

# Annual Report - 2010

Arab Air Carriers Organization  
43<sup>rd</sup> Annual General Meeting – Cairo



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## Arab Air Carriers Organization 43<sup>rd</sup> Annual General Meeting – Cairo

### **AACO: New Vision ...New Thrust**

Over the last term, AACO has set a new vision, mission, and set of objectives that were approved by AACO 42<sup>nd</sup> AGM Resolution number 7/2009. Our vision reflects our long term plan to establish our position as one of the leading airline associations that strives to serve its member airlines, and that differentiates itself by being a tool for cooperation, assisting its member airlines in achieving considerable economic returns through joint initiatives. AACO has reworked the internal methodology and workflow to ensure the achievement of the new objectives.

### **Vision**

To stand out globally as THE association that serves with dedication the Arab airlines and to be instrumental in dealing with an evolving aviation industry.

### **Mission**

To serve the Arab airlines, represent their common interest and be the catalyst for their cooperation.

### **Objectives**

- To support the Arab airlines' quest for highest safety and security standards
- To support the Arab airlines' quest for developing their environmental policies for processes in harmony with the environment
- To actively contribute in the development of human resources
- To interact with the regulatory bodies to support and protect the interests of the Arab airlines
- To launch and serve joint projects between member airlines with the objective of reducing their costs, increasing their revenues and embracing best practices
- To provide forums for members and for industry partners to enhance the knowledge base and improve cooperation amongst them
- To reflect the positive image of The Arab Airlines Globally

AACO's modus operandi is to initiate and implement Specific, Measurable, Attainable, Relevant, and Time-bound (SMART) synergic targets. AACO encourages cooperation among its members by initiating and maintaining these targets that serve its objectives.

### **AACO Executive Committee**



#### **Chairman of AACO:**

Eng. Hussein Massoud, Chairman & CEO,  
EgyptAir Holding Company

#### **Members of the Committee:**

Mr. Adel A. Ali, Group Chief Executive Officer, Air Arabia

Eng. Samer A Majali, Chief Executive Officer, Gulf Air

Capt. Sabri Saad Shadi, Chairman, Libyan African Aviation  
Holding Company & Chairman of Afriqiyah Airways

Eng. Khalid Abdullah Almolhem, Director General,  
Saudi Arabian Airlines

Mrs. Ghaida Abdullatif, Vice Chairman - Director General & CEO,  
Syrian Arab Airlines

Capt. Abdulkalek Saleh AL-Kadi, Chairman, Yemen Airways

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When the last AACO Annual Report was presented to the 42nd AGM, the Air Transport Industry was living, along with the global economy, in its deepest crisis in history. After a year of escalating costs due to fuel prices in 2008, the world in 2009 had to endure a financial meltdown that resembled that of 1929. Had it not been for the déjà-vu of 1929, which made it clear that the market economy cannot be salvaged without governmental intervention and support through the injection of huge funds, the 2009 crisis might have had worse ramifications than its 80-year predecessor.

Although the industrialized countries have pumped into the economy at least two trillion dollars, the dark clouds of the economic crisis still loom in the air. Some analysts believe that we are not bailed out entirely from the perils of economic crises, and that there is a sequel. This notion overshadows the outlooks of the private sector, underscoring the need for continued governmental financial stimuli, and requiring continued monitoring of the backbone of the market economy, namely the banking sector.

In 2008 and 2009 air transport industry gurus expected this crisis to be detrimental, or even fatal, to many airlines if no drastic measures were taken to alter the rules of the game, and to allow full cross-border mergers and free market access.

It goes without saying that a paradigm shift in these two areas is essential to the strategic future of the air transport industry, only that the level of urgency in introducing radical treatment was, at least from the governments' view, not at par with the industry's standpoint. Perhaps the traffic growth figures in some regions, especially in the Arab region, Latin America and parts of Asia serve as evidence of the need to take into account that there is not one panacea for all the structural problems of the industry. Indeed, the structure of the air transport industry in each region, and sometimes in each country, must constitute the basis for any analysis of its malaise. Perhaps the burden of the crisis led everyone to believe that radical measures are the remedy, while facts have deviated from the total accuracy of this proclamation.

# Milestones

# Milestones

The Arab Air Transport continued to grow at all levels: it grew in terms of the size of the Arab air transport market producing higher traffic from, to, and within the Arab world, and higher passenger numbers onboard Arab airlines. That growth came in contrast to an industry-wide decline. Traffic onboard AACO members measured in RPKs, increased by 10% in 2009 over 2008.

Numbers clearly establish that while crises may indeed create obstacles to growth, cost challenges, revenue decline and more labor issues, they may present airlines that wish to broaden their passenger base opportunities through promoting quality and added-value services, and for the airlines to take advantage from the travel value-chain to provide travelers with a downright quality experience at the airports, in the air, in transit where applicable, all the way to the destination. Drafting a one-dimensional aspect of the industry's grievances and relief-measures may sometimes lead to incorrect analysis and undesirable outcome.

At the end of the day, this crisis taught us that the world is still founded on the "nation state" concept, with all that this term conveys in dimensions of sovereignty, national interests and strategic depth, and more. No industry can surpass the geopolitical and economic realities. The rescue of the banking sector itself stemmed from national interests and strategic depth. In order not to construe this statement as a call for protectionism, what I mean by strategic depth is exactly how Europe dealt with the Greek crisis. No critical situation in an interrelated region can be put on the fringes and be ignored, because the impact on the neighborhood is inescapable. There are lessons to be learnt from that in the Arab world: the need to deeply weigh the impact of any wave or universal call on the national interests and strategic depth, and not to be fascinated by the novelty of some of these calls.

The national interests of every Arab state are intertwined with its neighboring Arab states and with some neighboring countries. The developments of the air transport industry, particularly in the Arab world, show that the Arab world and the environs contribute more than 80% of the Arab Air Transport Industry's volumes. In this regard, it is an absolute priority to move the Arab world on two levels: to establish a single Arab Air Transport Market in accordance with the Damascus Convention, whose rules and economic regulations protect the national interests of every Arab state, and to forge a new level in Arab aviation relations with our neighbors, especially with Europe, Africa, and with parts of Asia. These relations can be built on top of the already existing human and economic ties, and would set a base for a solid and equitable global aviation structure.

The year 2009 witnessed another global top priority: climate change. The manifestation of this change is very complex. The UNFCCC 15<sup>th</sup> Conference of the Parties (COP15) in Copenhagen, to

the disappointment of many environmental activists, could only muster taking note of an “Accord” between governments. This opens the door for the airline industry, through ICAO, to reach a global scheme that caters for the measures that the aviation industry needs to positively contribute to the mitigation of its emissions. Such a scheme would save the industry the pain of individual or regional schemes whose impact would be higher on costs, but none the better for the environment. At the time of writing this report, the industry had successfully reached a common position on the basis of three targets declared by IATA, while taking into consideration the investments made by airlines to improve their environmental footprint before 2020, as well as the special needs of airlines from developing countries. By the time AACO AGM convenes, ICAO would have concluded its own General Assembly, and we hope that ICAO succeeds in adopting a global scheme that is based on what the industry was able to agree on.

In the meantime, cooperative efforts remain the purpose of AACO’s existence. This term marks the first step to implement the directives of the 42nd AGM that was held in Jeddah on the new AACO vision, objectives and modus operandi. AACO, under the guidance of the Executive Committee, has embarked on a new platform that turns AACO into a tool for members to generate added value. You will see in this Annual Report how AACO successfully restructured its work, and enhanced joint cooperation and its global presence in the defense of its members’ best interests. AACO continues to act as the common voice of its member airlines.

A return to Cairo is a requisite for anyone who wishes to behold Egypt’s weight at the center of the Arab world, and its role in promoting joint Arab action, including the cooperation of AACO members. The last term was indeed full of challenges, but it was equally teaming with ongoing efforts to deal with those challenges by means of extracting added value to our members, and through acting effectively on their behalf. It is always an honor for us to meet in Egypt, “Umm El Donya”, and to live up, together, to tomorrow’s aspirations. During this term, it would not have been possible for AACO to play its role had it not been for your special support, especially at the level of Chief Executive Officers, and for the active participation, guidance and attention accorded by our Executive Committee, led by Engineer Hussein Massoud. To Engineer Hussein Massoud, we convey our deep appreciation, mine and that of the Secretariat General for inviting the Annual General Meeting to convene in Cairo. We reiterate that credit to him, and to his esteemed colleagues in EgyptAir in recognition of their efforts to stand true to the saying that whoever lands in Egypt has landed at home.

Abdul Wahab Teffaha



Secretary General

# Arab Air Transport

## Regulatory Environment within the Arab World: *Slow Progress*

### Damascus Convention

The Damascus Convention was adopted by the Council of Arab Transport Ministers in 2004; it was signed by 13 Arab states and ratified by 8. A **Multilateral** Agreement for the **Liberalization** of Air Transport between the **Arab countries**.

#### Challenges:

- The level of implementing the convention varies from one country to the other depending on their respective policies towards air transport and not necessarily based on the articles of the Convention.
- **Economic rules** differ from one Arab country to the other, leading to **anomalies between what the convention requires and the need to align the laws of the land**.

#### Implementation:

- Countries which **ratified** the Convention are: **Lebanon, Jordan, Syria, Palestine, Oman, Yemen, the United Arab Emirates and Morocco**. Countries which have **signed** but yet to **ratify**: **Bahrain, Tunis, Sudan, Iraq, Egypt, and Somalia**.
- **Regional efforts** to implement the Damascus Convention on various levels; **governments, civil aviation authorities, and airlines**.
  - Council of Arab Transport Ministers, at their 22<sup>nd</sup> session in October 2009, mandated a **working group** to **study** ways for the **implementation** of the **convention** and its economic regulatory code.
  - The group is **headed** by the **UAE** General Civil Aviation Authority and gathers representatives from the Arab civil aviation authorities, in addition to the **Arab Civil Aviation Commission (ACAC)** and the **Arab Air Carriers Organization (AACO)**.
  - The group met in January 2010 and presented its report to the Executive Bureau of the Arab Transport Ministers at their meeting on 28-29 April 2010.
  - **AACO** gathered information and comments from the **airlines** and provided **input to ACAC** and the working group, in addition to suggesting **interim measures** that could be taken while constituting a **legal framework** that could be the **arbitrator** of the parties of the convention.
  - The Transport **Ministers** issued a **resolution** in this regard:
    - The group to prepare a **survey** to be distributed to the Arab governments highlighting the **constraints** preventing the Arab countries from **ratifying**, joining and implementing the Damascus **Convention**.
    - To know the **strategy of each government** in terms of **ownership of airlines** and **liberalization** of the air transport sector.
    - To suggest any **updates** to the **convention** itself and its **economic regulatory code**.

- To study the **common EU policies** and code of work to **align** the Economic Regulatory Rules of the Damascus **Convention** with those of the EU, in preparation for a possible Arab-EU Aviation Dialogue.

**The Arab world did not actually undergo a fundamental transformation at the level of Market access, or at easing up the barriers to cross border ownership and control of investors in the Arab world.**

### **Ownership of Arab Airlines**

Some Arab governments have taken steps to partially privatize their national carriers:

- **Gulf Air:** In February 2010, Bahrain Government announced plans to privatize Gulf Air within one year.
- **Kuwait Airways:** Privatization underway. Expected to be finalized within few months.
- **Saudi Arabian Airlines:** Privatization underway. Sold 49% stake in the catering unit, and 30% of the cargo unit so far. Other units will follow suit. Memorandum of understanding was signed with Al-Ahli Capital and Morgan Stanley, who will act as financial advisers for the airline's privatization.
- **Royal Jordanian:** 71% of the capital of the company offered for sale.
- **Privately owned airlines** are being **established** in some Arab countries depending on the national policy of each government.

### **Agenda for Freedom and Statement of Policy Principles**

- A multilateral statement of policy principles regarding the implementation of bilateral air service agreements was signed by seven states in Montebello-Canada, on 16 November 2009.
- The signatory states are Chile, Malaysia, Panama, Singapore, Switzerland, the United Arab Emirates and the United States of America. The document was also endorsed by the European Commission.
- In October 2009, AACO 42nd Annual General Meeting adopted a resolution supporting the principles of the Istanbul Declaration i.e. the first "Agenda for Freedom" of Istanbul in 2008.
- In 2010 four Arab countries; namely, Bahrain, Kuwait, Lebanon and Qatar, endorsed the "Agenda for Freedom" Statement of Policy Principles.
- The Policy Principles mainly call for: Freedom to access capital markets; Freedom to do business in terms of market access; and Freedom to price services.

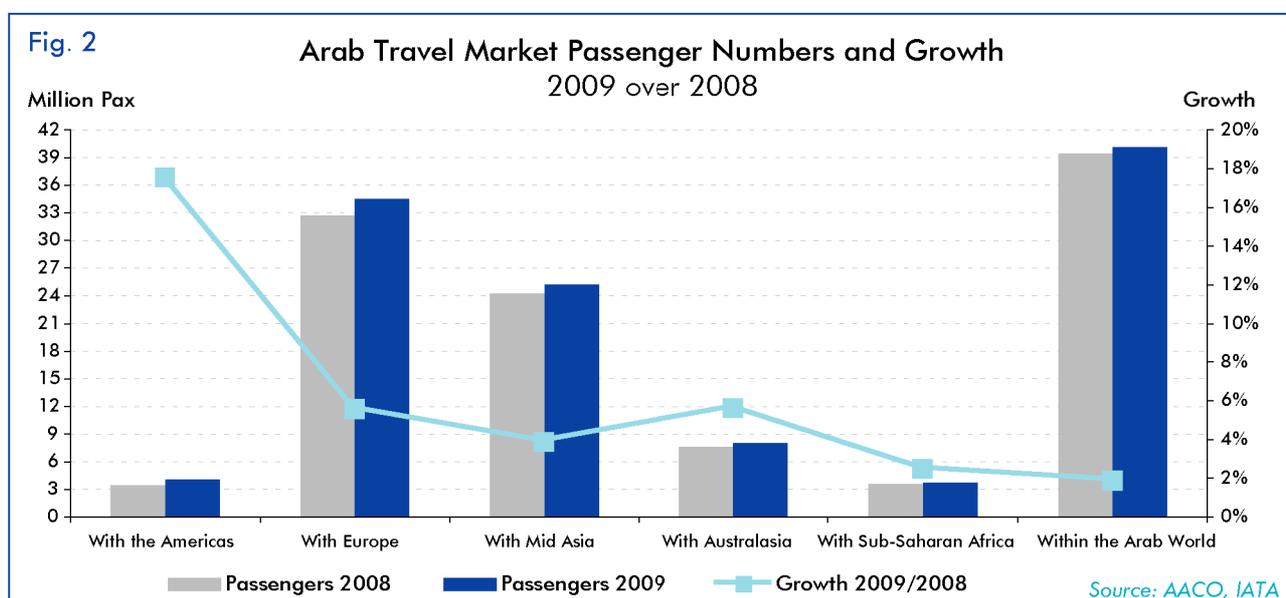
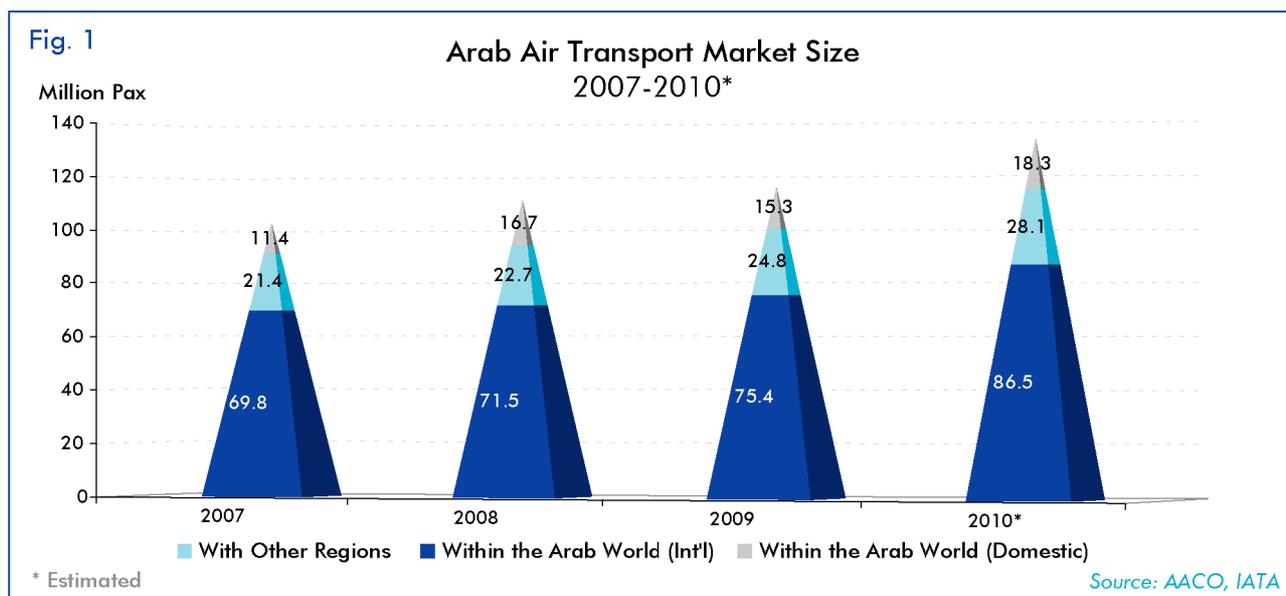
### **AACO with the Regional Aeropolitical Arena**

- AACO has established an **Aeropolitical Watch Group (AWG)** that gathers experts in Aeropolitical affairs from various airline members. The mission of this group is to follow up on the various regulatory affairs affecting the Arab airlines, lobby in favor of the joint interests of AACO members, provide awareness through AACO to the members on Aeropolitical affairs, and to suggest solutions wherever applicable.
- **AACO** and its airlines have maintained their **coordination** and **cooperation** with the Arab Civil Aviation Commission (**ACAC**) and the Arab civil aviation authorities as major players in the strategy and roadmap of the regulatory trends in air transport in the Arab region.

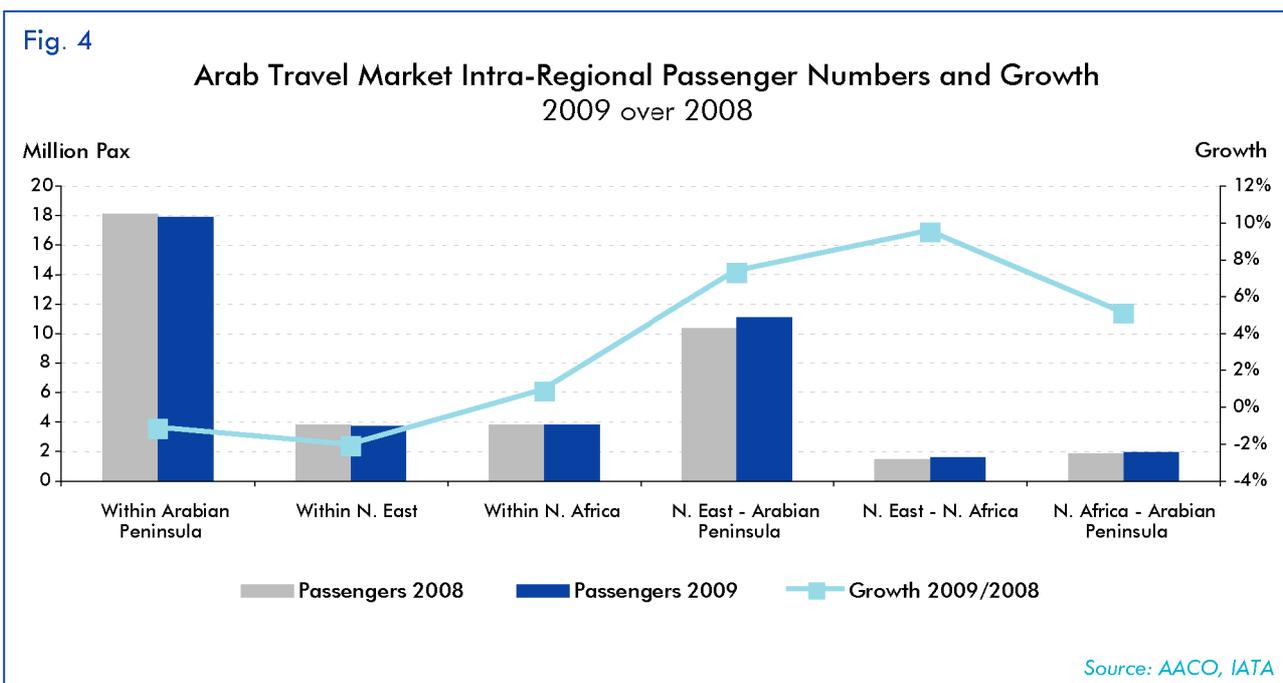
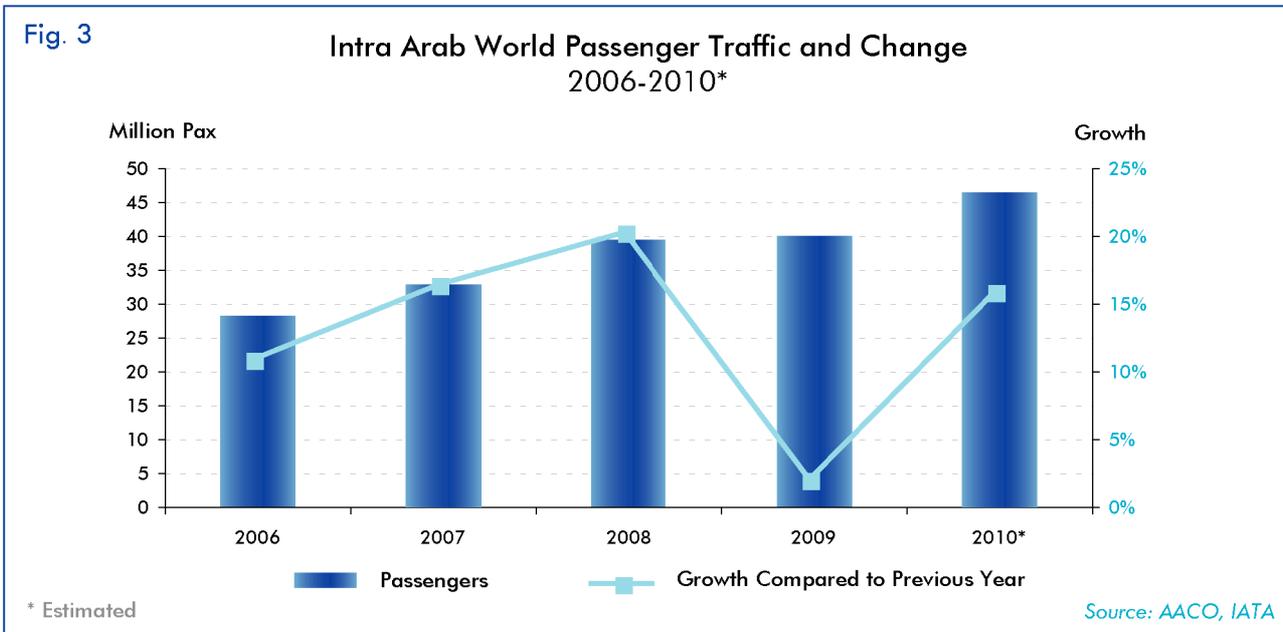
- AACO has been active in the **Arab League's** meetings and coordination especially on issues related to **liberalization** of air transport in the Arab world, aviation **relations with other regions** of the world, the **impact of environmental policies** on the region's airlines, in addition to **coordination** and **cooperation** between the regional associations for the **different modes of transport** in the Arab world under the **umbrella of the Arab League**.

## Arab Air Transport Overview: *Outstanding Performance*

The Arab air transport continued its expansion in 2009. Figures in the first half of 2009 indicate a slower rate as a result of the strong performance in the first half of 2008. The results of the second half of 2009, however, bore the effects of the financial crisis. The Arab air transport market grew by 4.2 percentage points compared to 2008. The number of passengers to, from and within the Arab world reached around 116 million passengers in 2009 compared to 111 million in 2008. As the economic recovery continues, we expect a healthier growth of 15% in 2010 to 133 million passengers. (Figures 1 and 2)



Passenger numbers within the Arab world grew by 1.9% in 2009 compared to 2008. The growth was curbed by the slowdown in domestic markets resulting from lower consumer confidence, which in turn led to the use of cheaper means of transport on domestic routes. We expect demand in the Arab world to pick up in 2010 in tandem with the economic and tourism recovery. Traffic is forecast to grow by 15.7% in 2010 compared to 2009. (Figures 3 and 4)



## AACO Members' Operations: Double Digit Growth

Some data for previous years has been recalculated for comparison consistency.

### Revenue Passenger Kilometers (RPKs)

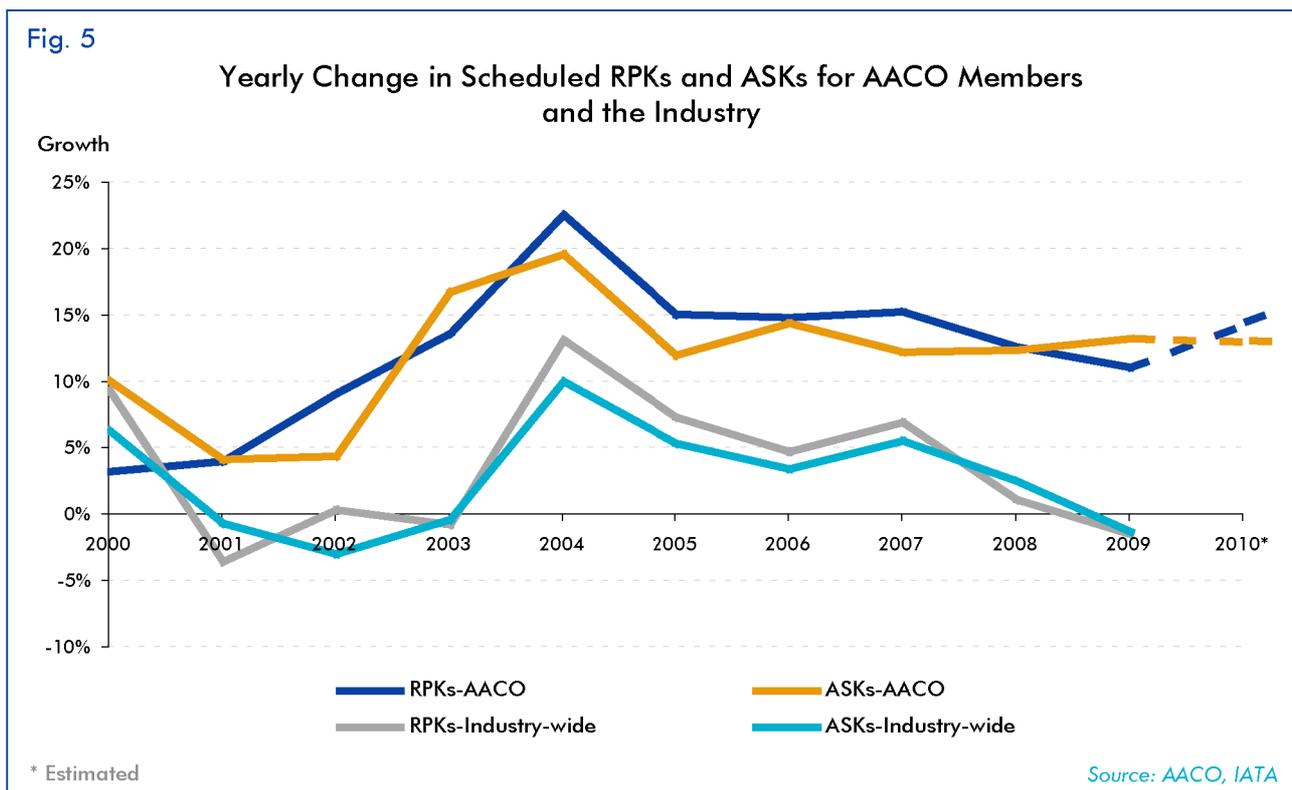
Member airlines registered an increase of 10.8% in 2009 in RPKs compared to 2008. The global decline for the same year was (1.8%) compared to 2008. We estimate a traffic growth of 13.9% in 2010 as Europe's and the Far East's economic recovery accelerates.

### Available Seat Kilometers (ASKs)

AACO members registered a growth rate of 12.9% in 2009 in ASKs relative to the year 2008, while the global decrease for the same period was (1.6%). AACO carriers are estimated to post a growth of 12.7% in ASKs in 2010 in line with aircraft deliveries expected to take place in that year.

### Load Factor

Load Factors at AACO members decreased by 1.3% to 71.3% in 2009 as capacity increase was higher than the growth in demand.

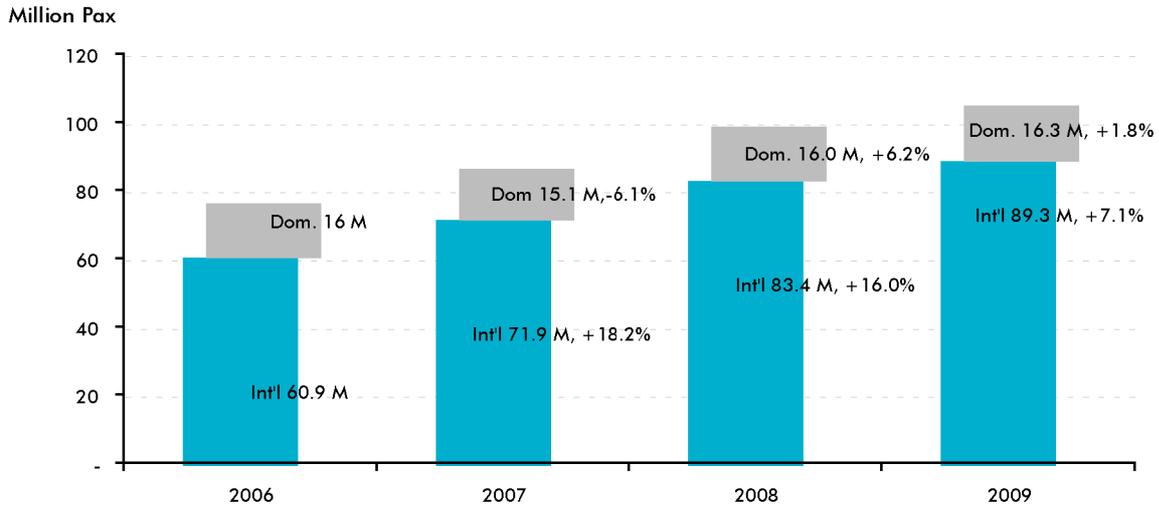


### Total Number of Passengers

The total number of passengers carried by AACO members reached 105.6 million passengers in 2009, an increase of 6.2% over 2008. This comes in comparison with an industry decrease of (1.6%). (Figures 5 and 6)

Fig. 6

### Number of Passengers on Most AACO Members 2006-2009



Source: AACO

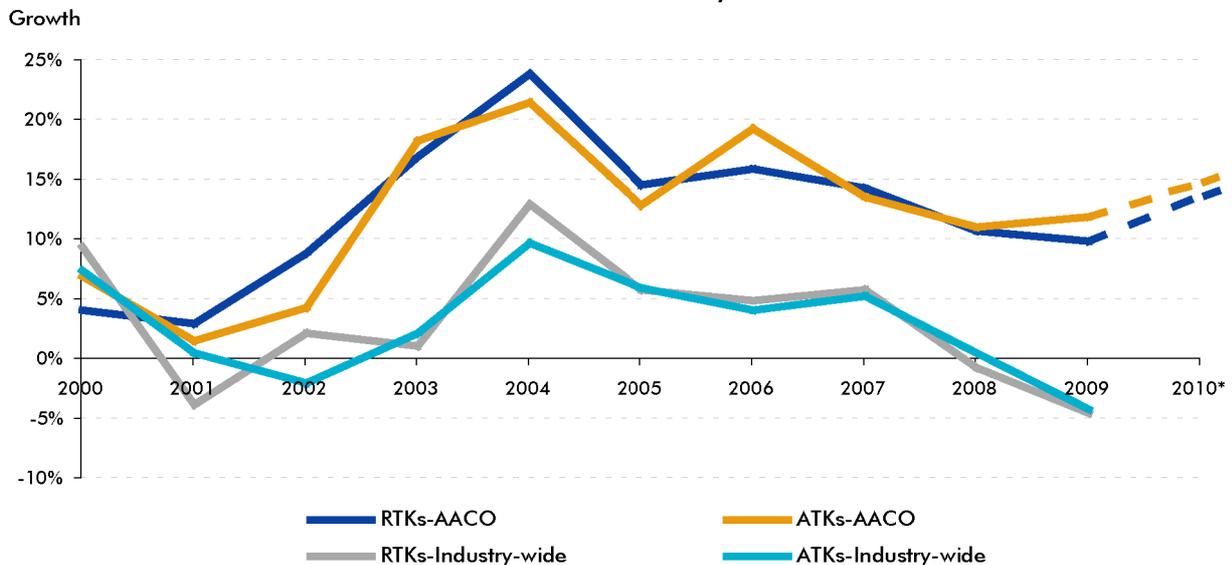
### Cargo in the Arab World

Arab airlines recorded a growth of 9.5% in 2009 in RTKs compared to 2008, in contrast to (4.9%) global decline for the same period, as a result of healthier trade conditions boosted by good levels of domestic demand. AACO members also recorded a growth of 11.5% in ATKs. Consequently, AACO carriers' Weight Load Factor declined by (0.8) percentage points to 58.8%.

We expect AACO members' cargo operations to increase by 13.3% in traffic and by 14.2% in capacity as world trade recovers, and consumer and business confidence restores. (Figure 7)

Fig. 7

### Yearly Change in Scheduled RTKs and ATKs for AACO Members and the Industry

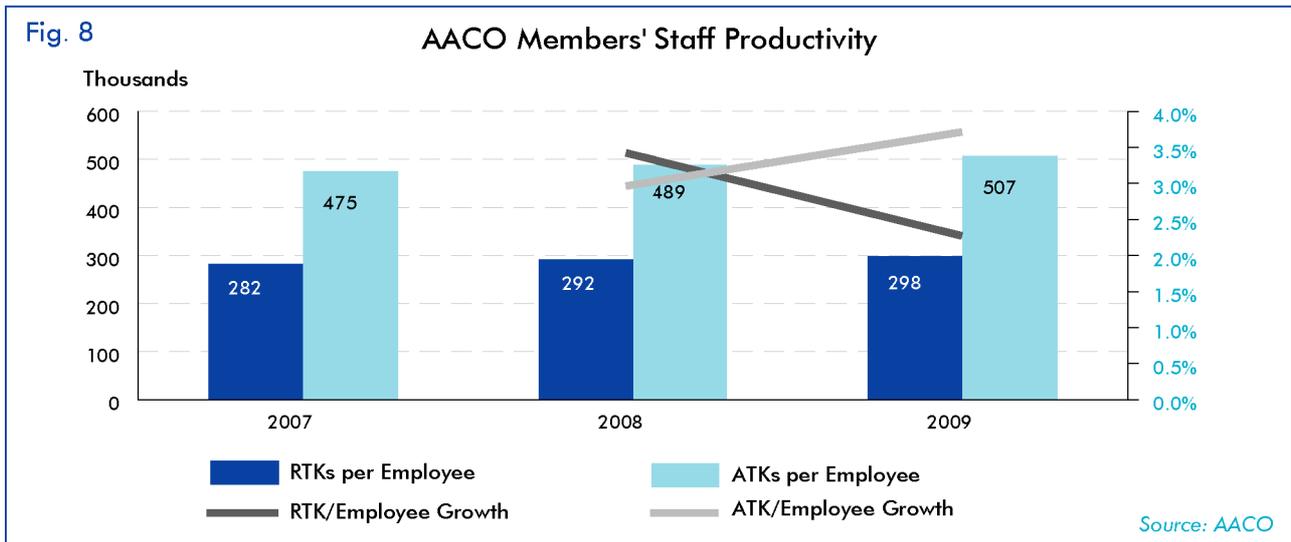


\* Estimated

Source: AACO, IATA

## Employees

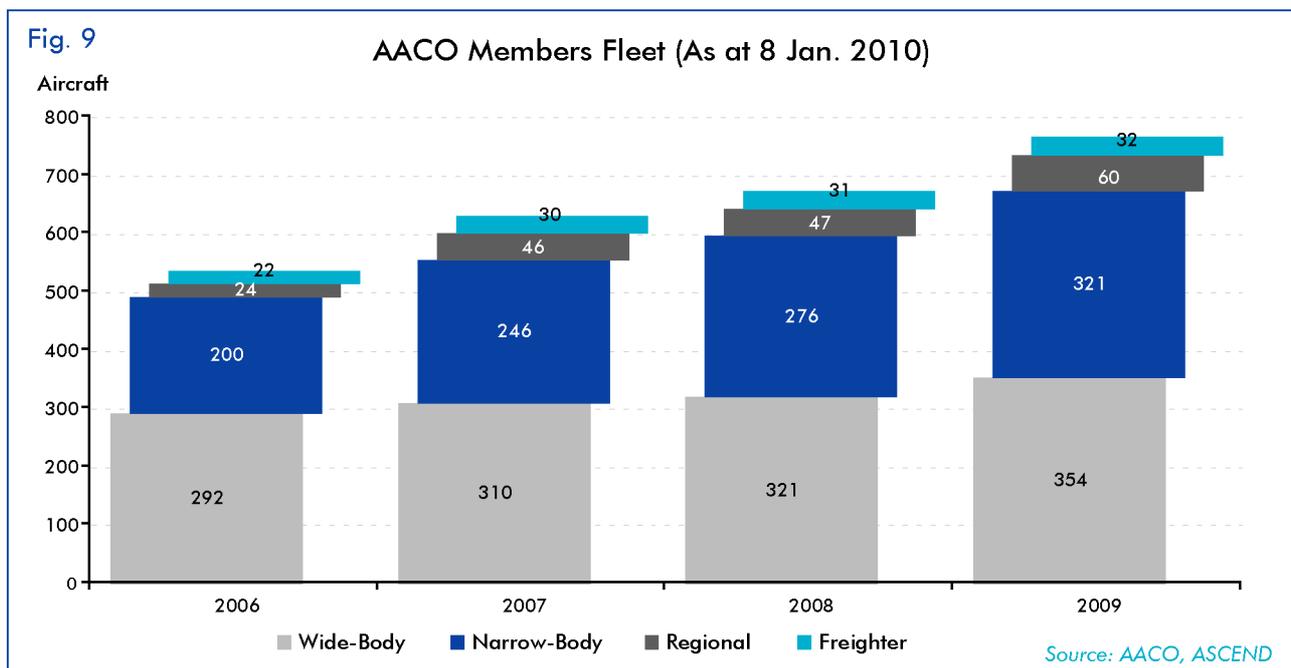
Staff counts at AACO members increased by 7.8% in 2009 over 2008. The restructuring that has been taking place at many carriers resulted in an increase in employee productivity to 298 RTKs per employee and 507 ATKs per employee, in thousands. The percentage increase over 2008 levels was 2.2% and 3.6% respectively, compared to a decline of industry-wide productivity of (1.6%) and (1.1%) respectively. However, in absolute numbers, the industry productivity averages were 344 and 529 respectively, which signals the need of additional optimization of staff at AACO members in order to reach optimal productivity. (Figure 8)



## AACO Members' Fleet: Youngest and Growing...

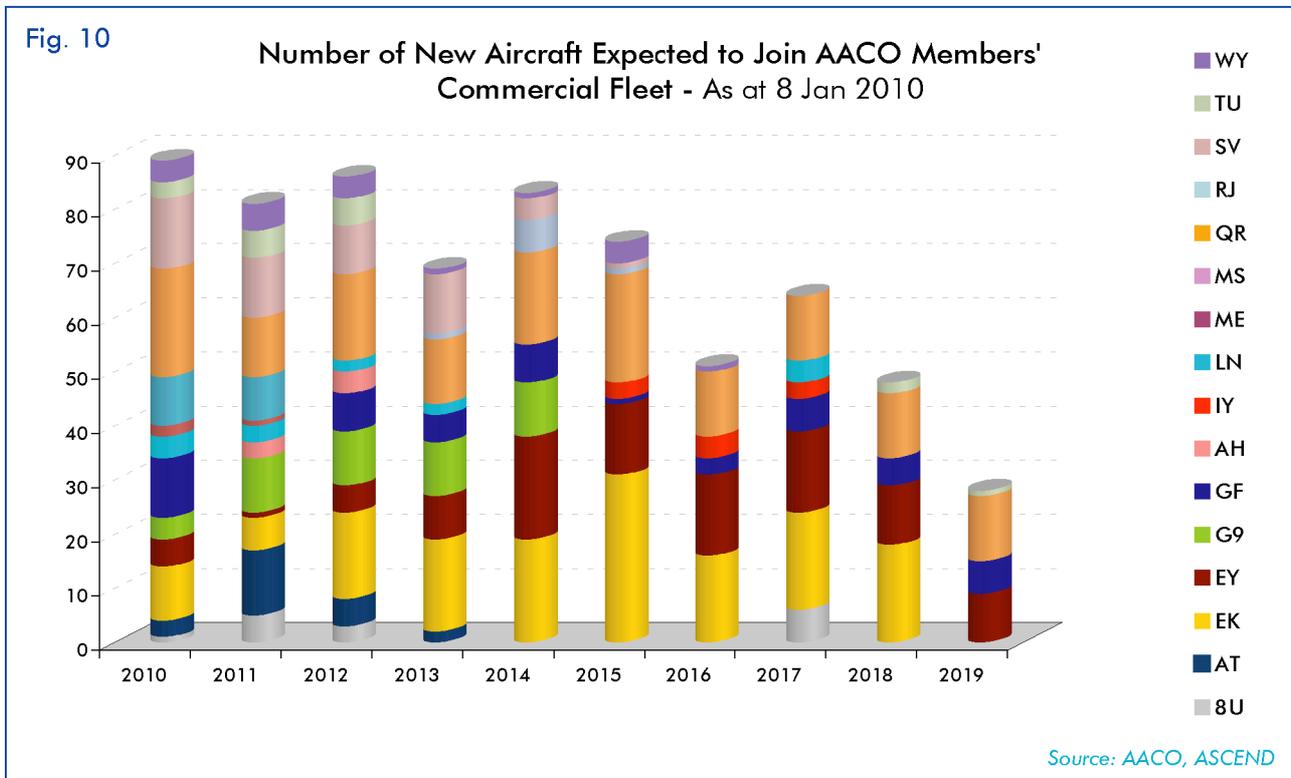
### Current Fleet

AACO members took delivery of 158 aircraft in 2009, including 94 brand new aircraft, and 64 older ones (Figure 9). These new acquisitions reduced AACO members' average age per unit aircraft by a considerable (15.6%) over 2008 fleet, bringing the AACO members' fleet age down to 7.7 years.



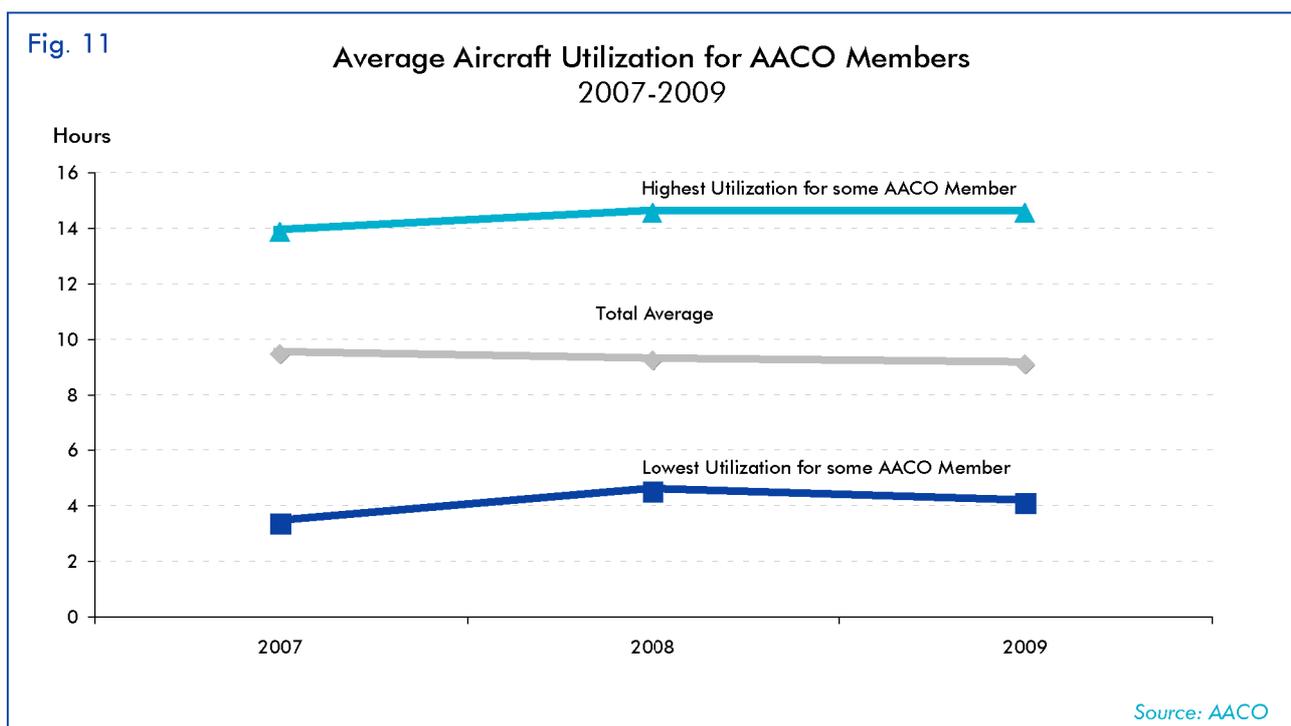
## Contracted Aircraft

Arab airlines are scheduled to receive 673 aircraft until 2019, among which 89 aircraft are scheduled for 2010. AACO members took delivery of 40 new aircraft during the first seven months of 2010, with 49 scheduled for delivery until year end. (Figure 10)



## Average Aircraft Utilization

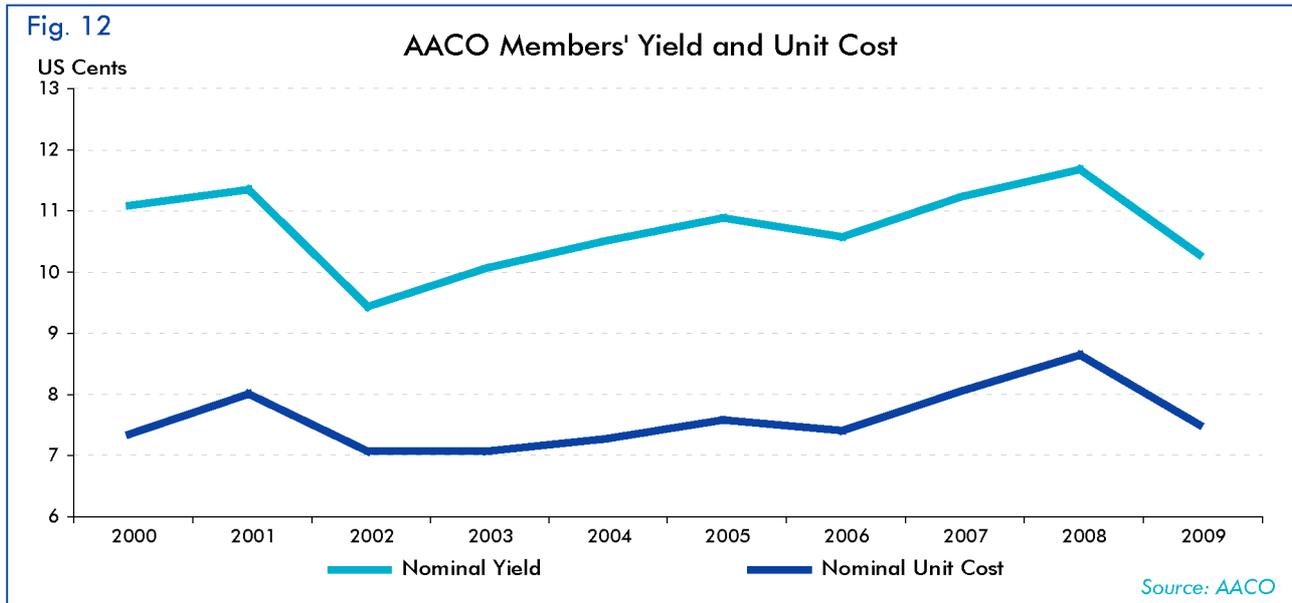
Resulting from the decrease in operations at some charter operators, and due to better economic conditions in the Arab world which led to increase of offered capacity in the region, AACO members' average aircraft utilization fell slightly in 2009 by (1.6%). (Figure 11)



## Financial Performance of AACO Members: *Positive but with Reserve*

### Yield and Unit Cost

Yield of 13 Arab airlines decreased by (12%) in 2009 together with lower consumer willingness to spend on air travel during the past period. On the other hand, AACO members succeeded in rationalizing their costs to oppose the decrease in yields, as a direct result of lower fuel prices on one hand, and the product of the carriers' restructuring programs. Consequently, unit costs decreased by (13.3%), easing break-even Load Factor by 1.1 percentage point, down to 72.8%. (Figure 12)



### Changing Costs

AACO members' benefited from the decline in the cost of fuel, which prices were driven down by the decrease in demand during the financial crisis. In addition, carriers rationalized their indirect operating costs, introducing price transparency mechanisms to passengers in an effort to remain in the black. In 2009, jet fuel cost for reporting carriers decreased by (23.1%) over 2008. In addition, AACO airlines rationalized their sales/marketing and administrative costs, bringing them down by (2.5%) and (14%) respectively. (Figures 13, 14 and 15)

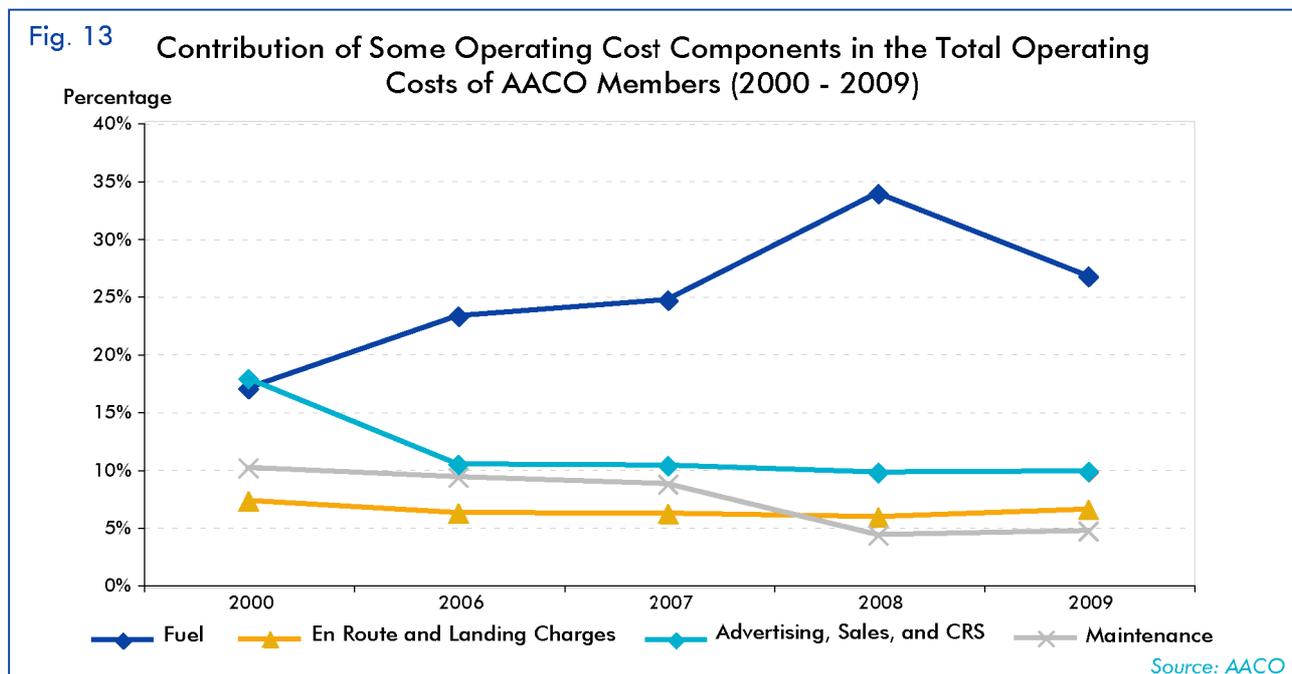
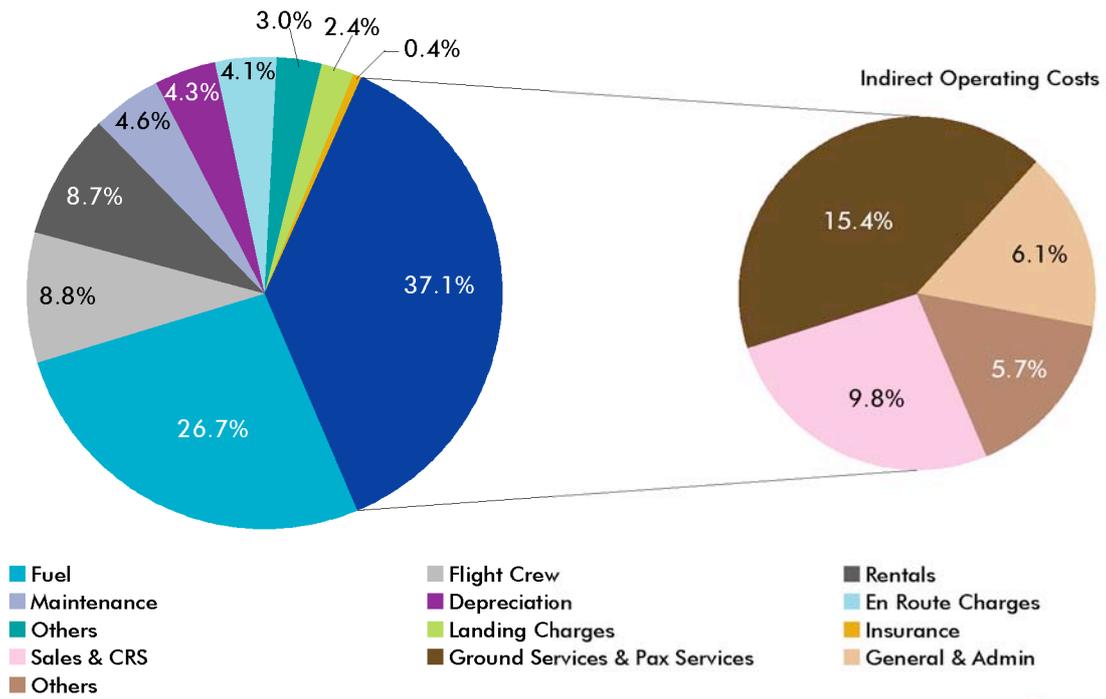


Fig. 14

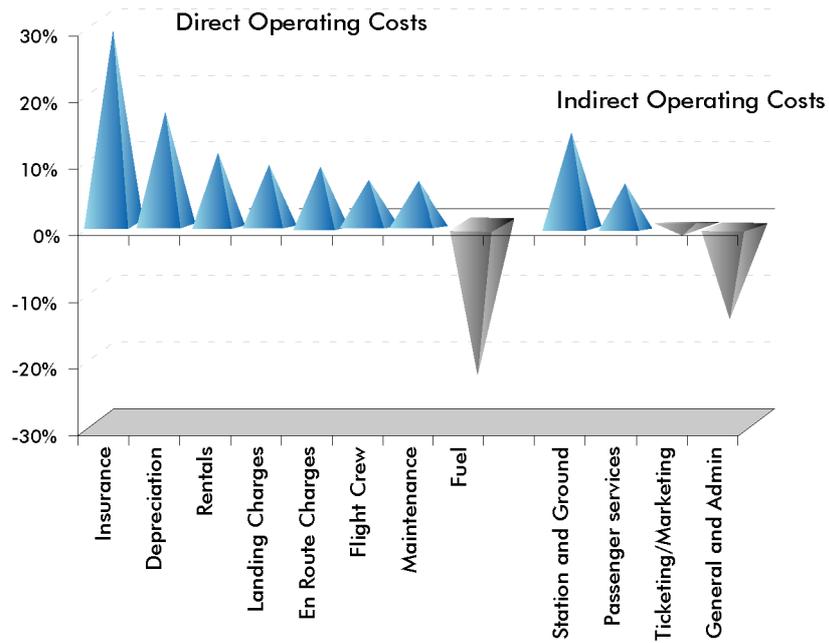
### Operating Expenses by Cost Item - 2009



Source: AACO

Fig. 15

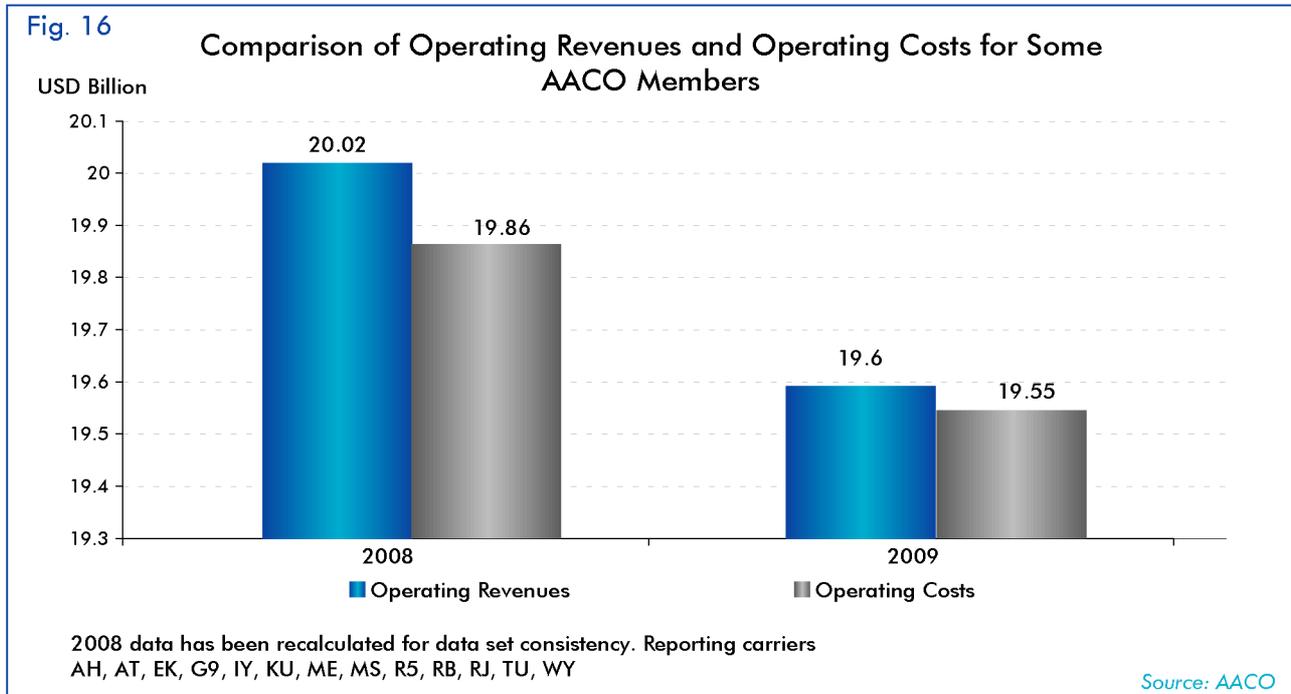
### Cost Changes - 2009



Source: AACO

## Financial Results

Thirteen reporting AACO carriers' aggregate operating revenues declined by (2.1%) in 2009 over 2008. On the other hand, airlines' operating expenses decreased by (1.6%). Consequently, reporting members remained in the black, posting an operating profit of USD 45.2 million, and a net profit of USD 856.5 million. The big difference between operating profits and net profits at the reporting carriers is backed by the exceptional increase in non-operating revenues from financial and asset related investment activities at some AACO members. (Figure 16)



## Arab Airports: Hubs of the 21<sup>st</sup> Century

### Passengers, Cargo, and Aircraft Traffic

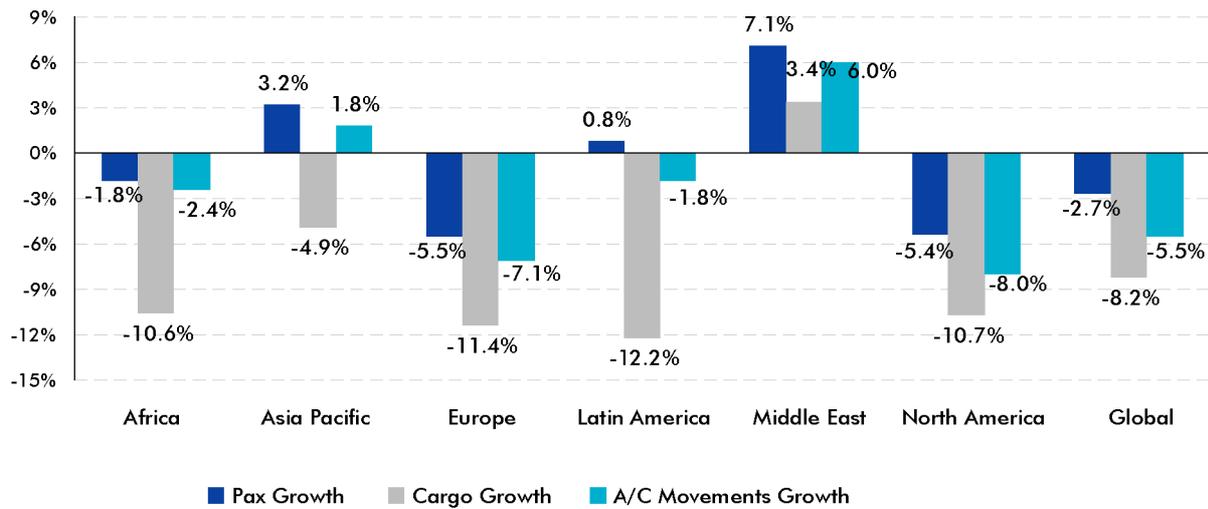
#### Global Traffic

According to **Airport Council International**, traffic at world airports witnessed a **decline in 2009** due to the global **financial crises** where effect was strongest in the first half of 2009, in addition to the **H1N1 outbreak** in Latin America during Q2 2009. As a result, global **passenger** traffic and **cargo** traffic **declined** by **2.7%** and **8.2%** respectively in 2009, and **aircraft movements** were **5.5%** below 2008 levels.

Looking at regional patterns, the slow economic recovery in **Europe** and **North America** led to a **decline** in passenger numbers in those regions' airports by 5.5% & 5.4% respectively in 2009, whereas the **Middle East** airports led the global **growth** in the number of **passengers**, growing by **7.1%** over 2008. The **Arab World** was the only region that recorded a **growth** in **international passenger & freight numbers**, growing at **7.9%** and **3.5%** respectively.

Fig. 17

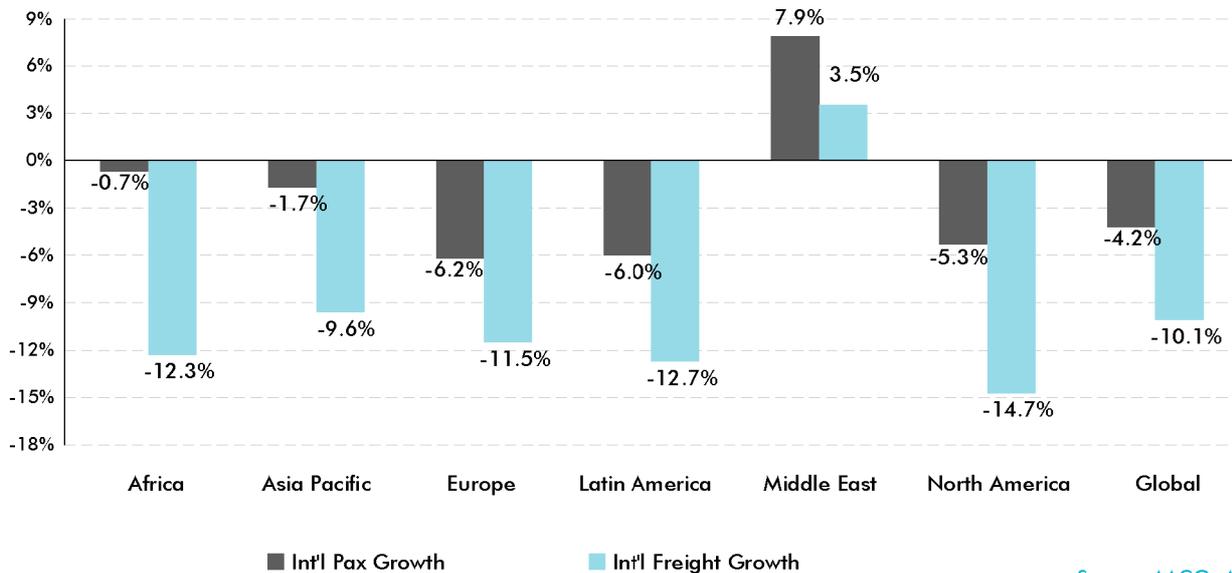
Worldwide Airports Traffic Growth - 2009/2008



Source: AACO, ACI  
ACI Regional Geostructure

Fig. 18

Worldwide Airports' International Traffic Growth - 2009/2008



Source: AACO, ACI  
ACI Regional Geostructure

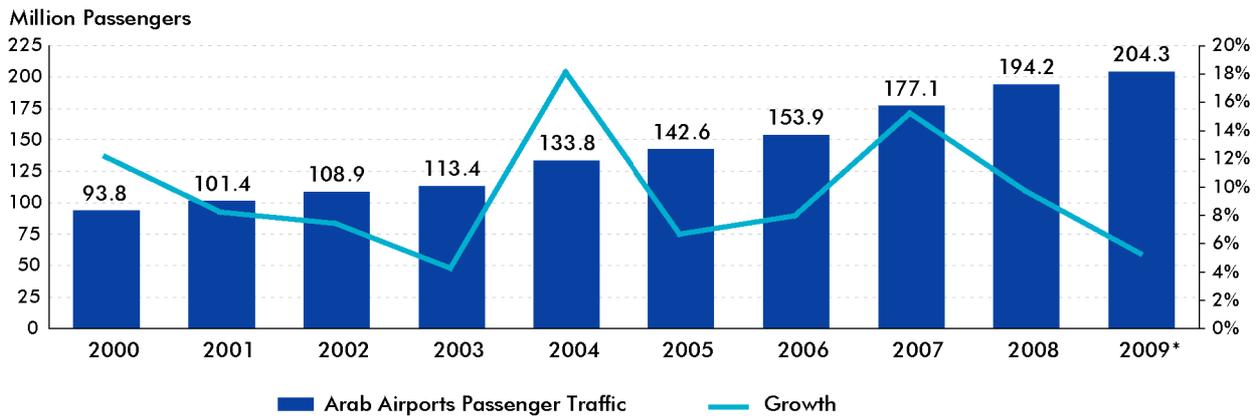
Among the top 20 busiest airports worldwide, **Dubai airport** was the second of only four airports that registered growth in 2009, growing at **9.6%**. In addition, **Beirut, Kuwait, and Sharjah** airports **led** the world's airports in terms of percentage international **passengers' growth**, and were the only airports reporting **double digit growth** over 2008.

## Arab Airports Traffic

In 2009, **passenger numbers** at Arab airports **grew** by **5.2%** over 2008. Five Arab airports reported double digit passenger growth, with two airports growing above 20%. On the other hand, ten Arab airports witnessed a decline in passenger numbers; three of these airports recorded a decline less than 1%, whereas five airports reported double digit decrease in passenger numbers. It is worth mentioning that almost all airports that reported a decline in their passenger numbers are airports used mainly for tourism purposes, a sector which was affected by the global economic crisis.

Fig. 19

Passenger Numbers and Growth at Most Arab Airports

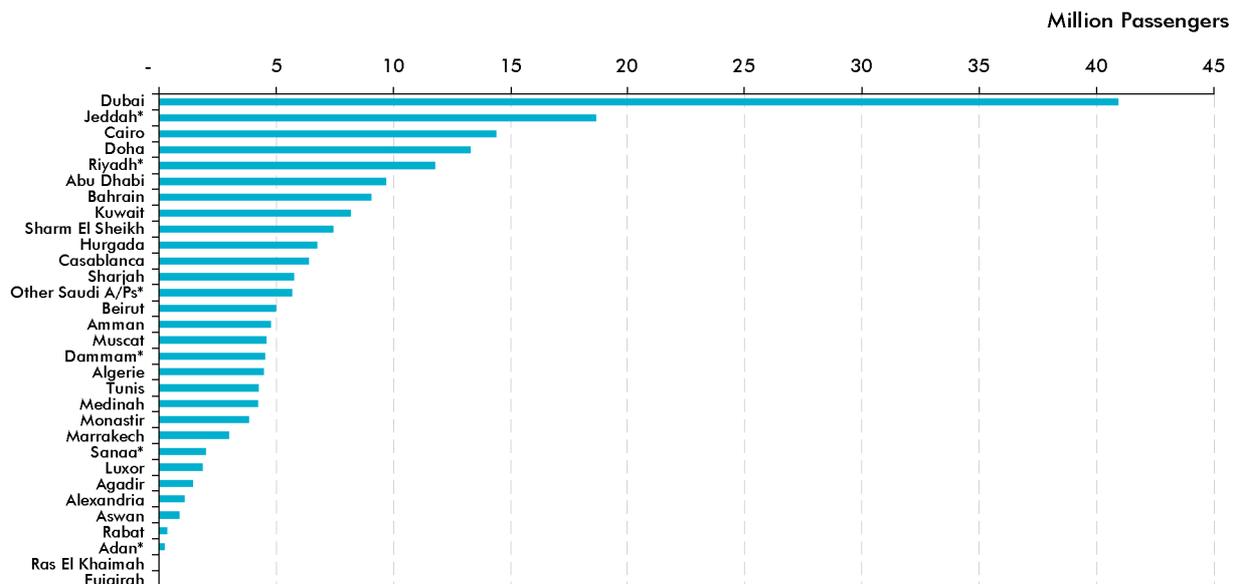


\* Estimated

Source: AACO, ACI

Fig. 20

Number of Passengers at Most Arab Airports in 2009



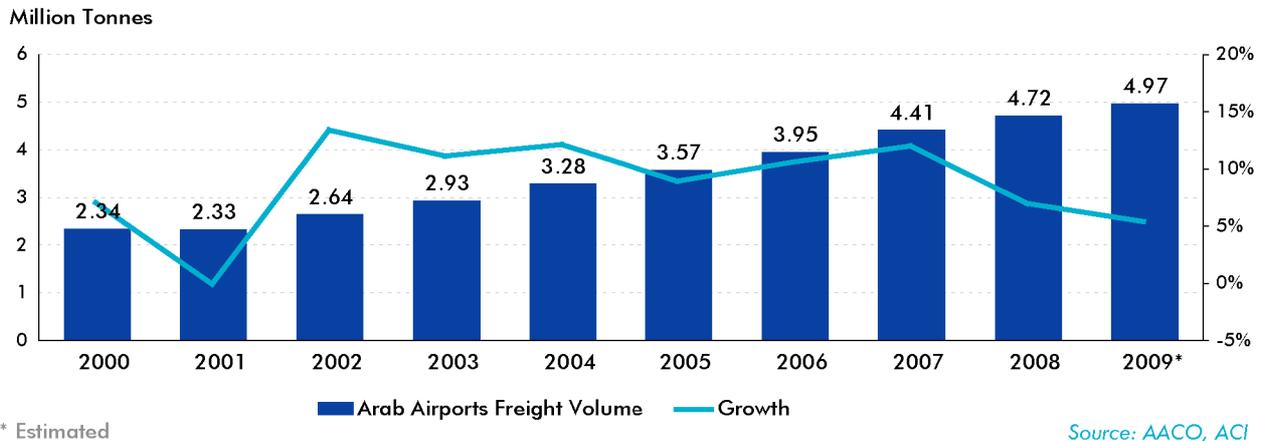
\* Estimated

Source: AACO, ACI

Similar to passenger traffic, **cargo traffic** at Arab airports **increased** by **5.3%** in 2009 over 2008, signaling a healthy economic recovery in the region. Sharjah airport led the freight growth, scoring 16.1% over 2008. In addition, four Arab airports reported double digit growth in freight volumes.

Fig. 21

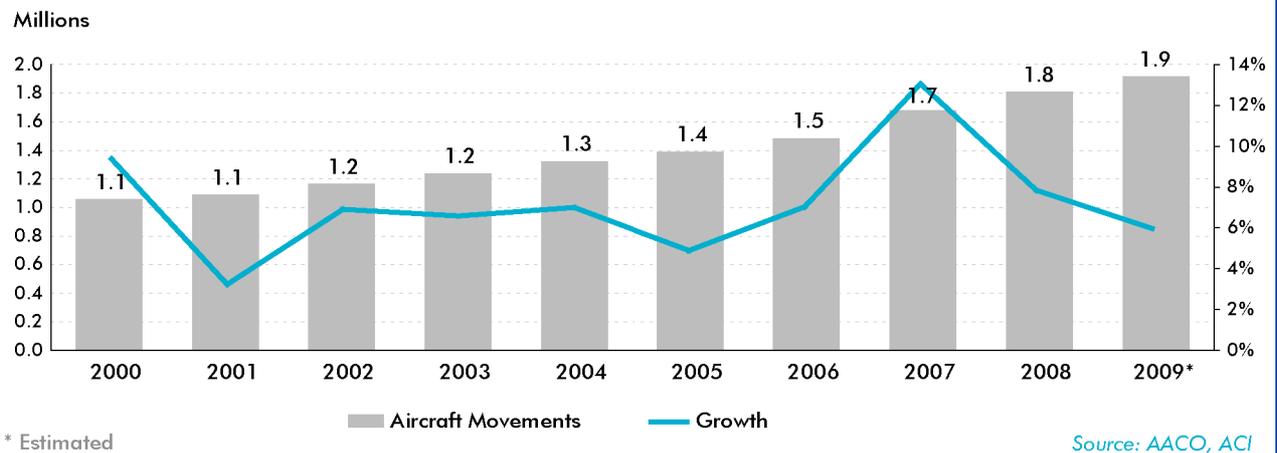
Cargo Volumes and Growth at Most Arab Airports



**Aircraft movements** recorded a **growth** of **5.9%** at Arab airports. Beirut airport led Arab airports in terms of percentage growth of aircraft movements' in 2009, scoring 22.6% over 2008. In addition, eight Arab airports recorded a double digit percentage growth in aircraft movement over 2008. On the other hand, nine Arab airports witnessed a decline in movements in 2009 over 2008.

Fig. 22

Aircraft Movements and Growth at Most Arab Airports



## Developments at Arab Airports

**Passenger numbers** at Arab airports **increased** by around **120%** in 2009 over 2000. Acknowledging the importance of infrastructure and service in the Arab aviation industry, Arab governments continue to invest in airport developments to support and fuel the growth in the air transport sector. In addition several ongoing projects, civil aviation authorities are announcing new initiatives aiming at improving the infrastructure and customer experience at Arab airports:

### United Arab Emirates:

- Dubai World Central Al Maktoum International Airport officially opened for cargo operations in June 2010, with an expected capacity of 250,000 tonnes of cargo by the completion of Phase 1. The airport is expected to open for passenger traffic in late March 2011, at a forecasted capacity of 5 million passengers in the first stage.
- Sharjah airport deployed the world's first Common Use Self Services (CUSS) Kiosks with an Arabic interface, in an effort to accommodate the needs of passengers who prefer to interact with the system using the Arabic language.
- UAE General Civil Aviation Authority awarded full certificate to Al Bateen Airport. The airport was previously used in military operations, and is now in the final stage of being converted to serve private and corporate air operations.
- Abu Dhabi Airport Council (ADAC) plans a new air traffic control center facility in Abu Dhabi to accommodate commercial air transport needs for the next 20 years. The facility will include 34 individual control centers and an additional 22 centers for emergency purposes.
- Projects in progress in UAE include Dubai World Central, expansion of Abu Dhabi International Airport, airport development and expansion projects in Al Ain, Ajman, Sir Bani Yas, Delma, Ras Al khaimah, and Fujairah airports.

### Saudi Arabia:

- **Jeddah's** King Abdulaziz International Airport **opened** its **new runway** in October 2009. The new runway is **4 km long** and **60 meters wide**. In addition, Saudi Arabia is planning a new terminal at the airport.
- Saudi authorities approved the expansion plans at Riyadh's King Khalid International Airport. The first phase of the project will increase the airport's capacity to 25 million passengers.
- Saudi Arabia is considering a new international airport in Makkah, and an upgrade to Medina airport to increase its capacity to 14 million passengers. In addition, plans are being finalized for the development and creation of 23 domestic / regional airports.
- In order to facilitate passenger travel experience, Saudi authorities introduced e-gate systems at King Khalid International Airport in Riyadh, and King Fahed International Airport in Dammam.

### Oman:

- **Development projects** are carried out at **Salalah** Airport, which is converted from domestic to international airport. In addition, developments at regional airports in **Sohar, Duqm, Ras Al-had** and Adam are underway, with all airports expected to start operations in 2012.
- **New Muscat International** airport is scheduled for completion in **2014**, with an expected capacity of 12 million passengers annually.

### Kuwait:

- Kuwait announced a new passenger terminal at Kuwait International Airport. The new terminal is planned for completion by the end of 2016, and will be able to handle 13 million passengers annually, raising the airport's annual capacity to 20 million passengers.
- Expansion efforts are put also in the current airport, including runways work, aircraft hangers, additional administrative buildings, car parks and fire stations.

### **Bahrain:**

- Development projects at Bahrain International Airport include the introduction of mobile radio service in the airport, which provides voice & data communication for airlines and ground handling staff at the airport. In addition, a second phase of the project is currently under assessment, which includes an RFTD Guard Control System.

### **Iraq:**

- Iraq plans to double capacity at Baghdad International Airport to 15 million passengers per year.
- In addition to the new runway at Irbil Airport, Iraq announced plans for a new international airport that would be built between the three provinces of Kerbala, Najaf and Hilla, and a new international airport in Salahaddin province.

### **Jordan:**

- Work is in place to restructure, develop, and enhance services at Queen Alia International Airport, in addition to development of Marka civil airport.

### **Sudan:**

- Sudan announced plans to build a new international airport at an estimated cost of USD 1.8 billion. The project will comprise three phases, and is expected to completion in mid 2013.

### **Tunisia:**

- Tunisian government approved fund allocation that will be used to modernize Tabarka airport in northern Tunisia, along with other Tunisian airports.
- 2009 marked the opening of the new Enfidah Zine El Abidine Ben Ali International Airport in December. The airport started operations with an initial yearly capacity of 7 million passengers, and is projected to increase its yearly capacity in 40 years to 22 million passengers.

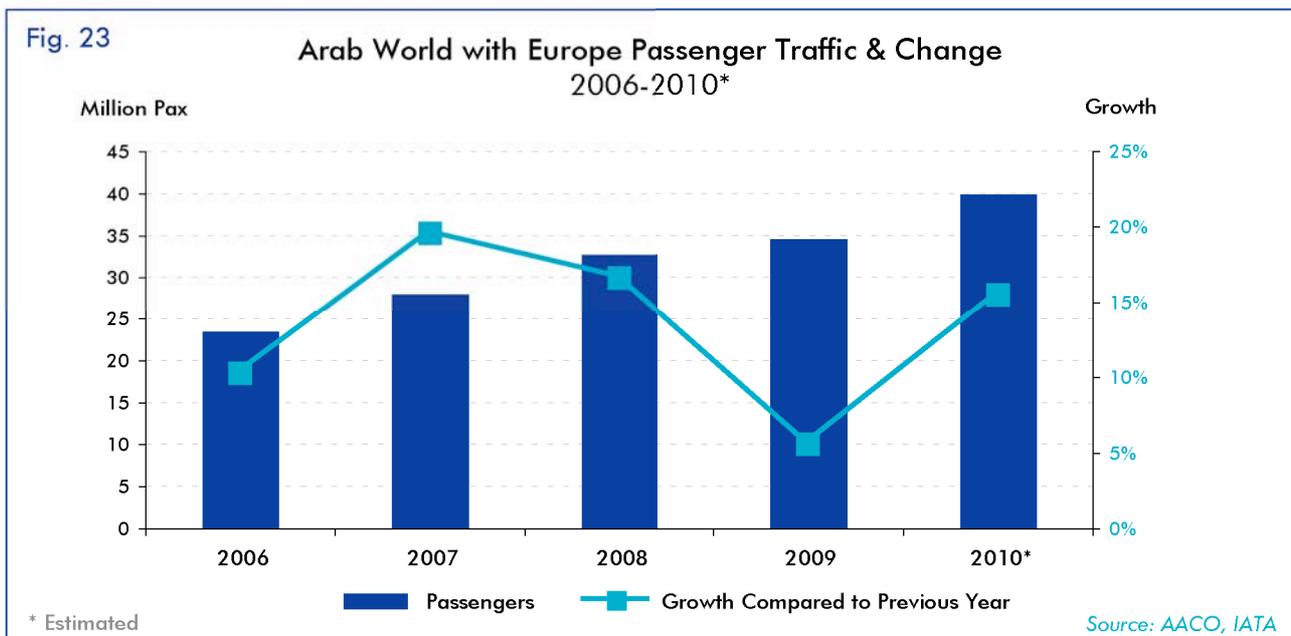
# Aeropolitical Affairs & International Relations

## Air Transport between the Arab World and Europe:

*Stronger Towards Regulatory Convergence*

### Traffic Update

In 2009, passenger numbers between the Arab world and Europe increased by 5.6% compared to 2008, mainly due to the slow economic recovery in Europe. As economic performance is expected to pick up in 2010, we forecast a traffic increase of 15.5% in 2010 over 2009.



### European Union External Aviation Policy

□ **Horizontal Agreements** to bring existing bilateral agreements between European and non-European countries in line with Community law, by **removing nationality restrictions** in these bilateral agreements.

The **United Arab Emirates, Lebanon (not ratified yet), Jordan** and **Morocco** signed "Horizontal" agreements.

□ **Common Aviation Area** with **neighboring** countries including Mediterranean countries through **Euromed agreements** under the Euromed Aviation Project.

**Morocco** and **Jordan** signed Euromed agreements with the EC, noting that Euromed agreements open the skies between the two parties in addition to a gradual regulatory convergence in areas like safety, air navigation, environment, competition laws and passenger rights.

#### Euromed Aviation Project

■ In December 2005, participants to the Euro-Mediterranean Ministerial Conference on Transport agreed on the need to work towards a Euro-Mediterranean Common Aviation Area. In January 2007 the project was launched for a period of 3 years.

- An **Extension in 2010** (till January 2011) has been agreed in November 2009 to carry on with the tasks of the project. A new project, **Euromed Aviation II**, will be launched in 2011 to pursue the implementation of the **Euro-Mediterranean Common Aviation Area (EMCAA) by 2018**.
- Arab countries part of the Euromed Aviation Project are: Algeria, Egypt, Jordan, Lebanon, Morocco, Palestinian Authority, Syria, and Tunisia.
- **Comprehensive Agreements** with countries around the world to set up open aviation areas with global partners.

## Arab – European Air Transport Relations

- **Sharm El-Sheikh Declaration:** signed in November 2008 between the European Commission (**EC**) on one side and the Arab Civil Aviation Commission (**ACAC**) and the Arab Air Carriers Organization (**AACO**) on the other side.
  - Confirmation of the principle of **reciprocity in commercial opportunities** to ensure a **level playing field**.
  - Strengthening future technical **cooperation** in areas such as aviation safety, aviation **security, air traffic management, environmental protection, competition laws** and **economic regulation**.
- **Muscat Declaration:** Signed between the **EC** and **ACAC** in October 2009 following the **first EU – Arab World Aviation Conference**, where **AACO** was **represented** and **provided input** to the conference.
  - Stressed the need to enhance EU-Arab Cooperation to ensure sustainable **development of air traffic** between the two regions.
  - The two regions identified areas of cooperation: **air navigation, safety, fair competition**, in addition to a determination to continue cooperation to **open up their market** for air transport.
  - Stressed the importance of making the **Euromed** agreement **on the level of the European and Arab regions** to create competitive and homogeneous airspace.
- Following a **working paper** submitted by **AACO** to the Council of **Arab Transport Ministers** in their meeting in April 2010, Arab Transport Ministers adopted a resolution that recommended the **use of the Sharm El-Sheikh Declaration** in bilateral relations/ negotiations with the EU.

## Regulation Highlight: Air Passenger Rights in the EU – EC Regulation 261/2004

### European Court of Justice (ECJ) Ruling

- The ECJ has issued a judgment in two passenger rights cases that a **flight delay of more than 3 hours** may be **treated** as a **cancellation** for the purpose of the application of the **right to compensation**, unless the airline can prove delay was caused by extraordinary circumstances which could not have been avoided even if all reasonable measures have been taken, noting that a **technical problem cannot be** regarded as “**extraordinary**” unless it stems from events which are not inherent in normal airline activity.
- Although the regulation itself did not change, its **applicability has widened**. It is likely that national courts will follow the ECJ’s interpretation in dealing with claims for delay compensation.

This Judgment has been **criticized** intensely by **AACO** and the airline **industry**.

### EC Consultation on Regulation 261/2004

AACO submitted responses to the consultation on Air Passenger Rights that touched upon the development of new business practices, and focused on the issues of mishandled baggage and rescheduling of flights. Results of the consultation have not been announced yet.

- At a time when industries begin to recover from the economic crisis, some governments' are predisposed to impose new kinds of taxes on airlines in an attempt to recover from the economic downturn. One of the most famous taxes in 2010 was the new 'ecological air travel levy' introduced by Germany. It is a departure tax that the government believes will raise USD 1.19 billion annually. It will be in place until aviation is included in the EU's Emissions Trading Scheme beginning in 2012.
- Another well-known government's intention to raise money from taxes imposed on airlines is the UK government's intention to replace Air Passenger Duty (APD) with a "per-plane" tax. Some analysis indicated that under the Liberal Democrats' manifesto proposals to make the switch to a "per plane" duty, passengers on short-haul flights would pay up to 75% more as part of plans to generate GB£5.3 billion from the tax – up from GB£1.9 billion under labor.

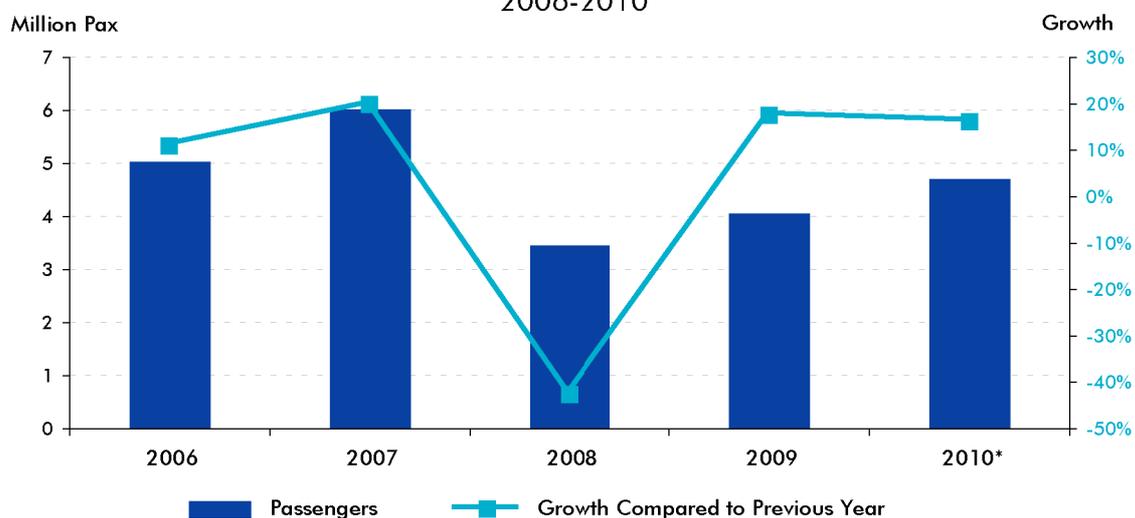
## Air Transport between Arab World and the Americas: *Solid and Expanding*

### Traffic Update between the Arab World and the Americas

Passenger traffic between the Arab world and the Americas grew by 17.5% in 2009, fueled by the depreciation of the Dollar and faster recovery at the USA compared to other advanced economies, and to the expansion of operations between the Arab world and Latin America on the other hand. Traffic growth is expected to remain strong in 2010, at 16.1%.

Fig. 24

Arab World with the Americas Passenger Traffic & Change  
2006-2010\*



\* Estimated

Source: AACO, IATA

**Bilateral Relations with some Arab countries:** Jordan, United Arab Emirates, Bahrain, Morocco, Oman, Qatar, and Kuwait have open skies agreements with the United States.

**US latest open skies partners:** Late 2009 and in 2010, the US signed open skies agreements with Uganda, Zambia, Trinidad & Tobago, Switzerland, and Laos.

## Regulation Highlight: US DOT Notice of Proposed Rulemaking (NPRM) on Passenger Rights

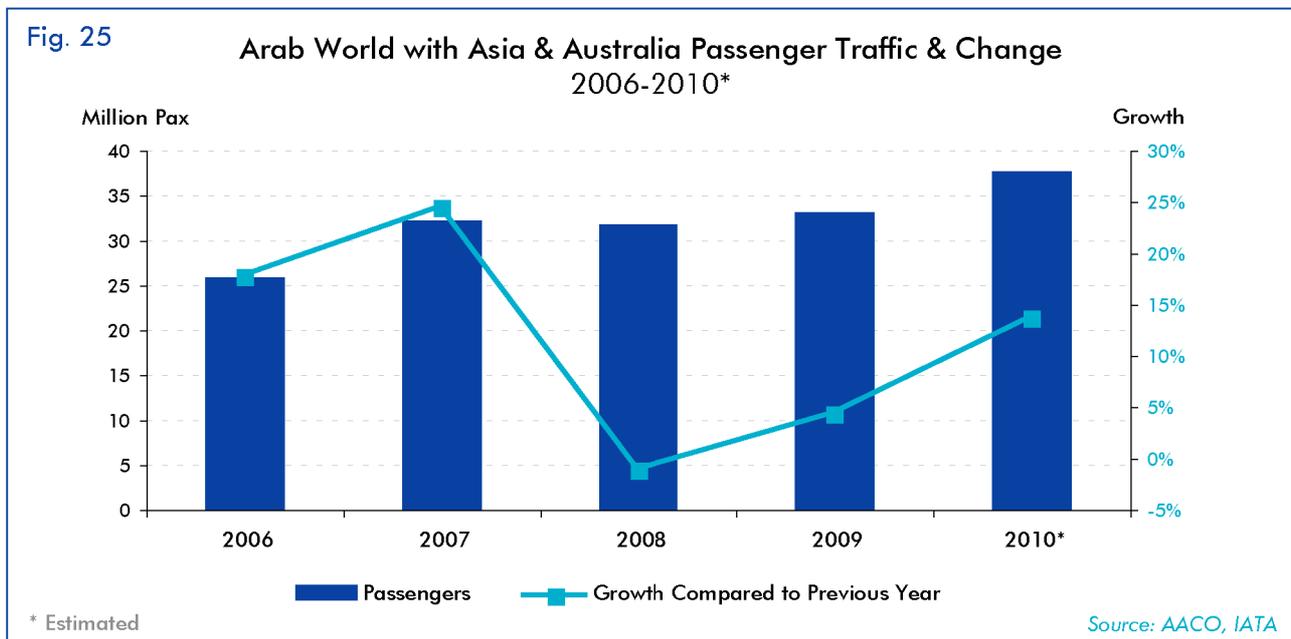
The US Department of Transport (DOT) issued a Notice of Proposed Rulemaking on Passenger Rights. Among other things, the US DOT is proposing the following that affect foreign airlines including Arab Airlines:

- To **boost** the maximum **payment** owed to **passengers** who were denied boarding from flights to **USD 650** from USD 400, and to **USD 1,300** from USD 800, depending on how many hours they would be delayed in arriving on an alternate flight.
- **Refunds to passengers** who paid to check **bags** that **didn't arrive on time**.
- **Foreign airlines to abide by tarmac-delay rules** that U.S. carriers already must follow for domestic flights only. Under that rule, US airlines must specify in advance their own time limits for deplaning passengers.
- Overseas carriers wouldn't be subject to a separate part of the tarmac rule that limits the time airlines can keep passengers waiting on the tarmac to three hours, as that provision only applies to domestic flights; however, the DOT is soliciting public **comments on whether the three-hour rule should apply to international flights** as well.

**AACO** cooperated with **IATA** and the various **regional associations** of airlines in an attempt to study and **solicit comments** and **analysis** to provide **comprehensive input** to the DOT.

## Air Traffic between Arab World, Asia and Australia: *Greater Presence*

Passenger traffic between the Arab world, Asia and Australia grew by 4.3% in 2009 over 2008. Traffic is expected to regain some of its momentum in 2010, at 13.6% in 2009.

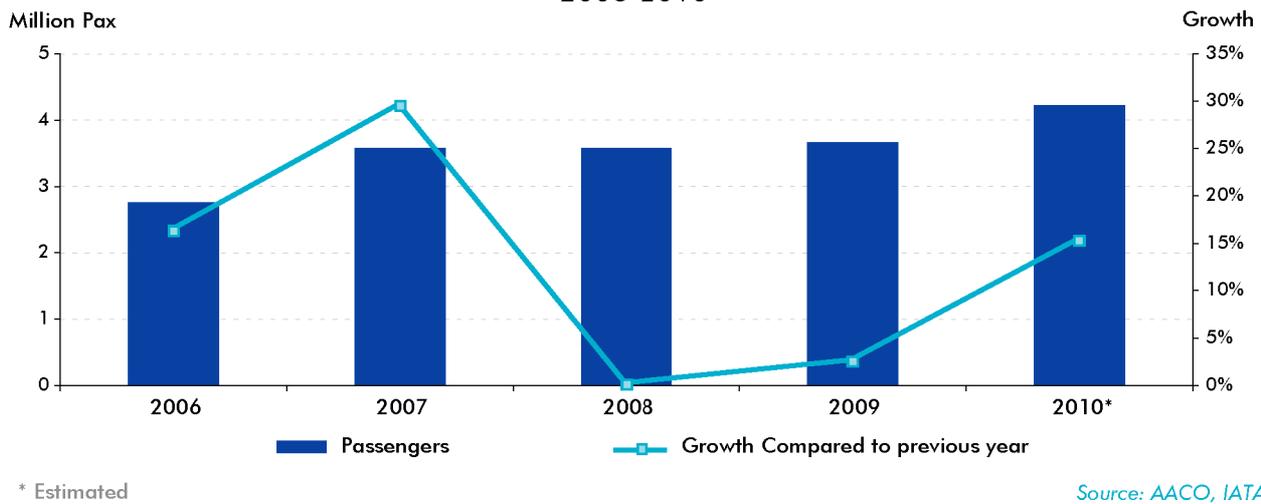


## Arab World with Central and Southern Africa: *Increasing Importance*

Passenger traffic increased by 4.4% in 2009 compared to 2008 as economic conditions in Africa improved. Traffic between the Arab world and Sub-Saharan Africa is forecast to increase by 15.3% as business confidence increases.

Fig. 26

### Arab World with Sub Saharan Africa Passenger Traffic & Change 2006-2010\*



## European-American Air Transport Relations: *Small Steps but no Giant Leaps*

### First Phase

- The **first phase** of the **Open Skies Agreement** between the EU and the US came into effect on 30 March **2008**. The first phase allows the **liberalization** of air services between the two sides by removing all restrictions on routes, pricing and number of weekly flights between the two markets. Furthermore, the agreement established a **comprehensive framework** for cooperation with the United States on a wide range of aviation issues, such as aviation **security**, **competition** policy, the **environment** and **passenger rights**.
- The EU, the US, Iceland and Norway have signed an aviation agreement in **2010** to extend the application of the **EU-US Open Skies Agreement** to cover **Iceland** and **Norway** as well.

### Second Stage

- On 24 June 2010, the **EU** and the **US** formally signed the **second stage open skies**.
- **Greater access** for EU airlines to the "Fly America" program.
- **Reciprocal liberalization** of airline **ownership** and **control**. Currently, foreign ownership in US airlines is limited to 25% of voting rights. Upon legislative change in the US, the EU will reciprocally allow majority ownership of EU airlines by US nationals.
- Subject to legislative changes in the EU concerning the process for introducing noise-based airport restrictions, EU airlines will gain additional rights to fly between the US and a number of non-European countries.
- A **number of obstacles** for **EU investment in third-country airlines will be removed**. Similar rights will be available for US airlines when the US laws allow EU majority ownership of US airlines.
- In terms of **regulatory cooperation**: The agreement strengthens cooperation on **environmental** matters, **labor rights**, **security**, and extends the role of the EU-US Joint Committee, the body that monitors the implementation of the agreement and coordinates the various work streams of regulatory cooperation.

## ATM

- Following the agreement, the **EC** and the **US FAA** officially **initialed** the **Memorandum of Understanding** and a first technical Annex promoting **interoperability** between their respective **air traffic management (ATM)** modernization programs: **SESAR** and **NextGen**.

## PNRs

- **Passenger name records** also returned to EU-US **negotiating agenda**. The EU is preparing for a new series of talks with the US over the transfer of air passenger name record data (PNR). The Commission needs the formal green light from EU capitals before it can start talks with the US.

### Some of the benefits of the agreement as stipulated by the EU:

- In economic terms, worth up to 12 billion euros in economic benefits and up to 80,000 new jobs.
- Forecasts for 26 million additional passengers on transatlantic flights over a period of five years. This compares with current annual traffic of just under 50 million (2007). At the end of the 5 year period, growing the market by 34% over its pre-agreement size.
- A reduction is envisaged in the cost of tickets for companies and private customers, with consolidated economic benefits of between 6.4 and 12 billion euro over a period of five years by eliminating the bilateral agreements and their restrictions on traffic rights.

# AACO and Environmental Issues

## Unilateral Emissions Trading Schemes: *Are they in line with the Chicago Convention?*

### European Union Emissions Trading Scheme (EU ETS)

#### General Provisions & Updates

- The EU Emissions Trading Scheme (**EU ETS**) was extended to the aviation industry pursuant to **Directive 2008/101/EC**, which came into force on 2 February 2009, stipulating that as of **1 January 2012**, all flights arriving at or departing from an EU airport will be included in the ETS.
- Various requirements for **compliance** were requested including submission of **monitoring plans** for Tonne-Kilometre (TK) data and emissions data, and **verified TK reports** and annual verified emissions reports as of 2010.
- On 1 January 2010 the Emissions Trading Scheme for aviation was **expanded** to include flights to, from **Norway, Iceland and Liechtenstein**, or domestic flights in these countries.
- On 14 July **Member States** in the **Climate Change Committee** unanimously **voted** in **support** of the Commission's draft **Auctioning Regulation**. The Commission would submit the draft Regulation to the European Parliament and the Council for a three-month scrutiny. Some highlights of the regulation are listed below:
  - The regulation lays down the rules for auctioning emission **allowances** valid for the third trading period of the EU ETS starting in 2013 as well as allowances to be used **by aircraft operators** already **as from 2012**.
  - For **aviation**, **15% of allowances** will be **auctioned** in **2012** and this proportion will stay the same in subsequent years.
- The European Commission is working towards potential rules to add airlines that do not comply with the EU ETS to the list of banned airlines to the EU. An unofficial draft regulation has been sent by the EC Directorate General for Climate Action to EU Member States for advice.

#### Legal Challenges against the EU ETS

- In December 2009, the Air Transport Association of America ("**ATA**") and three of its member airlines (**American, Continental and United**) filed an **application** for a **judicial review** in the **High Court of London** to **challenge** the **legality** of the extension of the EU ETS to international aviation.
- On 27 May 2010, the **UK High Court** in London **gave** the US Air Transport Association of America (**ATA**) **permission to take** its **legal challenge** of the EU ETS to the European Court of Justice (**ECJ**).
- The court also granted **permission** for a **transatlantic coalition of environmental groups** to **join** the **action**. Similar applications by the International Air Transport Association (**IATA**) and the National Airlines Council of Canada (**NACC**) to **intervene** were also granted although as a combined brief.
- ATA and the supporting **parties argue** that the **extension of the ETS** to aviation is **unlawful** for the following reasons:

- It violates the fundamental principle of international law that each state has complete and exclusive sovereignty over the airspace above its territory.
- It violates a number of provisions contained in the Chicago Convention.
- It violates the terms of a large number of bilateral agreements, including the Open Skies Agreement (1997) between the EU and the US.

### AACO and the EU ETS

- AACO estimates that the **EU ETS** will **cost AACO members** around USD 3.8 billion between 2012 and 2020.
- AACO **member airlines** in compliance with the EU ETS, have **successfully submitted** their monitoring **plans** for **emissions** and **tonne-kilometre** to their competent authorities in their administering member states.
- Airlines will have **to submit** annual **verified** emission and TK **reports** for 2010.
- AACO has signed an **agreement with SITA** for **consultancy** service.
- 11 AACO members have installed, with the support of SITA AEM, an **automotive tool for collecting airlines data** for all flights to/from Europe which produces accurate reports and simplifies the verification process.
- 13 AACO members have signed with **Lloyd's** for the **pre-verification** of monitoring plans submitted on time to the competent authorities.
- **AACO team** has been **active** in participating in the **consultations workshops** convened by EU states for transposing the EU ETS Directive into the national laws.

### Other Unilateral Emissions Trading Schemes

- **New Zealand** - staged implementation of an ETS (2010 - 2015) aims at cutting carbon emissions to 1990 levels.
  - Fuel suppliers bear the responsibility for compliance and they in turn pass the costs on to the users. Airlines can voluntarily opt-in the scheme.
  - The scheme applies only to domestic air travel, while jet fuel used on international flights is exempted.
  - Beyond 2013, the New Zealand Scheme depends on the outcome of the current negotiations for a possible successor to Kyoto. If no successor emerges, New Zealand will fix national/regional targets.
- **USA** - federal cap-and-trade proposals are facing difficulties.
  - Progress in the Senate has been very slow and all indications are that no cap and trade legislation will pass the Congress in 2010.
- **Australia** - cap-and-trade bill consideration postponed.
- **Switzerland** - voluntary cap and trade as an alternative to a CO<sub>2</sub> tax.
- **Japan** - voluntary cap and trade, to gather experience. Proposals are in the country's parliament for mandatory ETS.

## Global Policy governing Aviation's Impact on the Environment:

*ICAO, ICAO and ICAO!*

### Background and International Treaties in Place

- International treaty -- the United Nations Framework Convention on Climate Change (**UNFCCC**).
  - Objective: Stabilizing Green House Gases (GHG) concentrations at safe level.

- Principles: several, among them Common but Differentiated Responsibilities (**CBDR**).
- Commitments: Annex I Parties (industrialized) are committed to reduce emissions, and to support financially and technologically actions by non-Annex I Parties (developing) to implement the Convention.
- Number of nations approved an addition to the treaty: the Kyoto Protocol - 2005, which has more powerful and legally binding measures.
  - New commitments for Annex I Parties to reduce emissions over 2008 -2012.
  - Kyoto Mechanisms: **Clean Development Mechanism, Joint Implementation, Emissions Trading**.
  - Second commitment period to start in 2013.
  - The Kyoto Protocol has recognized **ICAO**, as the **global instrument** to pursue the limitation or reduction of greenhouse gas emissions from international aviation.
- **Bali Action Plan** 2007, negotiations ongoing.
  - In parallel with negotiations for Kyoto Protocol second commitment period.
  - Commitments for all developed countries.
  - Actions by developing countries.
  - So far it led to the "**Copenhagen Accord**".

## Governments

### ICAO

- **ICAO High Level Meeting Declaration – October 2009:** To achieve a **global annual average fuel efficiency** improvement of **2 per cent** over the **medium term until 2020** and an **aspirational global fuel efficiency** improvement rate of **2 per cent per annum** in the **long term from 2021 to 2050**, calculated on the basis of volume of fuel used per revenue tonne kilometer;
- **Friends of the President:** In preparation for the Assembly, President Kobeh-González has set up a group of DGCA "Friends of the President" **to develop the declaration of the HLM** to be submitted to the 37<sup>th</sup> ICAO Assembly.
- **37<sup>th</sup> ICAO Assembly:** The 37<sup>th</sup> triennial ICAO Assembly will take place in Montreal from 28 September to 8 October 2010. One of the **main items** on the agenda will be **climate change**.

### 15<sup>th</sup> Conference of the Parties (COP15)

- The United Nation Framework Convention for Climate Change (UNFCCC) held its 15<sup>th</sup> Conference of the Parties in Copenhagen between 8 and 18 December 2009. The **conference** was **concluded** with the **Copenhagen Accord**.
- The Kyoto Protocols which dealt with mitigation and reductions of emissions, identified targets and commitments up till 2012. Therefore, COP15 was supposed to provide the commitments of mitigation and reduction beyond 2012 giving time from the end of 2009 up till the end of 2012 for states to ratify the new protocols if agreed upon.
- The **primary focus** of the states' delegations, except very few, **was not on aviation**. It was **rather** on other **economical issues** related to **energy** and **industries** on the one hand, and getting access to **financial aids** on the other.
- The Accord is a **non-binding** agreement in-between governments, which stipulates the following major items:
  - The Accord **did not mention aviation** which can be considered a plus or a minus depending whether governments will see aviation as a "Free Game" for their "individual or joint mitigation measures" or not.
  - The Accord **did not mention a global sectoral approach**.
  - **ICAO** was **not assigned nor mentioned**.

- The Accord did **mention CBDR** which is good news for developing nations because ICAO mentioned that they will abide by the principles of CBDR if agreed in COP15.
- Latest Status of the Copenhagen Accord:
  - From the Arab countries: **Morocco, Jordan, UAE, Lebanon and Tunis, supported the Accord.**
  - **Almost all (Annex I) countries supported the Accord.**

## Airlines – AACO, IATA and Regional Airlines Associations

### AACO AGM Resolution – October 2009

- **IATA** in Kuala Lumpur (June 2009) decided to lobby for the support of its four pillar strategy and committed the following 3 industry targets on the basis of giving ICAO a mandate to formulate a global sectoral approach for the mitigation of emissions for aviation:
  - **1.5% average annual efficiency target up till 2020.**
  - **Carbon neutral growth beyond 2020.**
  - **50% absolute reduction over 2005 level by 2050**
- **AACO 42nd AGM** in Jeddah **resolved to support the industry targets provided that the Common but Differentiated Responsibilities (CBDR) principle is applied on aviation and provided further that the unique situation of airlines who have invested in their fleets be recognized in any mitigation measures.**

### AACO's Work since the Jeddah AGM Resolution

- **Establishment of an AACO Environmental Policy Group (EPG):** The group's target is to follow up on the various environmental policy issues pertaining to aviation and in addition to finding solutions that would help AACO members in facing environmental challenges.
  - **AACO** has participated in **COP15** as part of the Arab League delegation, and lobbied to include aviation in any agreement based on the following:
    - Provide **ICAO** with the **mandate to develop a global sectoral approach** to be presented to COP-16.
    - **ICAO should be guided by the CBDR** in a way which minimizes competitive distortions.
    - **No taxes** and levies should apply on aviation as a measure to mitigate emissions. Mitigation **measures** should be **agreed mutually** by the concerned states.
    - **Investments** made by airlines should be **recognized.**
- AACO has worked throughout the past period on comprising an Industry Position in cooperation with IATA and the Regional Associations of the airlines of the world; **Combined efforts** that have led to the **IATA resolution** declared in **Berlin June 2010.**

### IATA AGM Resolution – June 2010

- Strongly endorses the continuing efforts of its airline members and **ICAO** to **develop a comprehensive proposal for a global carbon emissions management framework** under ICAO as opposed to a patchwork quilt of unilateral national and/or regional plans, such as the EU ETS.
- Agrees that a **priority area** for IATA is to ensure that responsibility for meeting the **collective industry CNG 2020 target** be equitably and fairly distributed to individual carriers, giving **due consideration to early actions** taken by airlines in advance of 2020 and taking into consideration the **special needs of developing countries** and the **maturity of aviation markets**, while ensuring a **level playing field amongst airlines.**

- Encourages the industry, ICAO and governments to gain endorsement at the 37<sup>th</sup> ICAO Triennial Assembly for a global framework (or globally accepted approach) to limit and reduce aviation emissions consistent with industry's proposals.

### Preparation for the next steps

- In addition to the above mentioned efforts, AACO has been working with various international bodies to secure the interests of AACO member airlines in any global solution to tackle aviation's impact on the environment, AACO has worked on the Arab front as well in preparation for the 37<sup>th</sup> Assembly of ICAO and consequently the 16<sup>th</sup> Conference of the Parties to be held end of this year in Cancun, Mexico. The **Council of Arab Transport Ministers** have **adopted a resolution** based on a **working paper** submitted by **AACO**, as below:
  - The ministers recommended that **national delegations** to the 16<sup>th</sup> UNFCCC Conference of the Parties (**COP16**) to take with them **aviation experts**.
  - Arab Civil Aviation **Authorities** attending **ICAO's 37<sup>th</sup> Assembly** to **take** with them aviation experts from their respective national **airlines**.
- **AACO** submitted a **working paper** to the **ACAC Annual General Assembly** held in May 2010. The working paper called for the following:
  - To support reaching a **global deal** under the **umbrella of ICAO** based on what ICAO HLM agreed on (mentioned above), or any other collective option that could result from ICAO, ensuring that **earlier investments** taken by Arab airlines to renew their fleet are **taken into consideration**. In addition to **recognizing** the concept on **CBDR**.
  - AACO called the Arab Civil Aviation Authorities to take into consideration that adopting the policy of **taxes** and **charges** to deal with aviation's impact on the environment **would not resolve** the problem, but **would increase travel cost** that could threaten the strategic interests of Arab countries as most are tourist attractions.
  - Arab Civil Aviation **Authorities** to try to get **onboard** the **national delegations** of their respective governments to **COP16** in order to lobby for ICAO to be the responsible party for dealing with aviation's impact on the environment.
- **AACO participated** in the first and only meeting so far of the newly established **ACAC Environment Committee**. One of the main objectives of the meeting was to **constitute** an **ACAC position paper** to the **ICAO Assembly** in September.

**Further updates on the outcome of the ICAO 37<sup>th</sup> Assembly resolution on the Environment will be distributed in a special flyer during AACO 43<sup>rd</sup> AGM.**

## Carbon Financial Markets: Overview and Challenges:

### *New Costs but Competitive Differentials*

As the world governments debate the shape of future environmental policies, most parties are calling for the creation of a global Carbon Market. Climate policy will be written either globally, if all players agreed to join hands to address the environment issue, or individually where we will witness the emergence of individual states' environmental regulations should the global approach fail.

If either scheme takes place, a Cap-and-Trade program featuring a carbon trading mechanism will be applied. Past experience proves that market-based systems achieve the same environmental benefits of traditional command-and-control regulations, however at a much lower cost.

Adding carbon to financial products results in many questions on the policy and applications of carbon transactions. This article will shade some light on the fundamental questions: Why? How? Where? and By whom? It will be to eye opener on the challenges facing the implementation of a global carbon trading system.

### Why?

Carbon markets are ideally there for environmental purposes: regulated entities access those markets to buy & sell carbon certificates supplied by the regulators in order to cover for their emissions in excess of allocated quantities. Although the overall target is quite simple, the inclusion of carbon in commodity based financial transactions requires the highest attention and oversight from regulators due to the complexity of the financial trading system.

### How?

Carbon will be traded in primary and secondary market. Primary markets will be mostly constituted of government distributed allowances through free allocations and auctions, whereas secondary markets will be dominated by derivatives trading.

Derivative transactions include several types of financial instruments; however, the most commonly used derivatives are forward contracts, future contracts, options contracts and Swaps. As derivatives are financial products that are not limited in number as the allowances, the value of derivatives traded will be much higher than the value of underlying allowances. Looking at other commodities, the volume of oil derivatives traded in 2006 was 15 times the actual demand; another example is corn and bean future contracts that usually trade 20 to 30 times the global production of those commodities.

### Where?

Trading usually takes place on Exchanges and Over-The-Counter (OTC). Exchanges are highly regulated platforms which are characterized by transparency, absence of counterparty risk (default positions), ease of oversight, and expediency.

Over-The-Counter (OTC) transactions are less regulated than exchanges (sometimes called “dark markets”), and are characterized by more flexibility due to the lower restrictions on transparency and risk. That flexibility can take several forms, i.e. customization of contracts, flexible collateral requirements, and the ability to negotiate prices. Table 1 illustrates the characteristics of exchange versus OTC transactions.

	OTC Transactions	Exchange-based Transactions
Flexibility / propensity for customization	Contracts are shaped freely by transacting parties.	Contracts are standardized.
Transparency	The regulatory reporting of OTC transaction data is not systematically required.	Transaction data is accessible to the public and regulators.
Default protection	Counterparties assume default risk as they see fit and cash collateral or clearing is not a systematic requirement.	All exchange-based transactions must be cleared. Clearinghouses bear all credit risk.
Accessibility to small or nonfinancial players	There are no prerequisites to carry out a bilateral transaction.	Participants must be members of the exchange or have an account with a member.
Oversight efficiency	Keeping track of a multiplicity of heterogeneous transactions for which there is no organized market is more costly than keeping track of transactions on an exchange, but not impossible.	The standardized nature of contracts and the centralized, digitized, and transparent nature of trading facilitate oversight.

Source: Pew Center on Global Climate Change

## By whom?

Carbon markets are naturally very connected to other energy markets, such as natural gas, petroleum, etc. They can be accessed theoretically by financial institutions, pension funds and other passive investors, and any interested parties. However, some schemes like the EU ETS, acknowledged the delicate nature of carbon trading for some industries like air transport, for which a separate market with restricted access was created.

## Conclusion:

There are many challenges that may curb the intended goal of creating carbon markets. Previous global catastrophes caused by faults in the financial system should highlight to policy makers the critical need for appropriate market design, in addition to transparency and oversight. It is paramount to seek a proper system design that guarantees accepted tolerable balance between free trading and market oversight.

## Alternative Fuel: *The Future??*

### A needed technology

- **Fuel** is the leading cost element in airlines' **operational costs**, airlines are in constant search for **alternative measures** to reduce the consumption of fuel to **save** on the **cost** of buying, as well as **reducing emissions** resulting from fuel consumption as this too will have to be paid for in the very near future.
- **Alternative fuels** are known as **non-conventional** or advanced **fuels**, comprising materials or substances that can be used as fuels, other than conventional fuels such as fossil fuels (petroleum (oil), coal, propane, and natural gas), and nuclear materials such as uranium.
- **Biofuels** are a wide range of fuels which are **derived from biomass**. The term covers **solid biomass, liquid fuels** and **various biogases**.
- The aviation industry did not specify a "preferred" or "best" feedstock to be used for the production of bio fuel, accordingly and since **demand on bio fuel** from the aviation sector would be **large then various kinds of feedstock** will need to be used.
- It would be **important** for the industry to use **second** or **third generation biofuel**:
  - Second-generation biofuel implementation from **non-food crops**.
  - **Algae fuel**, also called third generation biofuel, is a biofuel from algae. Algae is a low-input, high-yield feedstock to produce biofuels.

### Certification

Aircraft and engine manufacturers have reported that after successful air and ground fit-for-purpose testing, jet biofuels blended 50/50 with conventional jet kerosene are likely to be certified for commercial airline use **before the end of 2010**, or **early 2011** at the latest.

### Timelines

Airbus and Boeing expect biofuels to be **available** to commercial use **within five to ten years** if government support is available.

### Major Challenges

- Scale at which aviation bio fuel can reach **scale production**? The ultimate goal of the industry is to have large units producing commercial quantities under commercially viable cost.

- **Prices** of biofuels?
- The **elements** that would **affect and determine** the **prices**?
- Involvement of **governments** to **support** the aviation industry in its quest to reduce its carbon footprint by using alternative fuels?

## Airlines

- **Airlines are cooperating with technology providers** to develop bio fuel for aircraft use.
- **Qatar Airways**, Qatar Science & Technology Park, and Qatar Petroleum reached an agreement to establish the Qatar Advanced Biofuel Platform (**QABP**) with the aim of developing a detailed engineering and implementation plan for the production and supply of sustainable **biomass-to-liquid (BTL) jet biofuel**.
- **Qatar Airways** operated the **first ever commercial passenger flight powered by fuel made from natural gas**. The aircraft is an Airbus A340-600 powered by a Rolls-Royce that was operated between London Gatwick and Doha using a jet fuel made from natural gas blended 50-50 with conventional petroleum-based kerosene. The synthetic **Gas-to-Liquid (GTL)** blended fuel was developed by Shell. The GTL kerosene will be produced in commercial quantities by the Pearl GTL project, currently under construction by Qatar Petroleum and Shell. The project is expected to produce around one million tonnes per annum of GTL kerosene from 2012. GTL Jet Fuel, with GTL kerosene up to 50 per cent, was approved as safe for use in civil aviation by ASTM International.
- **Etihad Airways** joined forces with Boeing, Honeywell fuel technology subsidiary UOP and Masdar Institute of Science & Technology on a seawater farming project aimed at growing the feedstock salicornia. The Sustainable Bio energy Research Project (SBRP) is to explore the potential of **seawater farming** as a means of **growing mangrove forests** and **salicornia** as a **bio fuel feedstock**.
- **British Airways**, in partnership with the Solena Group, is to establish a sustainable jet-fuel plant and plans to use the low-carbon fuel to power part of its fleet from 2014. The new **fuel** will be **derived from waste biomass** and manufactured in a facility that can convert a variety of waste materials, destined for landfill, into aviation fuel.
- In February 2010, **EADS** has revealed plans to assess the potential of **microalgae** over a 12-month period, in particular with Singapore's Agency for Science, Technology and Research (ASTAR) whereby the two parties will investigate methods to convert the microalgae oil to fuel.
- Other airlines from various regions of the world are also involved in alternative fuel projects or undergoing **alternative fuel test flights** like **Interjet** in Latin America, **Air New Zealand**, **Continental**, **United Airlines**, **Japan Airlines**, **KLM** and **Virgin Atlantic**, and others.
- Airlines from the **low cost sector** as well, are considering potential feedstocks including **Jatropha**, **algae**, **waste forest residues**, **organic waste streams** and the **non-edible** component of **corn**, **corn stover**.

## Technology Development: *In the near time!*

With high **fuel prices** and the impending environmental **emissions** and **noise restrictions**, and the **ageing** of the operating airline **fleet**, namely A320 family and B737, **airlines** have to **reinvest** in order to **cut costs**, mainly direct operating costs. **Manufacturers** are offering **options**:

**A new aircraft design** that would span over a decade and cost about **US\$8 billion**.

**Design of new parts** (especially **wings**): The natural occurrences of vortices around the tips of the wing limit or reduce the effective lift surface of the wing. One way to reduce this is **to place another wing on the tip of the main wing**. Boeing calls them **winglets**; Airbus calls them **sharklets** and offers them on some types of Airbus aircraft. These can either be ordered (offered) as standard on the original wing or retrofitted on a wing to **help wing efficiency, cut noise and improve fuel efficiency by** as much as 5%. The list price of winglets ranges between \$100,000-\$500,000.

**Winglets/Sharklets enable a higher RTOW** from climb limited airports (hot, high or noise abatement) or obstacle limited runways. They **allow reduced climb thrust**: A **winglet equipped aircraft** can typically take a **3% derate over the non-winglet equivalent aircraft**. This can **extend engine life and reduce maintenance costs**. The **derate** will also **reduce noise footprint by 6.5%** and **NOx emissions by 5%**, allowing good savings on airport noise quotas or charges. Cruise fuel flow is reduced by up to 6% giving savings in fuel costs and increasing range. Winglets can allow aircraft to reach higher levels sooner. This could improve an airline's step-climb performance and avoid congested airways sooner.

# AACO and Industry Issues

## Volcanic Ash Crisis *Regulatory Problem...Airlines' Malaise*

### Facts and Figures

- **Volcanic ash** from Iceland **disrupted air traffic across Europe** for almost a week in April 2010, causing the **cancellation** of some **100,000 flights**, and over 10 million passengers unable to travel. The cloud led to **USD 1.7 billion** in **lost revenues** for the airlines industry, according to IATA's estimates. AACO member airlines were amongst the airlines affected.
- During that week, **AACO airlines would have offered 27,683** seats to the **21 European countries** affected by Iceland's volcano ash cloud, **representing 3%** of the total number of available seats during that period.
- Also some **Arab airports** were **closed** due to the ash cloud that moved to Southern Europe **in May**, approaching northern Africa. **Morocco** had to close **five airports** at the time. **Spain** and **Turkey** were also amongst the countries affected.

The majority of airlines' losses were due to

- Compensating passengers
- Previewed penalties on delays and cancelation in spite of the fact that the event was a force majeure
- Grounding flights
- Uplifting more fuel to avoid restricted areas
- Crew positioning and alternate travel arrangement
- Post through-Ash maintenance checks and Service Bulletin.

### Regulatory Decisions following the Ash Cloud

- The **European Commission** has put a proposal for the EU Transport Ministers **for relief measures** following the volcanic ash cloud.
- The **EU Transport Council**:
  - **Passenger rights regulations**, including requirements that airlines pay for stranded passengers' hotel rooms, "**remain fully applicable**" and should be enforced in a **uniform manner**.
  - It is **up to individual** EU member **states** to handle **aid requests by airlines**.
  - Emphasized the importance of drafting an EU proposal for managing risk from volcanic activity and presenting it to ICAO in September.
  - Endorsed acceleration of the Single European Sky.
- The **EC** and the **National Enforcement Bodies** have reached a set of **informal guidelines on the application of** some articles of **Regulation 261/2004**. Amongst the guidelines was an agreement that the **cancellation of services due to volcanic ash** should be considered an **extraordinary circumstance** and consequently passengers have no right to compensation for flights cancelled as a direct result of that disruption. The Commission also called upon NEBs to show flexibility in the specific case of the volcanic ash.
- The **FAA exempted** volcano **cancellations** from **slot usage** rule.
- The **ICAO** European and North Atlantic Volcanic Ash Task Force (EUR/NAT VATF) agreed on a common working agenda to improve contingency plans in the European and North

Atlantic Regions. The results of the Task Force will be incorporated into the work of the **International Volcanic Ash Task Force established** by ICAO on 29 April 2010.

### **AACO Action**

- AACO acted quickly with the members to activate the “**Irregular Operations Agreement**” amongst AACO members.
- AACO was also **in contact** with various airline **associations** and **regulatory bodies**.
- AACO has **communicated with** the **European Commission** with regards to the **relief measures for** non-EU airlines and particularly **AACO members**. The **EC** stated that there is **no EU-wide support scheme for airlines**, but rather they will **allow** member **states** to grant **aids** to affected airlines **if they so wish**.

### **Safety: Top Priority**

#### **AACO's Top Objective**

“**To support the Arab airlines' quest for highest safety and security standards.**” This comes at the top of AACO's objectives. The top priority of any airline and any party working in the aviation industry is that passengers reach their destination safely. With **new technologies** and **increased coordination**, the **level of safety** has **increased** with decreasing number of accidents and incidents over the years.

#### **Global Safety**

- Though in 2008 and 2009 the number of aviation accidents remained the same but **accidents with fatal results went down** noticeably.
- In **2009**, the **Commonwealth of Independent States**, Latin America and the Caribbean, North America and Asia-Pacific had **fewer numbers** of total **accidents** than in 2008. **North Asia, Africa** and the **Middle East** and **North Africa** regions had a **higher number** of total **accidents** than in 2008. The number of accidents in **Europe** remained **unchanged**.
- Based on **IATA's figures**:
  - **2.3 billion people flew safely on 35 million flights** (27 million jet, 8 million turboprop)
  - **19 accidents** involving **western built jet aircraft** compared to 22 in 2008
  - **90 accidents (all aircraft types, Eastern and Western built)** compared to 109 in 2008
  - **18 fatal accidents (all aircraft types)** compared to 23 in 2008
  - **685 fatalities** compared to 502 in 2008

#### **Safety and Arab Airlines**

In 2009 two accidents involved Saudi airlines, two from Sudan, one from the UAE, one from Morocco and one from Yemen. **One AACO airline** was involved in a **fatal accident** being **Yemen Airways** in June **2009**.

### **Security: Another Top Priority**

#### **Security, Bridging Governmental and Commercial Requirements**

AACO (from an airline point of view) greatly appreciates the impact of a security culture on business expansion and continuity of its members and has thus its dedication in creating a security aware culture, with its:

- Contact with international regulatory bodies and consequently informing members of developments.
- Providing and supporting educational programs on a managerial level and provide training to its AACO members as well as certification in aviation security management.
- Encouraging the exchange of information between members; such as blacklisted passengers.

With security checks mainly falling under governmental jurisdiction and demand, the industry nevertheless appreciates its responsibility to maintain security with minimum if any interruption or delays to its commercial partners (Airline, Airport). This is why planting the seeds of a security culture in an Airport or Airline shall help bridge requirements.

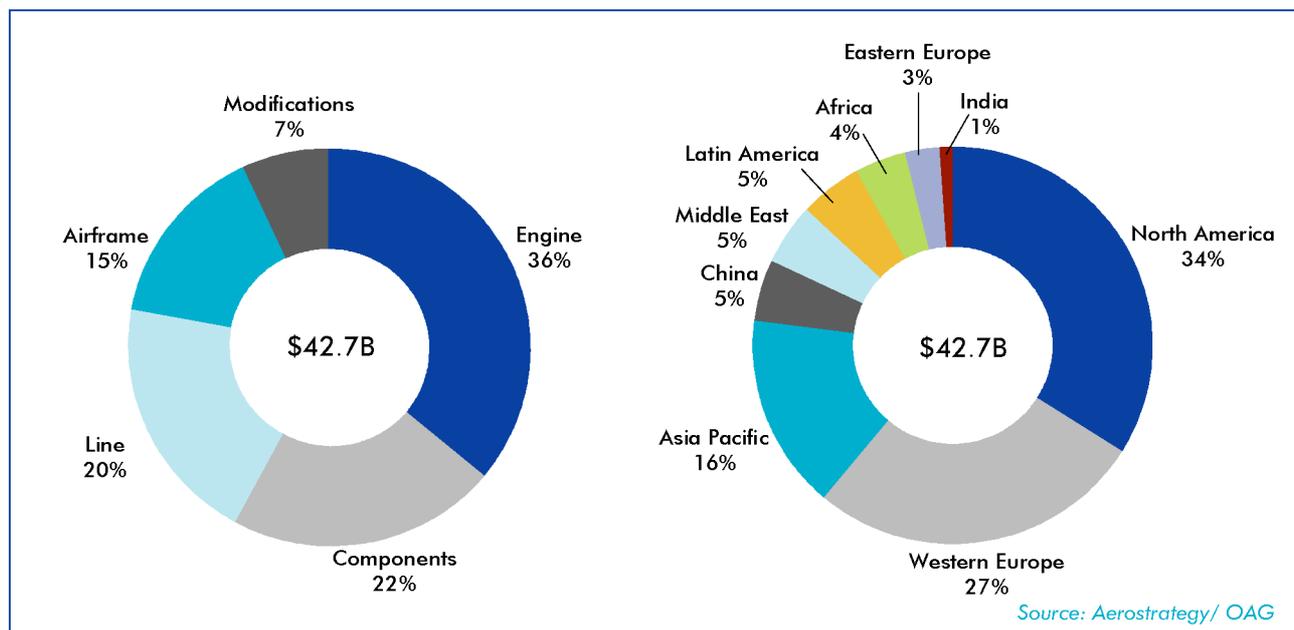
This magnifies AACO's role in promoting education and workshops. We continue to work side by side with our member airlines for individual and regional security advancement.

## Maintenance, Repair & Overhaul (MRO): *New Thrust for AACO*

### Introduction

- Maintenance, Repair, and Overhaul (**MRO**) involves all actions which have the objective of retaining or restoring an item be it an aircraft or parts to a state in which it can perform its required function. The actions include the combination of all technical and corresponding **administrative, managerial, and supervision actions.**
- **MRO Demand Factors:**
  - Aircraft cyclic Checks, Regulation adherence, part of aircraft cycle
  - Part & Aircraft refurbish: interior, avionics, IFE
  - Conversions (Primarily to cargo but not excluding Executive)
  - Paint and re-Paint
  - Dismantling and Retiring
  - Applying cost saving service bulletin (New Wings, Re-Engining)
  - Extending service life of old aircraft due new aircraft unavailability

### 2009 Air Transport MRO Market



## AACO

AACO has established an **MRO Focus Group** to **develop** and **promote technical agreements** between members in order to **save costs** and **create mutual benefits**. The joint management of spare parts and highly utilized material is among the high priorities of the group.

The **group** is currently **laying foundations** for future joint **cooperation** in areas like shared management of **spare parts** and the management, maintenance, and storage of **retired aircraft**.

## Airlines Data – MIDTs, PaxIS: *Market Knowledge*

### Latest Development

- Over the **last term**, several **changes** have occurred, namely the **European CRS Code of Conduct** proviso that prevents GDSs from showing travel agency details in Europe without the consent of those travel agencies. GDSs are obliged to seek opt-in agreements with travel agencies. The willingness of European travel agencies to grant consent varies between one European country and the other.
- **Litigation between GDSs and IATA** has **masked certain portions of PaxIS**.
- In addition to the legal masking of data, the **expansion of direct sales**, **growth of low cost carriers' market share**, and the **GDS bypass channels** affect the coverage MIDTs or BSPs provide of the actual market situation.

### Uses of Market Intelligence

- The usage of market intelligence **varies between carriers**. An **ideal situation** warrants that carriers **use market intelligence for** both sales and **planning** purposes.
- This is **not the case** for many **small** or **mid-sized carriers** in AACO who are faced with the **high cost** of market intelligence data: The reality is that in almost all cases these airlines are obliged to limit their acquisition of market intelligence, and unwillingly accept **partial visibility** through acquiring selective markets or routes.
- Moreover, the **sales power** of small or medium sized carriers in highly competitive markets might be **curtailed by** the **cost** and **difficulty** of **having strong sales teams beyond the national market**, not to mention that the **economic downturn** revealed how big players countered "sales efforts" by slashing fares to damaging low levels.
- The other uses of market intelligence, namely **network planning purposes**, is **faced by** the **cost of acquiring full data tapes** on one hand, and the **limitations of the existing data structures** on the other.

## AACO

- AACO is **working with primarily IATA** and various market intelligence and analysis **providers to arrive at** an **extensive** and **unified database** that **brings together** various **booking data** from **multiple sources**, and for **all markets** around the world whereby Arab airlines would be able to cost-effectively access this single database.

## Distribution: *The New Paradigm*

### Direct Sales

- Surveys of major airlines estimate that currently, over **40% of airlines tickets** are **sold directly** to the public, and that the **number will increase to 55% by 2013**. **Online sales** will **represent** about **38%** of the total airline sales **in 3 years**.

- **Direct sales** can be made through **airline offices, online, through call centers**, or through kiosks at airports and **key spots**. The shift of the markets towards direct sales requires the **airlines to upgrade** their **systems** in order to accommodate the new market dynamics. New trends in distribution require airline systems to up-sell bundle and unbundle fares in addition to charging for additional services such as baggage, advance seat selection, meals, special transport, frequent flyer points redemption, lounges, and other travel related services such as hotels, insurance, and car rental.
- Moreover, the fast development of mobile telecommunications makes **mobile phones/smart phones** the **fastest growing direct channel**: the airlines' ability to sell tickets through mobile sales channels is crucial.

## Arab Airlines

- The Arab airlines have **invested in their host systems and websites**. Most Arab airlines **have active websites for online sales**, and the steady growth of users of these websites is impressive.
- Still, **AACO carriers maintain** that the **travel agencies are a high yielding sales channel** which continues to bring value to the travel chain. The Arab market – public and corporate - **depends on travel agencies for customized and highly valued personalized services**. This requires moving forward with the **partnership with Global Distribution Systems** to offer the travel agency community superior distribution technology on one hand, and balancing the cost of distribution on the other.
- Currently, **18 Arab airlines are under three distribution agreements with the three GDSs, 13 airlines with Amadeus, 2 with Travelport, and 3 with Sabre**. Evidently, the partners GDSs maintain the highest market share in the assigned national markets.
- The coming period will see AACO carriers work collectively on capitalizing on the wealth of touristic, religious, and business content that the Arab world possesses.

## Low Cost Carriers: *Creativity and Branding*

### Low Cost Carriers' Focus

- Typically, what characterises the low cost carriers' operational model versus the traditional network airlines model is in the **focus of low cost carriers to cut costs on service, and to reduce operational, overhead, and distribution costs**.
- Low cost carriers also focus on **shorter point to point operations and single type aircraft fleet** out of **secondary airports**.
- Still, there were **changes** to that model in the last few years whereby low cost carriers add frills while **network carriers emulate the LCC model** to cut costs and streamline operations, and many network carriers, including airlines in the Arab world, are operating higher frequencies between cities using smaller aircraft.

### Arab Region

- In 2000 **low cost airlines** had no presence in the Arab region. In **2010**, they have around **6% of seat capacity**, and are **expected to grow to 8% in 2011**.
- **LCCs Fleet** (As at 18 August 2010): **Air Arabia** operates **18 new Airbus A320s** and has **44 on order** from Airbus. **FlyDubai**, operating from Dubai with a current fleet of **9 aircraft**, plans to have a fleet over **50 aircraft by 2015**. In Kuwait, **Jazeera Airways** operates a fleet of **8 aircraft** and has **29 on order**. Saudi based **NasAir** operates a fleet of 3 aircraft and has **27 on order**, while **Bahrain Air** currently operates **5 aircraft**. Abu Dhabi is contemplating a launch of an LCC of its own in the coming period. In other Arab countries, Yemen based **Felix Airways** fleet currently includes **4 aircraft** with **6 on order**. In Morocco, in addition to **Air Arabia Maroc** operating **3 aircraft** at the

moment, 2 Low Cost Carriers operate in Morocco - **jet4you** and **Atlas Blue**- operating **6 and 5 aircraft** respectively. **Karthago** Airlines in Tunis operates **4 aircraft**, while **Air Arabia Egypt** operates **2 aircraft**.

- **Low cost carriers** that operate from secondary or regional hubs have a positive contribution to **boosting regional traffic**. In a geographically widespread stretch such as the Arab World, the low cost carriers have an important economic and social role to play by serving and developing secondary hubs. **Air Arabia**, which started operations in 2003 out of Sharjah- UAE, now **operates** to over **60 destinations** across the region out of **4 operational hubs: Sharjah, Casablanca, Alexandria, and Amman in the near future**. It has played a crucial role in boosting the airport positioning of Sharjah Airport from 1.6 million passengers in 2004 to over 5.7 million passengers in 2009.
- In the Arab world, **Air Arabia** is a **success example** of a low cost carrier in terms of unit cost that has adapted itself to the Arab region's market demands by incorporating some non-LCC features to its operating model such as free baggage allowance and wide leg room while still maintaining a low unit cost (5.66 cents in 2008 and 4.3 cents in 2009), but the success story of Air Arabia is not necessarily the case with existing LCCs in the region.
- The **growth of the low cost carrier model** in the Arab world, which has benefited from the growth of intra-Arab passenger traffic, is still at its **early stages due to the slow paced liberalization** on one hand and **travel restrictions** between some Arab states on the other.
- For the low cost operators in the region, **there is room for more growth** for operations particularly to and from secondary and underserved areas, and to stimulate travel among certain age and budget groups. It remains that uncalculated expansion, capacity dumping and price wars can prove detrimental to several start-up low cost carriers.
- In the Arab world, where the **market is expanding**, and where **premium service is a prerequisite** for a large number of the travelling public, **flag carriers** in the Arab world **were not negatively affected by the rise of low cost carriers – in terms of passenger numbers, however** there is admittedly a **pressure on yields** in several markets for all operators, LCCs included.

## **Airlines' Cooperation – Alliances and Mergers:** *Bigger but not Alone*

### **Available Cooperation**

Amidst the global **economical pressures**, increasing **fuel prices**, and **regulatory challenges**, **airlines** are **seeking cooperation** and **consolidation** as a **solution** to the heap of problems facing the industry. Solutions currently available to the airlines **include interline agreements, code shares, alliances** and **mergers** and **acquisitions** which obviously have many strategic advantages over unilateral approaches.

**Interline agreements:** allow an airline to sell another carrier's flight under one ticket. These ticketing arrangements provide **revenue boost** and **increased customer satisfaction**.

**Codeshares:** Code shares can be particularly advantageous as a means of **eliminating excessive competition and overcapacity** on thin routes. The **marketing airline gains an extended network** and reach to un-served or underserved markets, without requiring the dedication of a hull.

**Consolidation** between airlines is viewed as means to reverse the vicious cycle of losses, competition, over capacity, labor contracts, and other operational inefficiencies. Also **Mergers** and **Acquisitions** **promise higher returns and decreased risk** through the establishment of a central entity with control of capacity, pricing power and economies of scale. **However, barriers** to these transactions are **not to be underestimated**.

## Existing Barriers to cross-border cooperation/consolidation

**Operational:** Existing bilaterals that restrict market access and frequencies, antitrust and competition regulation, and some governments' actions to protect flag carriers.

**Ownership:** constitutional requirements for majority local ownership and substantive ownership clauses in bilateral agreements.

**Labor:** Unions oppositions and harmonization of contracts.

**Shareholder/Management:** Shareholder's support and management disagreement on merged teams and control.

**Logistical:** System integrations, fleet optimizations, and capacity rationalization.

## Arab Airlines

The Arab airlines are divided into two categories.

- **Mega carriers:** The self reliant mega carriers in the Arab region are expanding their fleet and network coverage. These airlines are developing their hubs in the Arab region, and attracting traffic with their premium services, at a time when the traditional hubs in Europe for example suffer from congestion and deteriorating services. The mega carriers, for reasons of their own, or reasons emanating from the alliances themselves, would not become alliance members in the foreseeable future.
- **Medium to Small sized carriers:** Joining an alliance means that passengers would have wider access to the joint network of an alliance that may not be feasible for a single airline to operate to.
- The Arab world might see additional airlines join an alliance in the near future, in addition to **Royal Jordanian** and **EgyptAir** who are already members in **oneworld** and **Star** alliances respectively.

## Arabesk

- In response to the **need for collaboration** between airlines, and in the **absence of the regulatory environment** that would drive towards consolidation between AACO members, **AACO** launched **Arabesk Network Cooperation Project** in **2005**. The Project unites **a number of AACO member airlines** to **align schedules, link networks and destinations** in order to **gain competitive advantage** in the Arab Air Transport Market.
- **Arabesk** aims to **strengthen the competitive stance and connecting networks** and to evolve from a group of separate markets to a more unified market, giving the operating Arab airlines a **stronger leverage**, and enabling them to **better cover** their **national markets** and **improve** their **competitive positioning**.
- In its **four years** of actual operations, **Arabesk** has **achieved** around **US\$80 million** on codeshare revenues by mid-2010, at an average US\$20 million annually. The cooperation has also protected the yields of member carriers on the joint network.

## Variation of Fuel Prices: *A Reprieve from Speculation*

*AACO member airlines' fuel bill decreased by 23.1% in 2009 over 2008*

## Factors Governing Oil Prices

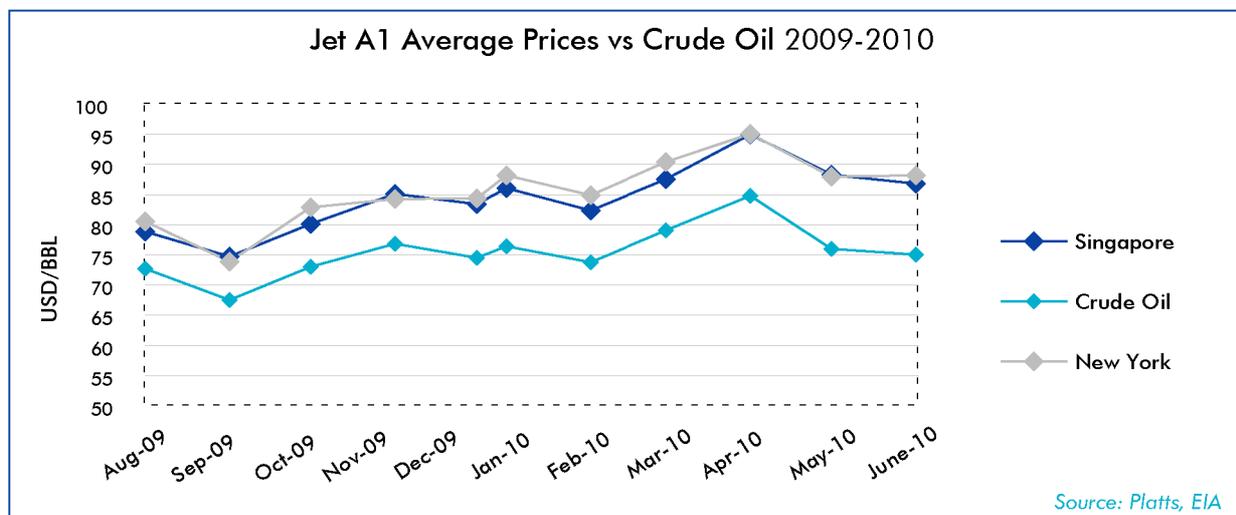
- Two primary factors: **supply and demand**
- **Other factors:** **proportion of oil refineries productions, cost of transportation and shipping** and the impact of **fluctuation in financial markets**. In addition to the **geopolitical changes**, as well as **crude oil supply** and **petroleum quantity**, especially in situations of economic recessions.

## Variations and Airlines' Costs

- Oil price entered the first week of **January 2010** (80.67\$/bbl) with an **increase of 13%**, the highest price increase since October 2008 (71.4\$/bbl), **followed by a slight decline** in the price with a range of **4%** as average for February over January 2009, where the index of fuel bill increase declined from **18 to 16 billion dollars** (IATA). In spite of that, the fuel bill still represents a very significant cost item for airlines, around **30% - 40% of airline budget**. The **total annual fuel bill for the aviation industry in 2009** is estimated at **\$113 billion**, compared to \$189 billion in 2008, where fuel accounted for 24% of total airline operating costs.
- As for **AACO member airlines**, the **fuel bill decreased by 23.1% in 2009** (for **11 airlines** only) over 2008 **reaching \$4.7 billion**, and amounting to **26.67% of their total operating expenses**.

## Variations Continued...

- Due to the above mentioned factors, energy price forecasts are highly uncertain. **Crude Oil prices fluctuated** considerably during **May 2010**, ranging from a **high average of \$88/bbl to a low of \$67/bbl**.
- According to some market analysts, uncertainty over the global economic recovery, particularly with respect to Europe's debt crisis and the tightening of credit by China, and liquidation of future contracts contributed to the crude oil decline. On the other hand, the worst oil spill disaster in US history, gushed at a rate of up to 60,000 barrels per day according to some estimates, along with a six-month moratorium that began in late May on new deep water drilling in the U.S, was not enough to prevent crude oil prices from falling nearly 10-12% over the period April to June as the sluggish world economy kept a lid on demand.



## Joint Fuel Purchasing

### Commercial Achievements

AACO works to successfully consummate profitable savings by reducing the cost of fuel purchasing to its member airlines at worldwide airports.

By the beginning of its second decade, the board achieved the highest amount of savings.

- During the past period, the Joint Fuel Steering Board worked on getting **lower prices** and **adjusting the contractual terms**, through implementing a **clear mechanism** and the adoption of systematic exclusion of suppliers at certain cases during the negotiations.
- This method of **transparency** in the **negotiations** during 2010 helped AACO achieve **excellent results; increasing** the level of **savings** to member airlines by **98% over the year 2006**.

- As for **AACO Tender – 2010, 460 airports** were included to cover around **520 million gallons** of the fuel requirements. The qualitative plan implemented by the board was the main factor in attaining the highest amount of **savings** estimated at a **25% increase** over 2009 results.
- The Steering Board is working on developing the collaboration with the suppliers and enhancing bilateral cooperation in Arab stations particularly in Bahrain, Saudi Arabia, Qatar and Algeria.

## Awareness

AACO Fuel Technical Committee played an important role to enhance and expand the knowledge base of AACO member airlines, through holding the **4th Aviation Fuel Forum** in cooperation with the Joint Fuel Purchasing Steering Board. The **event dealt with** the current and future **challenges** facing AACO member airlines **within** the **environmental, technical**, management and **safety** disciplines.

## Joint Cooperation at Outstations

AACO's project promoting joint cooperation at outstations has been **one of AACO's pillar joint projects** for more than a decade. The objective of the project is to **maintain** and **enhance** the **quality of services** delivered to member airlines **at outstations** at **reduced costs**, as well as **improving** the **contractual terms** with service providers in the following **domains**:

### □ Ground Handling Services

- Developments at outstations along with all related **legislation** and emerging matters.
- Exploring **further possibilities** like CIP Lounges, common Check-In areas... and other areas.

The Board has signed a number of Joint Ground Handling **agreements** with various service providers at outstations such as **Swissport, AFSL, Fraport, ADRH, and Havas**.

During this term, the Board has signed a new Joint Ground Handling Agreement with HAVAS that covers Atatürk Airport in Istanbul and 10 other Turkish airports. The new agreement offers all project carriers an enhanced quality of service to their passengers while controlling operational cost.

The Board is constantly working on expanding the project to cover more stations as well.

## AACO Regional Training Center

### Cooperation with Academic Institutions

#### American University of Cairo (AUC)

- AACO has worked closely with the American University of Cairo (AUC) that is working with AACO RTC to design the needed management programs which resulted in 4 initial management programs:
  - Post graduate diploma in Aviation Management
  - Post graduate diploma in Air Travel Marketing
  - Post graduate diploma in Passenger Handling Management at Airports
  - Professional Certificate in Emergency Response Planning & Disaster Management in Aviation

- The 4 programs were designed to comply with the rules of the Higher Education authorities as to be approved as accredited post graduate programs, and the AUC was successfully able to accredit the first 3 programs, while the 4th is expected by the beginning of 2011.
- These programs will be conducted in-house at the airlines' home bases to provide the service for their maximum number of staff at the lowest cost.

### Helwan University - Cairo

- In June 2006 a cooperation protocol was signed between AACO and Helwan University which paved the way for the first group of 32 researchers who started their study in February 2009 and expect to finish by October 2010. This program is sponsored by EGYPTAIR and conducted at Faculty of Tourism & Hotels premises in Cairo.
- The second group started their study including 33 participants in May 2010 and are expected to finish the program in January 2012.

### Concordia University - Montreal

- AACO has also extended its collaboration with Concordia University in Montreal – Canada in which AACO has also succeeded to sign an agreement with John Molson School of Business to introduce its (AVSEC PM) Aviation Security Professional Management Program in the Middle East region. This program is conducted in cooperation with ICAO, and AACO is coordinating for it to be conducted in the region and offer this service for members.

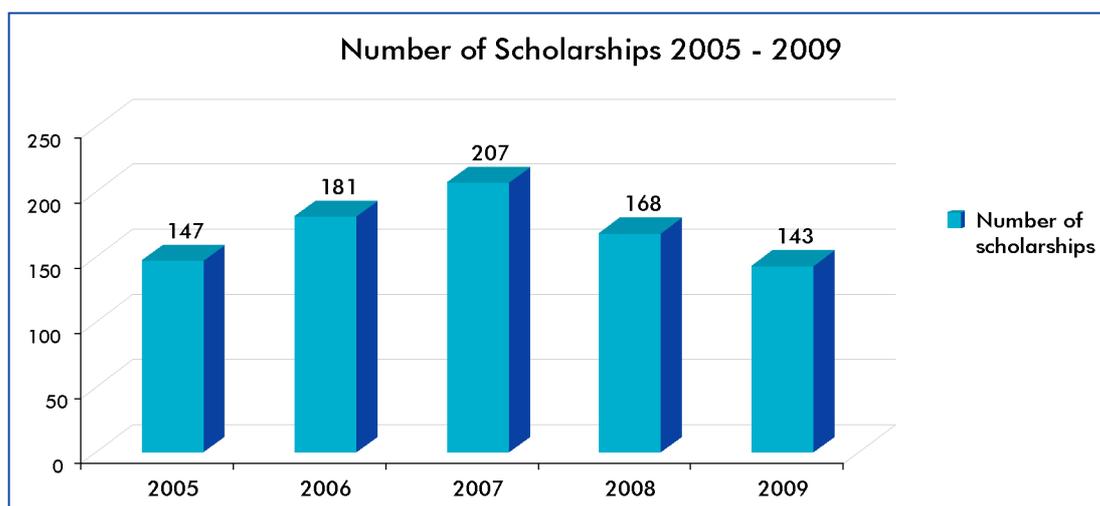
### Balamand University – Lebanon

- On the technical and maintenance side, AACO has signed a protocol with Balamand University – Lebanon, targeting cooperation with the Faculty of Engineering and the Faculty of Business Administration & Economics.

### What AACO Regional Training Center in Amman is doing

- AACO Regional Training Center which was established in Amman in 1996 has trained 20,999 trainees, conducting 1,161 training courses till mid 2010.
- Total **number of participants** in AACO RTC courses in **2009** was **2,158 participants** in 129 training courses, **providing quality training with lower cost.**
- AACO together with the Industry Partners through the Industry Partnership Program (IPP) have secured 143 scholarship in 2009.

**Graph showing number of scholarships funded by Industry partners from 2005 till 2009.**



## New Branch in Cairo

□ In **2009**, AACO finalized a **diplomatic agreement with the Government of the Arab Republic of Egypt with the support of EgyptAir to establish a branch for AACO RTC in Cairo**; this branch had started its soft operations in May 2010, and is expected to operate in full after the opening of EgyptAir Training Center new extension located at Cairo Airport.

**EgyptAir** had **generously hosted the new branch in Cairo** inside the new extension of EgyptAir Training Center, and offered its full support.

## Human Resources Development Steering Board

□ **AACO Human Resources Development Steering Board** has **reviewed the Joint Purchase projects** it is overseeing:

- The **ICAO English Language Proficiency (ELP) online tests**
- The **online assessment tests** using different types of tests used for recruitment, assessment and relocation inside the airlines. This includes tests specially designed for some airline jobs, and **AACO members were offered an open license** for unlimited number of tests per year.

## Arab Air Transport Database – AACO’s Publications

### The NASHRA - Industry's Pulse & Arab Aviation - Monthly

The **NASHRA** is **AACO’s Official Monthly Bulletin** that is distributed electronically in the English language. It is a monthly recap of aviation in the Arab world on a regional and International levels. Major issues covered in the NASHRA include:

- **Major developments** in the Arab aviation industry at various levels.
- **Statistical monthly data** related to the Arab world on passenger traffic flows, market shares, available capacity for Arab airlines and foreign airlines in the Arab world, Fuel update and others.
- AACO’s **Industry Partners news** – dedicated to our partners who sponsor this bulletin. The NASHRA is distributed to the CEOs and Executives of AACO member airlines, Director Generals and senior management of Civil Aviation Authorities in the Arab world, Transport, Tourism and Economy’s ministers in the Arab countries, worldwide regional associations and IATA, media around the world and AACO’s Industry Partners.

### AATS – Arab Air Transport Statistics

This **annual bulletin** highlights the **major operational developments** related to the **Arab airlines and airports** as well as a synopsis on the **world air transport developments** at large. It also includes some **vital statistics** on general economic trends with a particular emphasis on the ones which are more related to Arab Travel & Tourism sector.

It is distributed, in printed format, to the CEOs of AACO members and industry partners. This publication is in English language only.

### AACO Annual Report

AACO annual report is the **yearly harvest of all AACO achievements, developments, industry challenges and joint projects results**. A yearly update is distributed during AACO AGMs. It is in printed format, in **English and Arabic**.

### Weekly Web News

It is a weekly update on the **top and latest developments posted on a daily basis on our homepage** covering the previous week’s news. It is a link to our list of Arabic and English

news with the possibility of selecting, previewing and printing them as well as searching the News Archive.

<http://www.aaco.org/pub.asp>

### **Safe and Level**

It is about **major safety developments**, accidents and reports in the aviation at the international and regional levels. Its circulation is restricted to AACO technical committee and sub committees. This English newsletter is published **every month**.

### **RTC Catalogue**

The Regional Training Center catalogue is a detailed description of the yearly training courses. This catalogue helps in giving the trainees detailed information about the courses facilitating their choice of course, registration and accommodation.

<http://www.aacortc.com>

### **3D-Insight "AACO Quarterly Statistical Bulletin"**

3D insight "**AACO Quarterly Statistical Bulletin**" is a quarterly **electronic statistical** and **analytical** bulletin in English. This bulletin is in collaboration with Seabury Aviation & Aerospace and it contains a **detailed analysis of industry topics** affecting the Arab aviation market, in addition to **Arab airports statistics, Arab airlines operations data, and Arab fleet** data.

### **TOP VIEW**

A new **electronic** bulletin dedicated for **briefing the CEOs of AACO members** about the major industry developments and AACO's activities in a **very concise** and **executive** manner. The TOP VIEW bulletin is issued **every two months**.

## **External Representation and Regional Cooperation**

**AACO cooperates** with **regional and international organizations, governmental and non-governmental bodies, foreign airlines, manufacturers and service providers**, offering a broad **framework of cooperation for AACO members, protection** of their **interests, and support for better economic environment** for their operations.

The **coordination and cooperation** takes place at various levels and includes the **commercial, regulatory, legal, and operational** aspects, through continuous communication with **IATA, ICAO, ACAC, the Arab League, the European Commission, the U.S. Department of Transportation, and regional airline associations** around the world, **Arab civil aviation authorities, and environmental and aviation authorities in Europe**, and several b.

AACO also has a **solid base of industry partners** under the Industry Partnership program since 1998, and today brings together more than **49 partners** of aircraft and engine manufacturers, IT companies and global distribution systems, fuel companies, engines and aircraft leasing companies, consulting firms, ground-handling companies, financial firms and others. The program creates a mutually beneficial environment where partners benefit from AACO events and activities to strengthen their relations with member airlines, while AACO benefits from partner support in the various training programs and numerous other benefits to member airlines.

