

What are the Costs and Benefits of 'Open Skies' in the East African Community (EAC)?

Executive Summary



KEY FINDINGS

- A substantial body of research has repeatedly found that liberalisation has led to increased traffic volumes, greater connectivity and choice and lower fares. Furthermore, the benefits of air service liberalisation extend well beyond the aviation industry and passengers – it contributes to greater trade and tourism, inward investment, productivity growth, increased employment and economic development.
- Quantitative analysis, based on data from East Africa, provided robust and compelling evidence that liberalisation leads to **9% lower average fares** and a **41% increase in frequencies**, which in turn stimulate passenger demand.
- It is estimated that liberalisation between the five EAC countries could result in an additional **46,320 jobs** and **US\$ 202.1 Million per annum in GDP**.

Research Objectives

In 1999, the Yamoussoukro Decision (YD) was adopted out of recognition that the strict regulatory protection that sustains national carriers has detrimental effects on air safety records, while inflating air fares and dampening air traffic growth. The Eastern Africa Community (EAC) has elected to revise Bilateral Air Service Agreements (BASAs) to align with the principles of the YD.

However, implementation of YD remains pending although there has been tangible progress in other relevant matters, such as the establishment of joint air safety and security agencies. One of the factors contributing to the slow take-up of YD's principles is a lack of clear and specific information regarding the impacts of enacting such liberalisation.

As such, this study aims to close some of the information gaps around the impact of implementing the YD in East Africa.

Research Methodology

To address the research problem, the study is comprised of three elements:

1. **Synthesis of Evidence** - a comprehensive literature review was conducted on the aviation and economic impacts of air service liberalisation, with particular focus on research and papers specific to East Africa and the African continent.
2. **Stakeholder Consultations** – wide ranging qualitative interviews with stakeholders were conducted across the five study countries including representatives of the air industry and tourism associations, aviation authorities, airlines, investment authorities, tourism operators, government ministries, hotel associations and cargo representatives.
3. **Economic Modelling** - using data collected for the EAC region, quantitative analysis was undertaken to quantify the impacts of liberalisation. This analysis provided a unique insight into how previous liberalisation (of BASAs) in East Africa had impacted the local aviation market. From this analysis, it was possible to estimate the aviation sector and wider economic impacts of liberalising the remaining BASAs using a model specific and tailored to the EAC.

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Key Results & Implications for the Region

The *synthesis of evidence* demonstrated fairly consistently that BASA liberalisation resulted in increased frequencies, routes and connectivity, increased traffic and supported economic growth

A substantial body of evidence has developed over the last 10-15 years examining the impacts of BASA liberalisation for both the aviation sector and the wider economy. Repeatedly, these studies from around the globe found that liberalisation allowed new carriers to enter the market and existing carriers to better respond to demand. This resulted in lower fares for passengers and more travellers being able to access air services. However, more recently, research has found similar effects occurring in Africa where governments have chosen to remove restrictions on air services.

The benefits of air service liberalisation extend well beyond the aviation industry and passengers – it contributes to greater trade and tourism, inward investment, productivity growth, increased employment and economic development. A body of research has developed demonstrating a clear linkage between aviation growth and growth in tourism, trade, investment and the economy (i.e., growth in employment and GDP).



The *qualitative stakeholder interviews* revealed widespread dissatisfaction with current air services in EAC and general support for BASA liberalisation as a means to improve air services

Stakeholders frequently cited examples of where the current aviation services are limiting trade, tourism and business, and many recognised that BASA liberalisation would help remove these limitations and benefit the economy. There was unanimous agreement amongst stakeholders that trade and tourism would be significant beneficiaries from liberalisation. Tourism in particular is an industry dependant on good air access to a country and its associated offerings. Respondents noted that the ease with which goods could move through the EAC region would significantly boost trade and unlock additional opportunities and markets. Business development and investment is another area that would grow since it would allow for easy and affordable movement. One of the main challenges in many East African countries is poor transport infrastructure, which hinders swift movement and increases costs of doing business and limits investment. Improvements in air service from liberalisation would lead to savings in time and ultimately catalyse trade and investment.

Some respondents raised potential dis-benefits that may come along with liberalisation. Some stakeholders expressed a concern that liberalisation could lead to larger, better-capitalised foreign carriers “squeezing out” smaller, less-well-funded local carriers. However, it was generally viewed that the introduction of greater competition would ultimately be beneficial by offering existing carriers new market and investment opportunities and encouraging them to undertake greater efficiencies.

“When it comes to tourism, we are still operating with a system not designed to offer affordable services and products to EAC residents. It is time to recognize the potential of East Africans as a viable source market; they should be encouraged to travel within their own country and region.”

- Tourism Association

Quantitative analysis, based on data from East Africa, provided robust and compelling evidence that liberalisation leads to lower fares and higher frequencies, which in turn stimulate passenger demand

The empirical analysis of the impacts of air service liberalisation used a gravity model approach to modelling air traffic between nations, based on data collected for each of the five study countries. The analysis allowed an examination of the factors affecting air traffic between nations including market factors, economic and, of most interest to this research, the degree of liberalisation of the BASAs. In terms of the key results for liberalisation, the following significant results were found:

- Fully liberalising restricted routes reduces average fares by 9% on average (all else being equal).
- Fully liberalising restricted routes increase frequencies by 41% on average (all else being equal).

Furthermore, the results showed that that partial liberalisation in not effective in achieving equivalent impacts. Only once all the major restrictions are removed from BASAs is there a substantially impact on fares and frequencies.

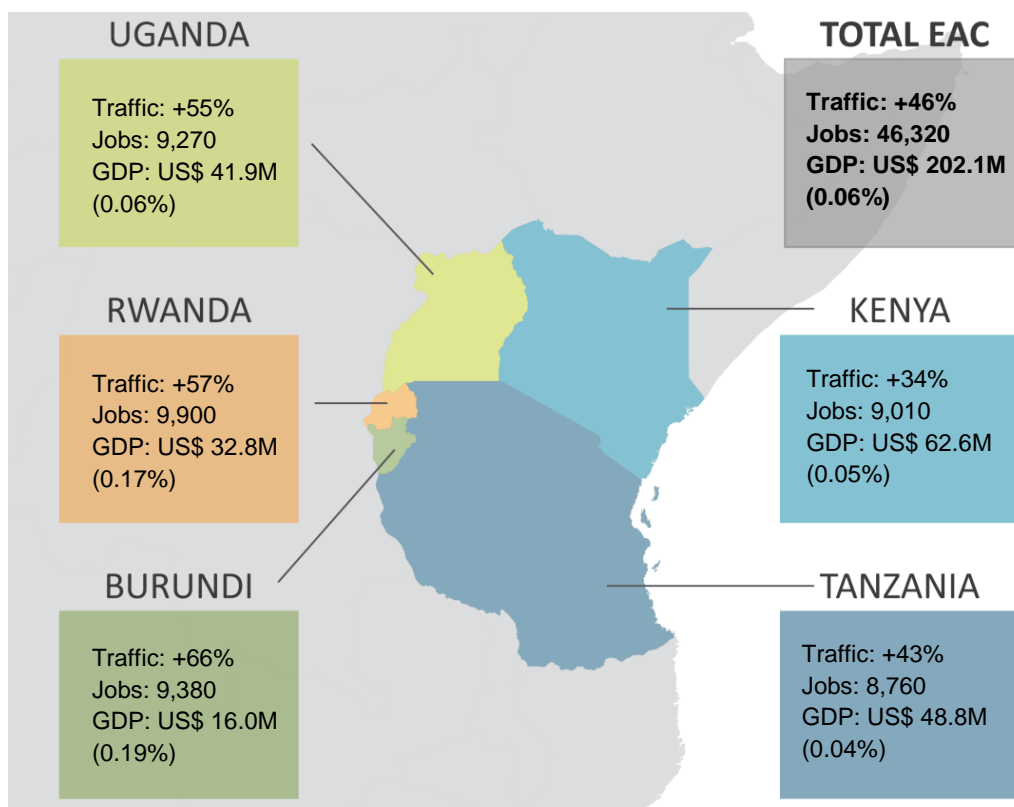
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Economic Impact of Liberalisation within the EAC

The gravity model was used to estimate the impact resulting from complete liberalisation of BASAs from the five EAC countries. This includes not just the impact on traffic and air services but also on the wider economy. The analysis assumes that all five countries are able to sign 'open skies' BASAs, along with improvements in taxation and infrastructure to fully maximise the benefits of liberalisation. The resulting impacts on traffic volumes, employment and GDP and are summarised in the diagram below.

Across the five EAC countries, liberalisation between the countries is projected to result in an additional 46,320 jobs and US\$ 201.1 Million additional GDP each year (0.06% of the total GDP of these countries).



Key Conclusions and Recommendations

- The synthesis of evidence consistently demonstrates that BASA liberalisation has resulted in increased frequencies, routes and connectivity. Frequently, liberalisation has allowed new carriers to enter the market and existing carriers to better respond to demand.
- The economic analysis demonstrates that increased air service and traffic resulted in positive benefits for the total EAC economy – it contributes to greater trade and tourism, inward investment, productivity growth, increased employment and economic development; and is supported by a range of regional stakeholders.
- While there are concerns in some corners that liberalisation may harm existing air carriers, liberalisation also offers a means to restructure the carriers and increase profitability by expanding into new markets, accessing a wider pool of investment and through consolidation.
- Given the conclusions of the study, we recommend the following actions:
 1. **Implement Open Skies Policy.** The EAC must fully implement YD and enable a multilateral 'open skies' policy.
 2. **Enhance the benefits of liberalisation** by ensuring the taxation of air passengers and air service charges is harmonised across the EAC. Additional recommendations include improving aviation infrastructure, security and facilitating the training of aviation professionals.
 3. **Attract private sector investment.** Remove foreign ownership restrictions to open up access to capital and financing so airlines can refresh fleets and airports can appropriately invest in infrastructure upgrades and capacity expansions.

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