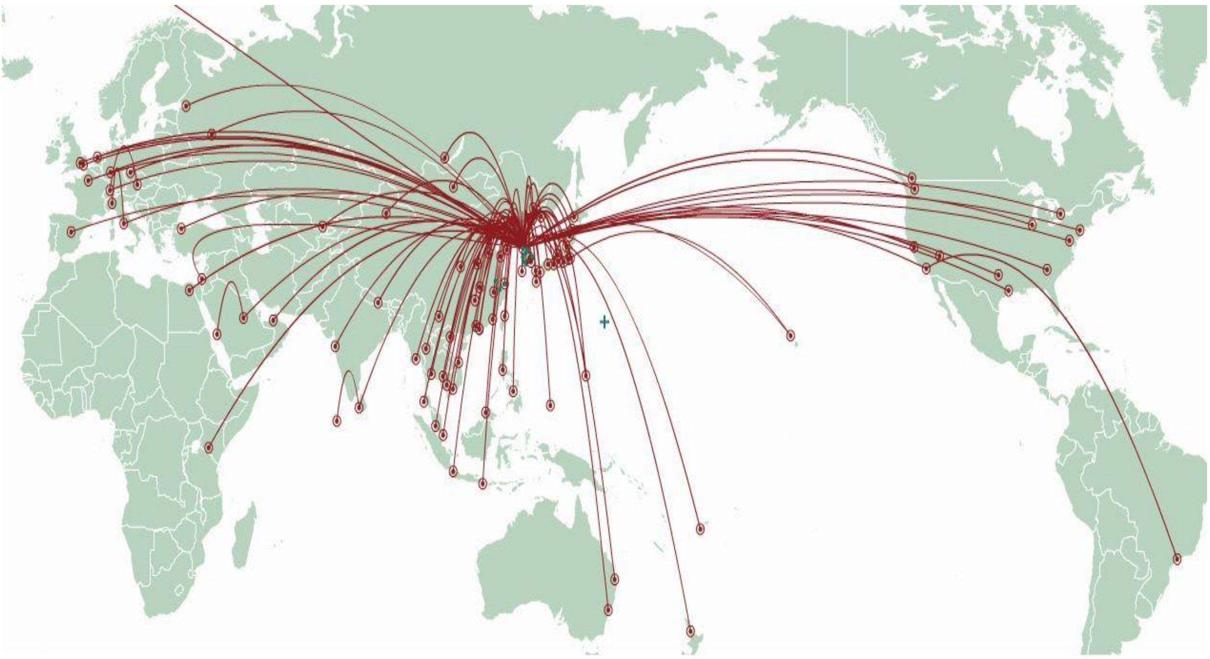


Source: Qatar Airways' website

Figure 3. **TURKISH AIRLINES**

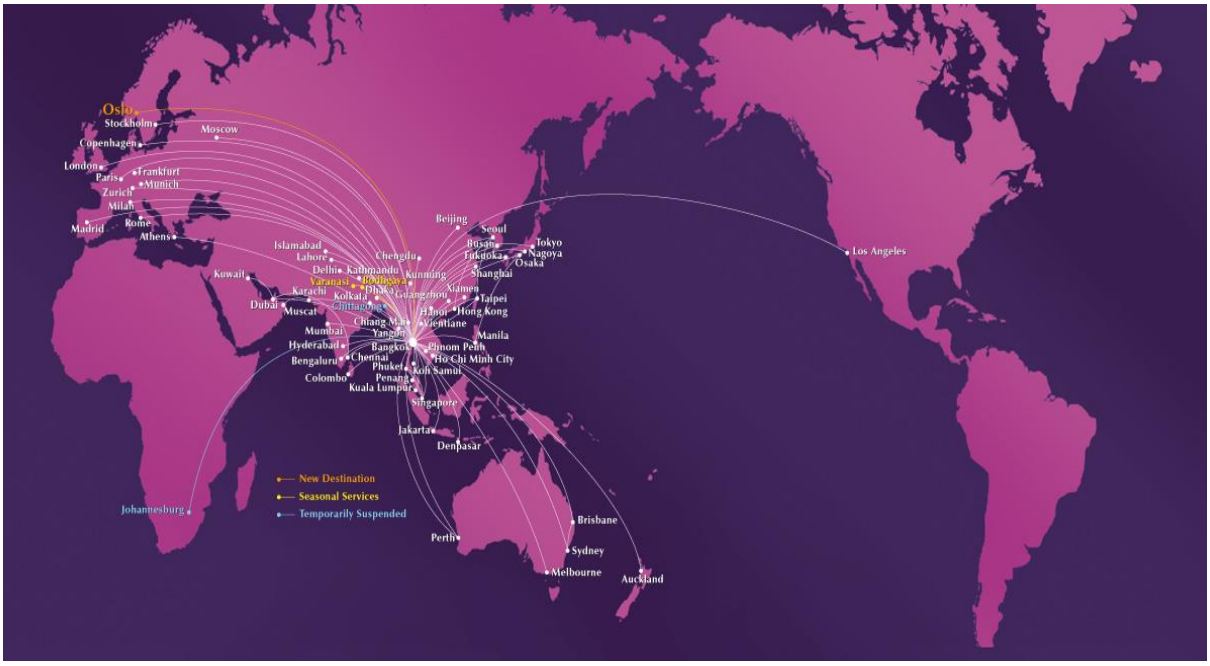
Source: Turkish Airlines' website

Figure 4. **KOREAN AIR**



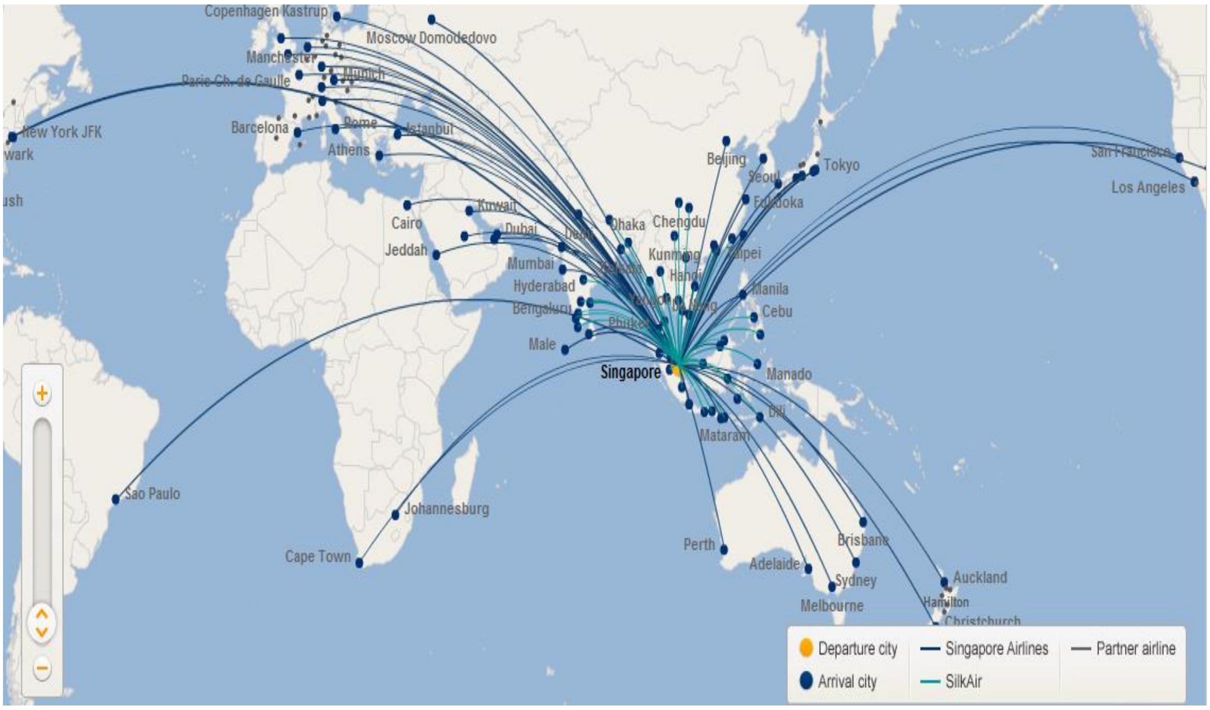
Source: Korean Air's website

Figure 5. **THAI AIRWAYS**



Source: Thai Airways' website

Figure 6. **SINGAPORE AIRLINES**



Source: Singapore Airlines' website

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