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Pacific Asia Travel Association

ISSUES&TRENDS

POWER OF ALIGNMENT

Helping to rationalise 'the world's most fragmented and most global industry', airline alliances are now intensifying their attention on Asia Pacific – the fastest growing aviation market in the world – in the hope of expanding their global presence, with China, India and Japan the focus of their attention.

Strength in Numbers

In 2008 despite a year-on-year drop of 0.6%, the Asia Pacific region achieved the highest market share of global passenger traffic (32.5%), carrying a total of 532 million travellers.

This included 182.4 million international passengers, placing it second after Europe (314.4 million international passengers), and 349.5 million domestic passengers, overtaking North America (334.1 million).

Within the top ten international city pairs six included Asian destinations, of which three were intra-Asian routes.

According to recent forecasts from the world's leading aircraft manufacturers Airbus and Boeing, Asia Pacific is, between now and 2028, likely to see passenger traffic grow at a higher rate than the world average.

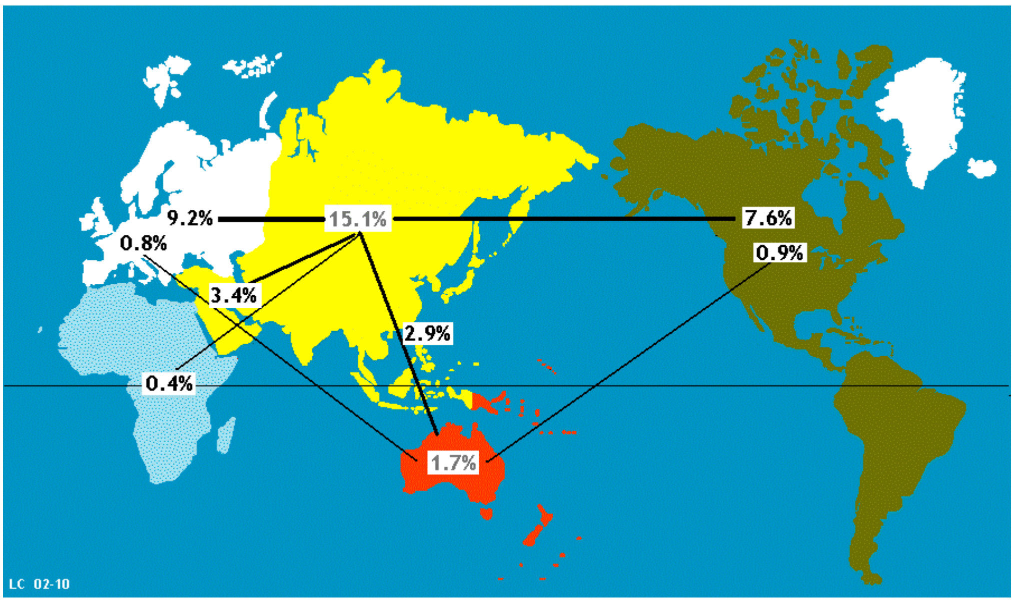
Airbus predicts Asia Pacific will grow by 5.9% per year compared to a global average of 4.7%; Boeing, on the other hand, believes the region will enjoy an average passenger growth of 6.5% compared to a world average of 4.9%.

Unsurprisingly, Boeing believe China will lead the way, with domestic passenger traffic likely to grow 8.6% between 2009 and 2028, while international traffic will, on average, increase 5.8%.

As a result of this growth both aircraft manufacturers estimate that, between now and 2028, the region will take delivery of 8,010 (Airbus forecast) to 8,960 (Boeing forecast) aircraft. China will likely account for about a third of all Asia Pacific orders in this period.

FIGURE 1- IATA Traffic flows from/to and within Asia/Pacific (2008) [1]

Percentage of total scheduled Revenues Passenger Kilometres (RPKs)



1 Source: IATA

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TABLE 2- Boeing Current Market Outlook for Asia Pacific 2009 to 2028[2]

Airline traffic growth by regional flow RPKs in billions	2005	2006	2007	2008	2028	Average annual growth % per year 2008 to 2028
Africa - Southeast Asia	4,7	4,8	5,7	5,6	32,2	9,2
China - China	163,8	182,4	210,7	227,6	1 174,9	8,6
China - Europe	60,9	73,9	77,4	77,9	235,1	5,7
China - North America	40,2	48,5	56,4	57,2	182,3	6,0
China - Northeast Asia	29,0	30,0	35,7	33,3	101,9	5,7
China - Oceania	17,1	19,3	20,4	22,4	71,1	5,9
China - Southeast Asia	48,9	48,6	52,1	50,4	145,7	5,5
Russia and Central Asia - Intra-regional	56,0	57,3	57,7	61,4	177,5	5,5
Russia and Central Asia - International	65,2	66,6	74,6	85,7	232,2	5,1
Europe - Northeast Asia	61,0	61,8	68,3	68,7	163,1	4,4
Europe - Southeast Asia	111,3	110,3	108,3	108,9	327,4	5,7
Europe - Southwest Asia	44,3	54,1	54,3	53,6	174,6	6,1
Middle East - Southeast Asia	33,3	38,3	45,1	45,7	165,0	6,6
Middle East - Southwest Asia	38,3	44,0	48,8	58,2	188,1	6,0
North America - Northeast Asia	126,2	122,4	124,1	122,9	229,7	3,2
North America - Oceania	31,5	32,2	29,5	29,5	89,3	5,7
North America - Southeast Asia	36,5	36,5	42,7	37,4	136,2	6,7
Northeast Asia - Northeast Asia	83,9	84,1	82,0	81,6	167,1	3,6
Northeast Asia - Oceania	25,7	24,6	23,3	20,9	57,3	5,2
Northeast Asia - Southeast Asia	67,1	74,3	79,0	74,1	234,4	5,9
Oceania - Oceania	63,0	67,8	72,6	78,2	184,3	4,4
Oceania - Southeast Asia	60,1	57,3	55,7	65,7	183,3	5,3
Southeast Asia - Southeast Asia	82,4	89,2	96,7	90,0	424,0	8,1
Southeast Asia - Southwest Asia	17,1	19,1	20,0	22,2	100,9	7,9
Southwest Asia - Southwest Asia	25,0	29,5	39,1	44,2	236,4	8,7

2 RPK: revenue passenger km (Source: Boeing)

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Alliances: The answer to a fragmented industry?

Alliances are certainly not a new idea. They have existed for a number of decades, although mostly on a bilateral basis. In Asia Pacific, for example, BOAC (which later merged with British European Airways to form British Airways) and Qantas Empire Airways cooperated on the London-Sydney route as early as the 1930s. Meanwhile, a commercial joint venture involving SAS Scandinavian Airlines Alliances with domestic carrier Thai Airways Company (TAC) gave birth to Thai Airways International.

Global alliances are a logical consequence of bilateral cooperation, but their impact on the air transport industry goes much deeper. In a time of increasing turbulence for the industry, as well as the rising demand for global travel, alliances are perceived as the easiest solution for cost management and improved productivity.

At a state of the industry address in Istanbul in 2008, IATA Director General and CEO Giovanni Bisignani commented that alliances can rationalise "the world's most fragmented and most global industry".

Alliances have certainly gone some way towards bringing together airlines that would have never formed mergers or partnerships due to various issues associated with having an independently operated national carrier.

While there has been some progress to rationalise air transport over the past decade, the scope of such consolidation remains limited. The most significant steps have been:

- The merger of Air France and KLM;
- Lufthansa becoming the main share holder in Austrian Airlines, BMI (UK), Brussels Airlines and Swiss;
- British Airways and Iberia finalising strategic details of their merger this year;
- In developing countries cross-country mergers have been achieved with LAN Group (Chile) taking over various airlines in Latin America and, most recently, between Avianca (Colombia) and TACA (El Salvador and Costa Rica).

Asian airlines are noted for their absence from this list. A handful of merger attempts were made – most notably between Qantas and Air New Zealand, between Qantas and Singapore Airlines, as well as the attempt of SIA to step into the capital of China Eastern – but all failed to materialise. Meanwhile, rumours surfaced in 2008 about a possible link between Qantas and Malaysia Airlines, however this remains unconfirmed.

When it comes to airline development national sensitivity, more so than in Europe or the Americas, seems to be the driving force behind politicians' agendas in the Asia Pacific region – sometimes to the detriment of any rational long-term vision. The involvement of a Japanese carrier with a Chinese carrier, for example, would seem inconceivable, despite the fact that it would likely bring commercial benefits.

Alliances allow airlines to maintain their independence while at the same time enjoying a number of benefits. These include:

- Sharing of costs, eventually resulting in cost reductions
- Enhanced productivity and yield control
- Better traffic feed through members/ hub strengthening
- Improved service quality, including seamless travel experiences and better rewards for customers
- A more attractive commercial product (timetable, frequent flyer programme, lounges, fares)

- Access to common technology platforms
- Global marketing approach
- Global presence or Reach
- Better brand awareness bringing worldwide recognition
- Revenue generator

The 'Big Three'

Four global alliances have emerged since 1997, although only three remain in existence today. The first, Star Alliance, was originally an initiative between Air Canada, Lufthansa, SAS Scandinavian Airlines, United Airlines and Thai Airways International, with Brazilian Varig joining a few months later. Today the alliance is the world's largest with 28 members, with an additional two to three new airlines being added each year (although such a pace of growth is unlikely to continue).

As a large alliance, Star has attained significant awareness amongst the travelling public and enjoys a high degree of recognition thanks to member aircraft bearing the Star Alliance livery and the existence of Star Alliance lounges.

Star Alliance was followed, in 1998, by the Qualiflyer Group. Unlike other alliances, the founding airline Swissair acquired a minority stake in the other members, which included European carriers such as Austrian, TAP Air Portugal and Turkish Airlines. The group later dissolved with the failure of Swissair in 2002.

Next on the scene was Oneworld in 1999. Its founding members were American Airlines, British Airways, Canadian Airlines, Cathay Pacific and Qantas Airways. The airline grouping recently scoured a significant coup in managing to retain Japan Airlines (JAL) as a member, who had previously shown interest in moving to the Delta-led SkyTeam alliance.

Oneworld was the first of the global airline alliances to put in place interline e-ticketing (IET) links between all members of the grouping in April 2005. This allows customers to travel with the convenience of just one electronic ticket throughout the combined network served by the alliance's member airlines no matter how many transfers between these airlines are required along the way.

Last to arrive on the market was Skyteam, which this year celebrates its 10th anniversary. Founding members were Aeromexico, Air France, Delta Air Lines and Korean Air. Despite recently losing Continental Airlines, Skyteam is now the world's second largest alliance and is poised to accelerate its presence with new partners in Asia and Europe. In 2009 the alliance launched its first aircraft designed in Skyteam's livery as well as its first co-branded lounge at London's Heathrow Airport.

Along with full membership, several of the alliances used to offer second-tier, 'associate', or 'affiliate' membership however, both Star and Skyteam recently integrated these affiliates into full-fledged members.

Star Alliance affiliates were generally regional airlines (such as Adria Airways or Croatia Airlines) providing feeder services for a larger carrier. At SkyTeam, Air Europa (Spain) and Kenya Airways became earlier this year full members and have been joined at the end of June by Tarom (Romania). Oneworld has no second-tier members but it extends an airline's membership to include affiliates such as LAN Argentina or LAN Peru for LAN Airlines, or Dragonair for Cathay Pacific in Hong Kong SAR.

While all of the major alliances have experienced exponential growth over the past decade, they have also seen a number of their members leave or even switch to another alliance. Oneworld lost Canadian Airlines after its merger with Air Canada and Aer Lingus, while SkyTeam recently lost Northwest Airlines after its merger with Delta

Air Lines and Continental Airlines. In addition, Star Alliance lost Ansett Australia and Varig due to bankrupty and saw Mexicana switching to Oneworld. The most recent change is due next October when Shanghai Airlines will withdraw from Star Alliance, following the announcement of China Eastern to join Skyteam. Shanghai Airlines merged at the end of last year with China Eastern. The merger between Continental and United Airlines will also cost one membership to Star, most probably by early 2011.

The three main airline alliances now account for around two thirds of the total world airline capacity (ASKs), while unaligned legacy carriers account for around a quarter of world capacity, with low cost carriers making up the rest.

TABLE 3- Comparison of the three main alliances [3]

	Oneworld	SkyTeam	Star Alliance
Date of creation	1999	2000	1997
Number of members	11 + 20 affiliates	13	28
Full Members July 1st, 2010	American Airlines, British Airways, Cathay Pacific, Finnair, Iberia, Japan Airlines, LAN Airlines, Malév Hungarian Airlines, Mexicana, Qantas, Royal Jordanian	Aeroflot, Aeromexico, Air Europa, Air France, Alitalia, China Southern, CSA, Delta Air Lines, Kenya Airways, KLM, Korean Air, Tarom, Vietnam Airlines	Adria, Aegean, Air Canada, Air China, Air New Zealand, ANA, Asiana, Austrian, Blue1, Bmi, Brussels Airlines, Continental Airlines, Croatia Airlines, Egyptair, LOT, Lufthansa, SAS, Shanghai Airlines, Singapore Airlines, South African Airways, Spanair, Swiss, TAM Brazil, TAP Air Portugal, Thai, Turkish Airlines, United, US Airways
Associate members	Lan Argentina, Lan Peru, Lan Ecuador, Comair, Dragonair among others		
Annual passengers (mil.)	335.5	394	627.5
Countries served	146	169	181
Destinations served	871	898	1,172
Daily Departures	9,366	13,000	21,200
Fleet	2,470	1,941	4,025
Number of employees	314,341	316,445	405,000
Revenue Passenger Km	697.02 million	n.a.	1,201.7 million

3 Sources: alliances

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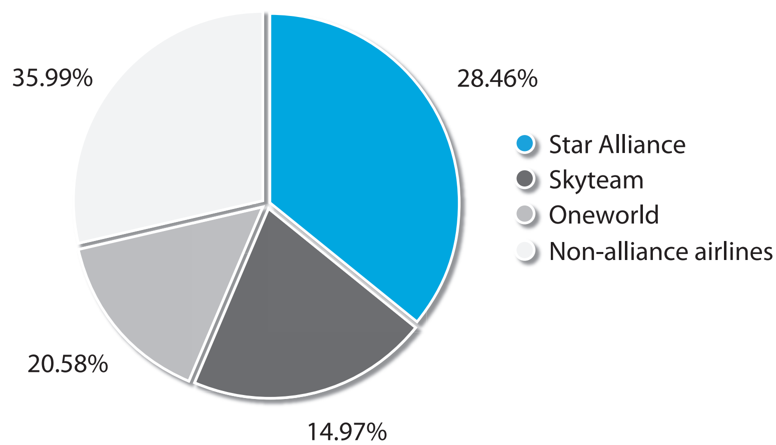
From a simple marketing tool created to rationalise costs, airline alliances have today turned into powerful cash machines, becoming increasingly influential in shaping a country's air transport policy.

In the past couple of years, in particular, airline alliances have proven their worth, with member carriers able to work together in a number of ways including revenue sharing or common promotional/marketing campaigns.

"Our job is to help bridge the downturn and prepare for recovery. Of course, we can't influence fuel costs but we can help our members reduce costs in many other areas without reducing the overall quality of their product. Why should each individual airline invest in the development of a new product when we can do this for all our members? Why should we not buy certain products and services as a team, saving money through larger volumes?" explains Jan Albrecht, CEO of Star Alliance (Source: interview in Star Alliance 'In Focus 2008' brochure).

FIGURE 4a- Market share of alliances in terms of passenger traffic for Asia Pacific in 2008 (calculated from passenger traffic of Asia Pacific airlines only)[4]



4 Source: IATA

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FIGURE 4b- Market share of alliances in terms of monthly seats in Asia Pacific in April 2010 (calculated for intra-Asia Pacific traffic only)[5]

The relative weak performance of alliances is due to the absence of large airlines, especially from China and South Asia.

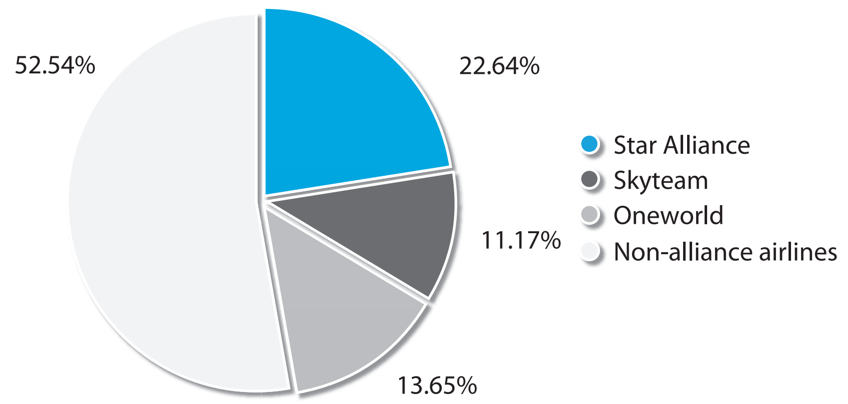
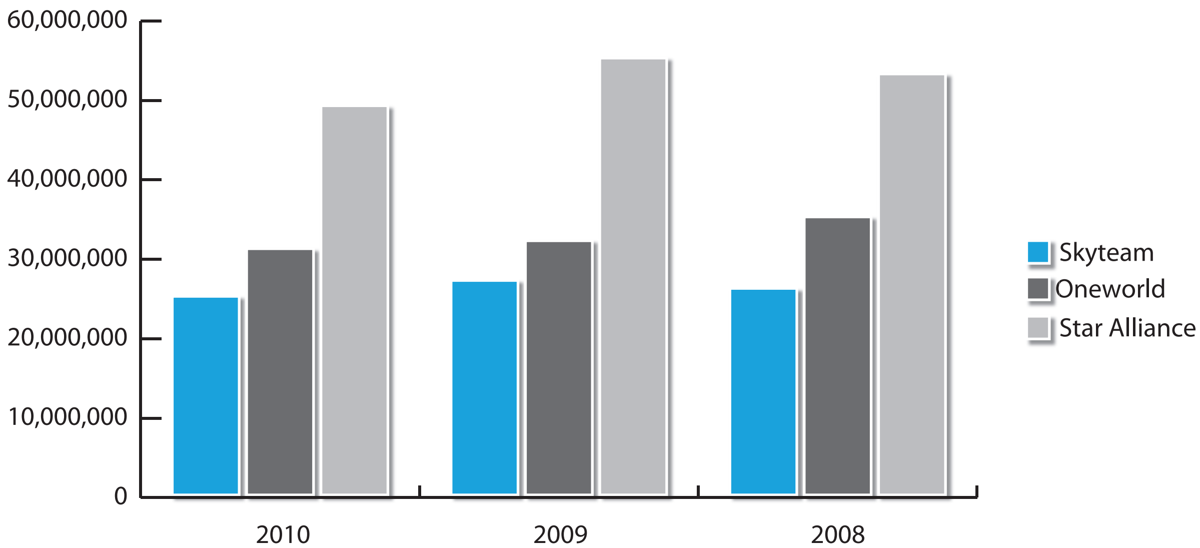


FIGURE 5: Evolution of yearly seat capacity of alliances in Asia Pacific (month-on-month basis April 2008 to April 2010)[6]



5&6 Source: OAG Aviation Solutions

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Reducing Costs: The Oneworld example

Speaking in June 2009, during Oneworld's 10th anniversary in Kuala Lumpur, Mr McCulloch highlighted that, thanks to Oneworld's coordination efforts, more than eight million passengers transferred between member airlines' flights in 2008, producing interline revenues within the alliance of US$2.4bn, up 10% compared to 2007. Revenues from Oneworld fares and sales activity in 2008 totalled more than US$850mn, a 25% year-on-year increase.

> *"Alliances today have evolved from a pure marketing tool to a management too"*
>
> **John McCulloch, Oneworld Managing Partner**

Revenue generated by Oneworld grew significantly faster than member airlines' overall passenger revenues which, collectively, increased just 3.5%.

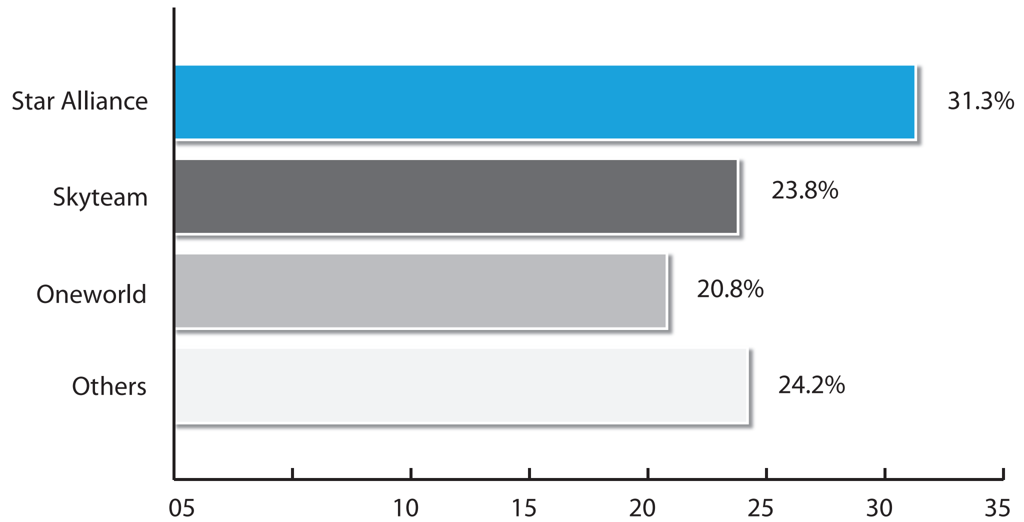
During its first decade the alliance generated a total of US$5bn for its member airlines through alliance fares and sales products, with revenues rising by 330% from the US$200mn reported in the alliance's first year.

By comparison, revenues generated by the alliance's member airlines from their passenger activities over the same 10 year period have risen 96%, from a collective US$39bn in 1999 to US$75bn in their latest full financial years.

Interline revenues generated within Oneworld - from passengers transferring between flights operated by one member airline to those of a partner in the alliance - have also grown faster than its member airlines' passenger revenues, up 153% during the 10 years of Oneworld's existence from less than US$1bn in 1999 to US$2.4 bn in 2008.

In 2009 the alliance launched a new project of cost reduction for all its member airlines under the acronym RACE – Reducing Airline Costs Effectively.

FIGURE 6- Alliances Operating Revenue Shares 2008[7]
Operating revenues of UPS and FedEx have been removed from IATA total operating revenues to calculate shares



7 Source: IATA-Star Alliance In focus 2008

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Asia Pacific: Full of promise

There are still a large number of network airlines in the Asia pacific region that remains outside an alliance. According to data collected from an IATA statistics report (WATS 2009), in 2008 Asia Pacific airlines outside an alliance carried 217.2 million passengers.

Of the top 50 biggest airlines in Asia Pacific in 2008, as ranked by passenger traffic, eight carriers with over nine million passengers per annum (each) were not part of an alliance (Source: IATA 2008 annual report/WATS).

The largest of these is China Eastern Airlines with 37 million passengers carried in 2008, while Hainan Airlines (14.5 million) and Malaysia Airlines (12.5 million) should also be considered important players.

TABLE 7- Asia Pacific non-alliance member airlines (as at December 2009)[8]

Airline	Country	Total passengers In 2008	Market share Domestic passengers In 2008
NORTHEAST ASIA			
China Eastern Airlines	China	36,923,272	82.19%
Hainan Airlines	China	14,480,431	98.08%
Shenzhen Airlines	China	11,839,549	97.82%
Xiamen Airlines	China	9,586,963	97.02%
China Airlines	Chinese Taipei	9,328,333	-
Sichuan Airlines	China	6,700,655	99.8%
Eva Air	Chinese Taipei	5,765,729	-
Shandong Airlines	China	5,276,955	96.5%
TransAsia	Chinese Taipei	2,212,794	69.25%
Air Macau	Macau SAR	1,866,459	-
SOUTHEAST ASIA			
Malaysia Airlines	Malaysia	12,631,094	39.84%
Garuda	Indonesia	10,172,252	76.17%
Vietnam Airlines	Vietnam	8,764,459	60.32%
Philippine Airlines	Philippines	7,641,304	54.32%
Silk Air	Singapore	1,936,782	-
Royal Brunei Airlines	Brunei	1,096,568	-
Bangkok Airways	Thailand	2,418,223	65.72%
Lao Airlines	Lao PDR	352,059	50.54%
Myanmar Airways	Myanmar	117,331	-

8 Source: IATA WATS 2009
In italic are airlines with confirmed integration into an alliance in 2010 or 2011° estimates

Airline	Country	Total passengers In 2008	Market share Domestic passengers In 2008
SOUTH ASIA			
Jet Airways	India	11,672,406	74.71%
Air India	India	11,021,358	43.83%
Kingfisher Airlines	India	7,546,732	98.21%
Pakistan Airlines	Pakistan	5,605,774	39.21%
Jet Lite India	India	3,435,117	100.00%
Sri Lankan	Sri Lanka	2,969,687	-
Biman	Bangladesh	1,364,792	8.35%
Royal Nepal Airlines	Nepal	470,000°	-
CENTRAL ASIA/SIBERIA			
Siberia Air	Russia	5,366,752	76.43%
Uzbekistan Air	Uzbekistan	2,033,933	20.93%
Vladivostok Air	Russia	802,314	24.13%
MIAT	Mongolia	277,112	4.53%
PACIFIC/ US PACIFIC COAST			
Hawaiian Airlines	USA	7,848,572	98.49%
Alaska Airlines	USA	6,787,046	79.45%
Air Pacific	Fiji	931,763	-

Chinese airlines are particularly under-represented in alliances. Beside China Eastern Airlines, large carriers such as Hainan Airlines, Sichuan Airlines, Shandong Airlines, Shenzhen Airlines and Xiamen Airlines are still not part of an alliance.

The likely reason is that many of theses airlines continue to focus on domestic routes and thus have little reason – or incentive – to join a global air alliance. Shenzhen Airlines international passenger traffic, for example, represented just 1.9% of its total of over 11.82 million passengers in 2009. At Sichuan Airlines, international traffic accounted for an even lower 0.1% of total passengers.
Of the Chinese carriers, next to join an alliance is China Eastern Airlines while Hainan Airlines has not yet taken a decision.

China Eastern is Shanghai's largest international carrier. In April 2010 (source: OAG) China Eastern represented 40.7% of all monthly capacities available on departures from Shanghai to the rest of Asia Pacific, the equivalent of 1.069 million seats. This represents a lead of 33% over Star Alliance capacities out of Shanghai (0.708 million seats).

China Eastern officially announced in April joining Skyteam and this will certainly have a negative impact on Star Alliance's current capacity in the region. With China Eastern joining Skyteam, Star Alliance will lose next October Shanghai Airlines (which join the alliance in 2007) following its merger with China Eastern by January 1st, 2010.

"We have always been aware that mergers could happen on a regional basis and could then affect the alliance composition in specific markets. For example, Delta/Northwest merger pushed Continental to reconsider its alliance membership," explains Markus Ruediger, Star Alliance Media Relations Director.

Hainan Airlines currently flies to 20 international destinations out of Beijing, Haikou and Nanning. Regionally, the airline already serves Bangkok, Hanoi, Korea (ROK) and Japan and connects to secondary markets overseas. Following China Eastern joining Skyteam, Oneworld Managing Director John McCulloch confirmed during IATA Annual Meeting in Berlin that " our alliance is not interested to consolidate our position in Mainland China. We deny any talks with Hainan," he told. However, synergies would be easy to build: Hainan flies for example in Europe to Berlin, Budapest and Brussels, as well as seven cities within Central Asia and Russia. With Air Berlin and S7 (Russia) soon to join Oneworld and Malev (Hungary) already a member, network's complementarity with Hainan Airlines would be easy.

With a relatively recent full liberalisation of its skies (in 2003) and, with the bulk of air traffic still being domestic, few Indian carriers had built a relationship wiht alliances. Only India's oldest airline and national carrier Air India was, in 2007, invited to join Star Alliance.

"We expect Air India to join by the end of the year. AI will add its domestic and regional flights to the Star Alliance network, but also add their key international routes. From our perspective, India's significant domestic network is what will bring a large improvement to our network coverage," explains Star Alliance's Markus Ruediger.

Air India has the largest share of international passenger traffic at 43.8%, compared to 25.3% for Jet Airways and less than 0.1% for Kingfisher Airlines. The latter just announced its integration into Oneworld, bringing 58 Indian destinations into the alliance.

Following new routes to Bangkok, Hong Kong SAR and Singapore, Kingfisher commenced flights between New Delhi and London at the end of March 2010. It is also currently negotiating a code share agreement for its UK route with British Airways.

This leaves Jet Airways as the last major Indian carrier not to have joined an alliance. One alliance to watch in this regard is SkyTeam, as it is the last global grouping without a partner in the Indian sub-continent. The only difficulty would come with Jet Airways' European hub operations at Brussels Airport, which is a stronghold of Star Alliance. Jet Airways currently flies up to six times a day to both India and North America via Brussels. Jet Airways can already easily feed Delta Air Lines primary US hub in New York. In Europe, it would be however forced to switch its network strategy, abandoning Brussels to favour Skyteam major hubs in Amsterdam, Paris, and eventually Prague and Rome.

Beside its extensive India network, Jet Airways could further boost SkyTeam's presence in the Middle East, the rest of South Asia and Southeast Asia. This would help close the existing gap between India on one side and Indonesia and Vietnam – its new or future partners in Southeast Asia - on the other side, as there are currently no flights offered between India and these countries.

For other countries within South Asia, political uncertainties have so far dampened any desire from global alliances to form partnerships with national carriers from countries such as Bangladesh, Nepal, Pakistan and Sri Lanka.

Political reasons are also behind the absence of Taiwanese carriers in alliances. Until mid-2008, China has pressured its partners to limit landing rights to carriers originated from Chinese Taipei. However, authorisation by both China and Chinese Taipei to allow scheduled cross-Straits flights has helped to 'normalise' the situation of Taiwanese carriers. Reports have already suggested that China Airlines is looking at SkyTeam with the backing of China Eastern. " We would then become the largest alliance in Greater China," confirms Pierre Henri Gourgeon, Managing Director for Air France-KLM.

ISSUES & TRENDS

Most surprising is the Alliance absence of some national carriers in Southeast Asia such as Garuda Indonesia, Malaysia Airlines, Philippine Airlines and Royal Brunei. After Singapore Airlines and Thai Airways International - the two carriers with the busiest airports in the region - entered into the Star Alliance, there was little interest from other alliances to entice the remaining carries in the region.

Asked about the relatively low interest to take on new carriers in Southeast Asia, John McCulloch from Oneworld justifies its decision saying that yields still remain low in the region. Northeast Asia - China, Japan and Korea (ROK) - certainly has a better balance between business, premium and leisure traffic.

Nevertheless, Southeast Asia still has a large potential to seduce alliances. Malaysia Airlines and Garuda carry over 10 million passengers a year and benefit from a very strong domestic network. Meanwhile, Philippines' national carrier PAL records close to eight million passengers per year. Jakarta, along with Kuala Lumpur and Manila also have many geographical assets as future alliance hubs.

Kuala Lumpur is particularly well positioned, sandwiched between the two major Star Alliance hubs of Bangkok and Singapore, and offers the same proximity to West and South Asia. It can also compete as a regional gateway to the Indonesian archipelago, Thailand and Cambodia as well as to Australia. Integrating Malaysia Airlines into an alliance would help counter Star Alliance's predominance in the region.

Oneworld would probably be the most likely partner as it is still relatively absent from the region; Oneworld's total monthly seat capacity in Southeast Asia in April 2010 stood at 563,678 (calculated from OAG database - total departures from Southeast Asia's 17 largest airports and capital city airports) compared to 2.27 million seats for Star Alliance and 296,800 seats for SkyTeam for the same month[9].

SkyTeam just boosted its presence in the region with the integration of Vietnam Airlines, which adds a further 541,436 seats, taking the alliance's monthly seat capacity to 838,337. And, while no official announcement has been made, Garuda is expected to join SkyTeam by 2011 or latest by 2012. If this were to occur the alliance's monthly seat capacity would rise even further to 1.52 million.

With the addition of Vietnam Airlines and Garuda the alliance's total market share in intra-Asia Pacific traffic would reach 56.96% in Ho Chi Minh City, 68.5% in Hanoi, 34% in Jakarta and 27.5% in Denpasar (Bali). The alliance would also become the largest in Phnom Penh (18.91%) and would be on par with Star Alliance in Vientiane (calculations based on OAG monthly seat capacity for April 2010).

Such rapid growth by SkyTeam would leave Oneworld with little option to look for a partner to raise its stakes in the region. Manila could act as an ideal base between Northeast and Southeast Asia as it is mostly reachable within a three to four hour flight range from all ASEAN capitals, as well as from most large cities in China, Japan and Korea (ROK).

Jakarta's position as a hub is probably less favourable than Kuala Lumpur or Manila, however, as with China, the inclusion of an Indonesian partner would give an alliance access to the huge Indonesian domestic market – 49.5 million passengers carried in 2009 on domestic and international routes by domestic carriers (source: Indonesian Civil Aviation). Jakarta can then be positioned as a gateway to the country as well as to the Pacific area (Australia, New Zealand, PNG and Timor Leste).

9 Source: OAG

FIGURE 8 Passengers traffic by geographical segment in Asia Pacific for independent airlines in 2008[10]

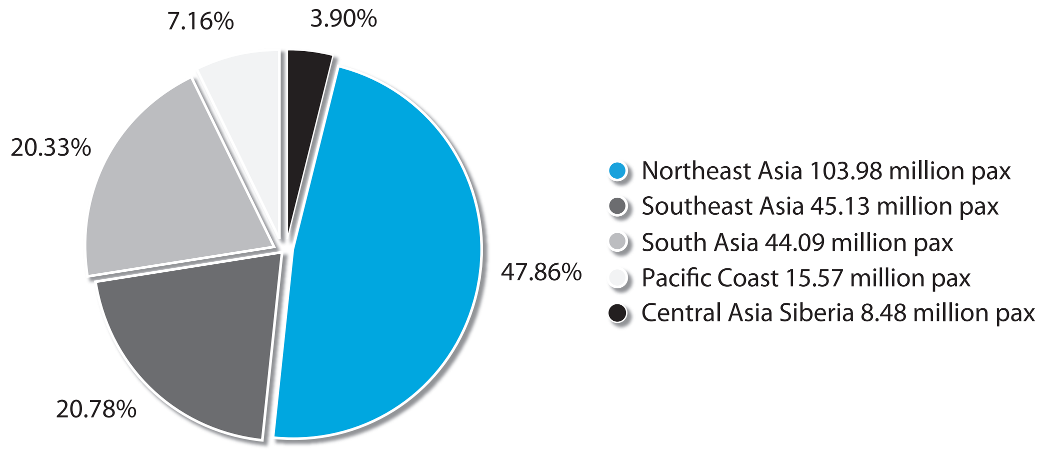


TABLE 9- Presence of alliances in Asia Pacific in terms of monthly seat capacity (April 2010) at major hubs[11]

Star remains clearly the dominant alliance in the region offering the highest number of seats at 11 major airports, followed by Oneworld with five airports and SkyTeam with two.

10 Source: IATA WATS 2009
11 Source: OAG; Graphics: Luc Citrinot

Battle for Influence

With promising signs of a return to growth after the 2009 slump, airline alliances are keen to expand in Asia Pacific.

While Star Alliance will most likely continue its dominant position, SkyTeam is well placed to play catch up with its plans to integrate more carriers until 2012.

After it succeeded in securing Japan Airlines' membership, Oneworld managed to lure Kingfisher from India. For the moment at least, it has abandoned the idea of integrating a Southeast Asian airline but this gap in its presence could eventually be filled by Jetstar. The latter is considered as the 'value-based network carrier' of Qantas with bases in both Australia and Singapore. Although Jetstar is not yet a member of Oneworld it does have a number of service synergies with its parent company – and alliance member – Qantas and concluded already some code share agreements with Oneworld members (JAL for example).

Jetstar recently signed a partnership with Changi Airport (Singapore) to develop its hub and spoke activities. The airline, which currently flies to 20 destinations, plans to grow its capacity by almost 50% with the delivery of three new Airbus A320 for its Singapore base. It just announced new flight to Auckland and Melbourne.

The next two years or so will see the three big alliances continue to battle for supremacy within the region, with China, India, Japan and possibly Indonesia the focus of their attention.

Earlier this year news headlines were abuzz with the possible defection of Japan Airlines from Oneworld to SkyTeam. Both American Airlines (part of Oneworld) and Delta Air Lines (SkyTeam) stepped up their offers of financial to help the beleaguered Japanese carrier in an attempt to win JAL management's support.

An official release from Oneworld dated December 2009 stated that, to reinforce their commitment to retaining JAL as a valued, full member, all other alliance members had put together a "total alliance value proposition" for JAL totalling some US$1.8bn of investment and additional revenue, which outstripped by threefold any other offer to lure JAL away.

The detailed Oneworld package included:

- Invest in the restructuring of JAL through a link with the TPG Investment Group – a specialised investor in the airline industry which, with American Airlines, would be willing to provide funding of up to US$1.1bn if accepted by the airline and the Japanese government.

- Develop an anti-trust immunised (ATI) joint venture agreement across the Pacific with American Airlines to be filed immediately after an open skies agreement is reached between the government of Japan and USA. This would represent, over a 10 year period, additional revenues of some US$700mn on a net present value basis.

- Expand co-operation with the two European carriers serving Japan - British Airways and Finnair to provide JAL with substantially improved access to Europe over two of the continent's most attractive gateways for Japanese travellers, London Heathrow and Helsinki. British Airways (BA) already proposed a far more extensive co-operation with JAL, including more extensive code-sharing across each other's networks.

- Develop its presence in the attractive Latin America market through expanded relationships with Oneworld partners LAN and Mexicana. Mexicana recently received approval to place the JL code on its Vancouver-Mexico City flights, following JAL's decision to suspend its own flights.

- Increase code-sharing with other Oneworld members, building revenue for JAL still further. Iberia has proposed to JAL an expansion in the number of destinations covered by their code share agreement. Talks with a similar aim are also currently underway between Cathay Pacific Airways and JAL.
- Identify opportunities for increased airport co-location for JAL alongside its partners at more key airports worldwide, making it easier for passengers to transfer between the airline's flights and those operated by its alliance partners, strengthening its competitive positioning still further.
- Draw on Qantas' expertise in developing its value-based airline Jetstar and its two-brand strategy. Qantas has offered JAL full access to this expertise should it be interested in drawing upon it.

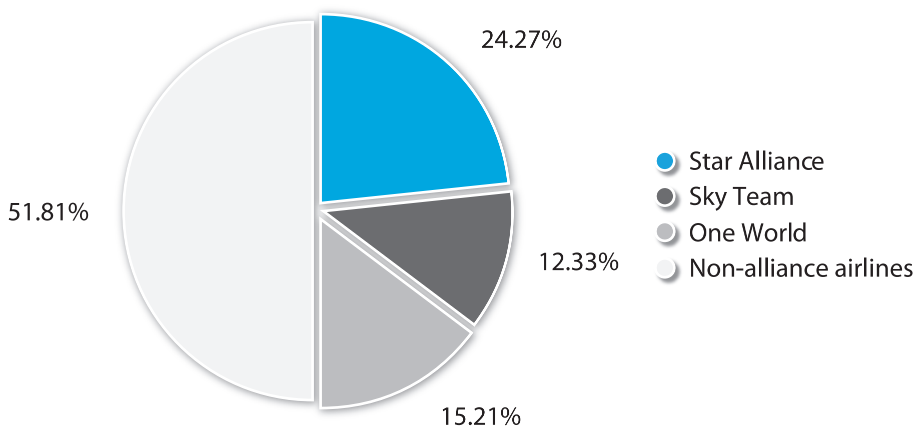
Japan Airlines finally chose to stay within Oneworld by justifying that it would be less costly to retain its current partnership and simpler for its passengers. As the Japanese carrier entered into a dramatic restructuring, it is keener than ever to use the proposed synergies from its Oneworld membership. For example, JAL – in partnership with American Airlines –applied for Antitrust Approval on Trans-Pacific routes at both US and Japanese authorities, an agreement which, if accepted, could also be extended to Cathay Pacific.

The battle over Japan Airlines and the involvement of other Oneworld members clearly shows the role alliances can play in rationalising air transport in the region.

In Japan another battle recently emerged surrounding new times given to US carriers at Tokyo's second airport in Haneda, following the signing of an open skies agreement between Japan and the United States.

With Tokyo Haneda airport opening next October to international traffic, Delta Air lines has been seeking exclusive access to this airport by taking all four available slots for US carriers. In justifying its demand for four new routes out of Haneda, the alliance card was once again being put into play. Delta explained that without those flights, Skyteam would be the only alliance without a presence at Haneda as it has no partnership with a Japanese carrier. Finally, Japan approved two daily flights for Delta to Los Angeles and Detroit, helping SkyTeam to achieve its coveted presence in the Haneda-US market.

FIGURE 10 - Market shares of alliances in monthly available seats within Asia Pacific, including possible future members in 2010 and 2011° (base: April 2010)[12]



12 Source: OAG Aviation Solutions ° including Air India for Star Allianceincluding Kingfisher for Oneworld. If China Eastern joins Oneworld the alliance's market share within Asia Pacific would grow further to reach 16.82%. Including Vietnam Airlines and Garuda for SkyTeam

Perfect Balance: Can Oneworld and SkyTeam loosen Star's grip on the region?

Holding the largest market share, with 26 out of a total of 41 airports in the region, Star dominates intra-Asia Pacific capacity and it seems unlikely the alliance's position will be challenged in the near future. In comparison, Oneworld dominates at 12 airports, while SkyTeam at only three. With the addition of Vietnam Airlines SkyTeam gains meanwhile another three airports (Hanoi, Ho Chi Minh City and Phnom Penh), and with Garuda the alliance would become the biggest player in Jakarta, Denpasar and Surabaya. With China Eastern opting for Skyteam, Star Alliance will lose its leading position at Shanghai Pudong and Hongqiao airports.

At those airports dominated by non-aligned carriers, the influence of alliances remains limited; the largest alliance does not generally exceed 17% of all seats available. Only a few cities have two alliances offering a similar number of seats. Tokyo Narita is one such airport, with an almost perfect balance in seat capacity between Oneworld (34.8% market share) and Star Alliance (34.2%). A relatively good balance of power can also be found at Seoul Incheon, Nagoya and in Colombo, albeit at a very low level for the latter.

In the future, India may be the best hope of achieving a perfect balance in seat capacity with Air India joining Star, Kingfisher joining Oneworld and Jet Airways intergrating into SkyTeam. The market share of each alliance in both Delhi and Mumbai would be as follows: in Delhi, Star would have 42.1% of all seat capacity for intra-Asia Pacific flights, followed by Oneworld, with 18.9% and SkyTeam with 16%; in Mumbai, Skyteam would be dominant with 26.3% of total seat capacity, followed by Star with 20.3% and Oneworld with 17.9%[13].

TABLE 11- Market share of alliances in monthly available seats within Asia Pacific by destinations (base: April 2010). Calculations for departures out of 41 airports in Asia Pacific (in %)[14]

Country	Destination	Star Alliance	SkyTeam	Oneworld
China	Beijing	51.67	18.00	3.13
	Shanghai	26.94	13.78	6.49
	Guangzhou	15.94	62.48	1.44
	Chengdu	43.95	10.43	0.82
	Hong Kong SAR	12.81	4.47	51.14
Chinese Taipei	Taipei	8.01	3.05	17.13
Korea (ROK)	Seoul Incheon	38.59	41.52	5.10
	Pusan	11.75	53.09	2.98
Japan	Tokyo Narita	34.19	13.74	34.83
	Osaka Kansai	39.40	11.73	28.45
	Nagoya	44.42	9.51	36.26
Philippines	Manila	5.75	3.67	6.13
	Cebu	1.22	3.37	4.20
Vietnam	Ho Chi Minh City	10.68	3.28	3.67
	Hanoi	8.13	3.38	2.81
Cambodia	Phnom Penh	13.96	3.61	0.44
Lao PDR	Vientiane	20.70	0	0
Thailand	Bangkok	44.51	3.70	6.44
	Phuket	32.92	2.65	2.96
Myanmar	Yangon	16.56	0.91	0

13 Source: OAG data April 2010
14 Source: OAG Aviation Solutions Feb 2010

Pacific Asia Travel Association

Country	Destination	Star Alliance	SkyTeam	Oneworld
Malaysia	Kuala Lumpur	2.99	1.37	2.41
	Kota Kinabalu	0.92	0.39	0.85
	Penang	1.82	1.55	4.34
Singapore	Singapore	40.06	1.85	8.22
Indonesia	Jakarta CGK	4.94	1.34	1.84
	Denpasar	2.43	2.76	4.93
	Surabaya	0	0	1.56
Brunei	B.S. Begawan	5.69	0	0
India	Delhi	3.14	0.26	1.61
	Mumbai	2.66	0.26	1.28
	Bangalore	3.69	0	1.60
	Kolkata	2.96	0	0
Sri Lanka	Colombo	8.83	0	6.86
Nepal	Kathmandu	7.46	2.85	0
Uzbekistan	Tashkent	4.75	0	0
Australia	Sydney	7.59	1.02	42.79
	Melbourne	7.06	0.50	37.68
	Brisbane	6.24	0.33	42.57
	Perth	6.93	0	52.23
New Zealand	Auckland	59.99	9.65	10.87
	Christchurch	65.48	0	2.12

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