



THE IMPACT OF OPEN SKIES FOR IB

Strategy and Corporate Development Direction

April 17th, 2008

OPEN SKIES

1. Brief historic analysis of Open Skies

- ✓ First steps and negotiations
- ✓ Major constraints and shadows on the process
- ✓ Final Implementation
- ✓ Current conditions and limits to the Agreement

2. Consequences of liberalisation. Background

- ✓ United States: 1978
- ✓ Europe: 1996

3. North Atlantic open skies

- ✓ Dimension of North – Atlantic
- ✓ North Atlantic LCCs
- ✓ Consolidation / Elimination of Foreign Ownership Restrictions
- ✓ Major consequences of Open Skies : Traffic and competition increase
- ✓ Further consolidation of liberalisation to other markets (5 to 10 years)

4. Impact of Open skies for Iberia

- ✓ Role of Iberia on process of Air Transport consolidation
- ✓ Allows a deeper relation with strategic partners: AA (ATI) and BA (JV)
- ✓ Improve efficiency or risk exiting business.



Brief Historic Analysis

- ✓ **2003: The first steps towards the EU/US Air Transport Agreement go back to June of this year.** The objective of the mandate agreed at the Transport Council was to create an open market for aviation between and within the EU and US.
- ✓ **2005: Although some improvements are made on the enhancement of co-operation on regulatory issues,** the fields of ownership and control of airlines pose already a major constraint for further development on the agreement.
- ✓ **2006:** Following the withdrawal of the US Administration proposal in December 2006, in response to strong opposition in the US, the Transport Council urges the Commission to enter into urgent consultations with the US to seek elements that could be used to restore a proper balance of interests
- ✓ **2007: Following three rounds of negotiations early 2007, the Commission obtained a number of important elements and strengthened the commitment by both sides to a second stage of Agreements.**



Brief Historic Analysis: April 2008 Balance

- The major objectives achieved as of April 2008 are :
 - **7th Freedom Rights for EU operators between EU and USA.**
 - **Antitrust immunity for operators and alliances.**
 - **Price fixing liberty**
 - **3rd, 4th, 5th and 6th Freedom Rights**
 - **Branding and Franchise between operators of both US and EU**



Brief Historic Analysis: 2007 Commitments

But **still the current Treaty poses important restrictions** to an ideal full liberalized market, chiefly **in the fields of cabotage and ownership**.

There is a commitment from American side to achieve the following in the medium term:

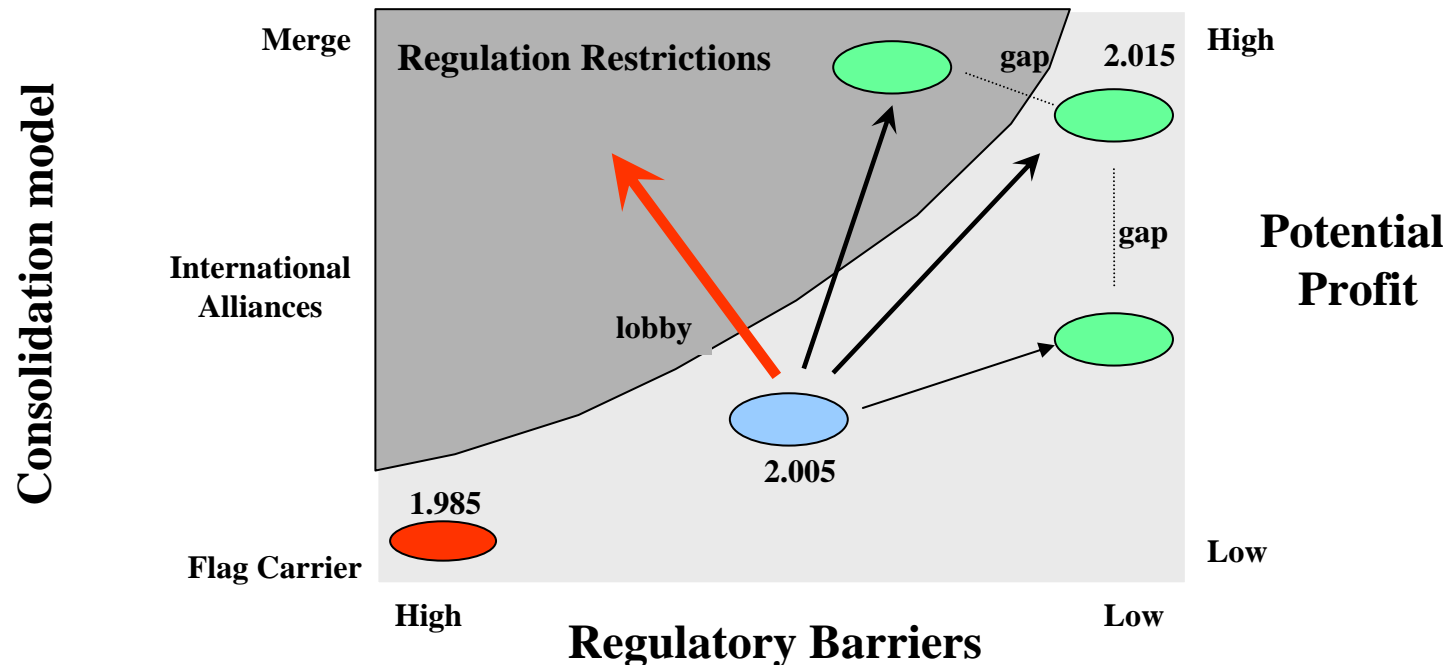
- **Percentage of US airlines equity that EU nationals may hold, including the option to hold more than 50% of total equity**
- **Guaranteeing fair and expeditious consideration of a transaction involving investment by EU nationals in US airlines**
- **Giving EU airlines operating to the US greater access to non-EU capital**
- **Allowing airlines of several 3rd countries operating to the US to be owned and controlled by EU nationals.**
- **Cabotage rights in US and EU territories (Probably this right will be reached by US carriers before than by EU operators)**

Consequences of Liberalisation: A Historical Perspective

During the last three decades, liberalisation has always produced major structural changes with the appearance of new players

- I.e. Easyjet and Ryanair or AF-KL or LH-LX, DL-NW

Liberalization → Competition → Consolidation



Consequences of Liberalisation: A Historical Perspective

USA

- **1978:** Airline Deregulation Act
- **1978-1990:** 1st consolidation process of USA Air Transport : Development of Southwest and People Express. Braniff and Eastern disappear
- **1991-2001:** 2nd consolidation process. PanAm disappear and American Airlines buys TWA. Hub and spoke model is developed.
- **2001-2007:** Crisis of American Network operators : United, Delta, US Airways and Northwest enter into "Chapter 11". Second phase of growth of Southwest y Jet Blue.
- **2007:** Open Skies Agreement is announced in the North Atlantic
- **2008:** Delta an Northwest combination

**Liberalisation of US Air Transport:
Increased competition
New players appear**

US Air Transport consolidation

EUROPE

- **1992:** Spanish government liberalizes Spanish Domestic Air Transport : New players appear: Air Europa y Spanair
- **1994:** Air France buys UTA and Air Inter and strengthens CDG Hub
- **1996:** Liberalisation of European Air Transport. New players: Easyjet and Ryanair
- **1997:** Iberia takes over Aviaco
- **2001:** New business model for Sabena and Swissair
- **2002-2003:** EasyJet buys Go, and Ryanair gets Buzz,
- **2004:** Consolidation: Air France+ KLM
- **2005:** Lufthansa absorbs Swiss
- **2001-2006:** State financial aids to Olympic and Alitalia

European liberalisation gets started

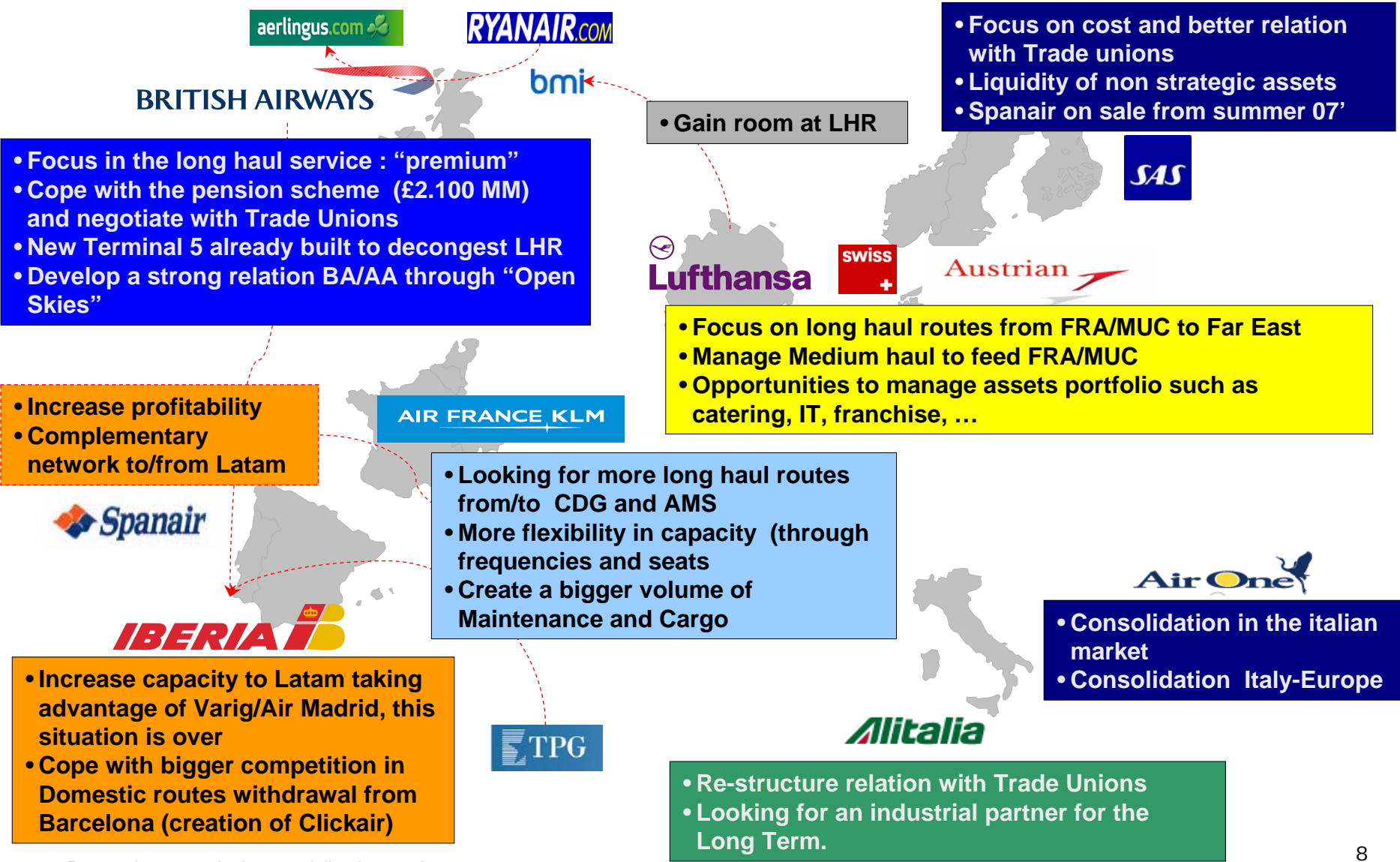
**European Liberalisation:
Competition increases. First European LCC's**

Some flag carriers change their model

European consolidation gets started

- Operations influenced by liberalisation
- Key Element of liberalisation

Consequences of Liberalisation: A Historical Perspective



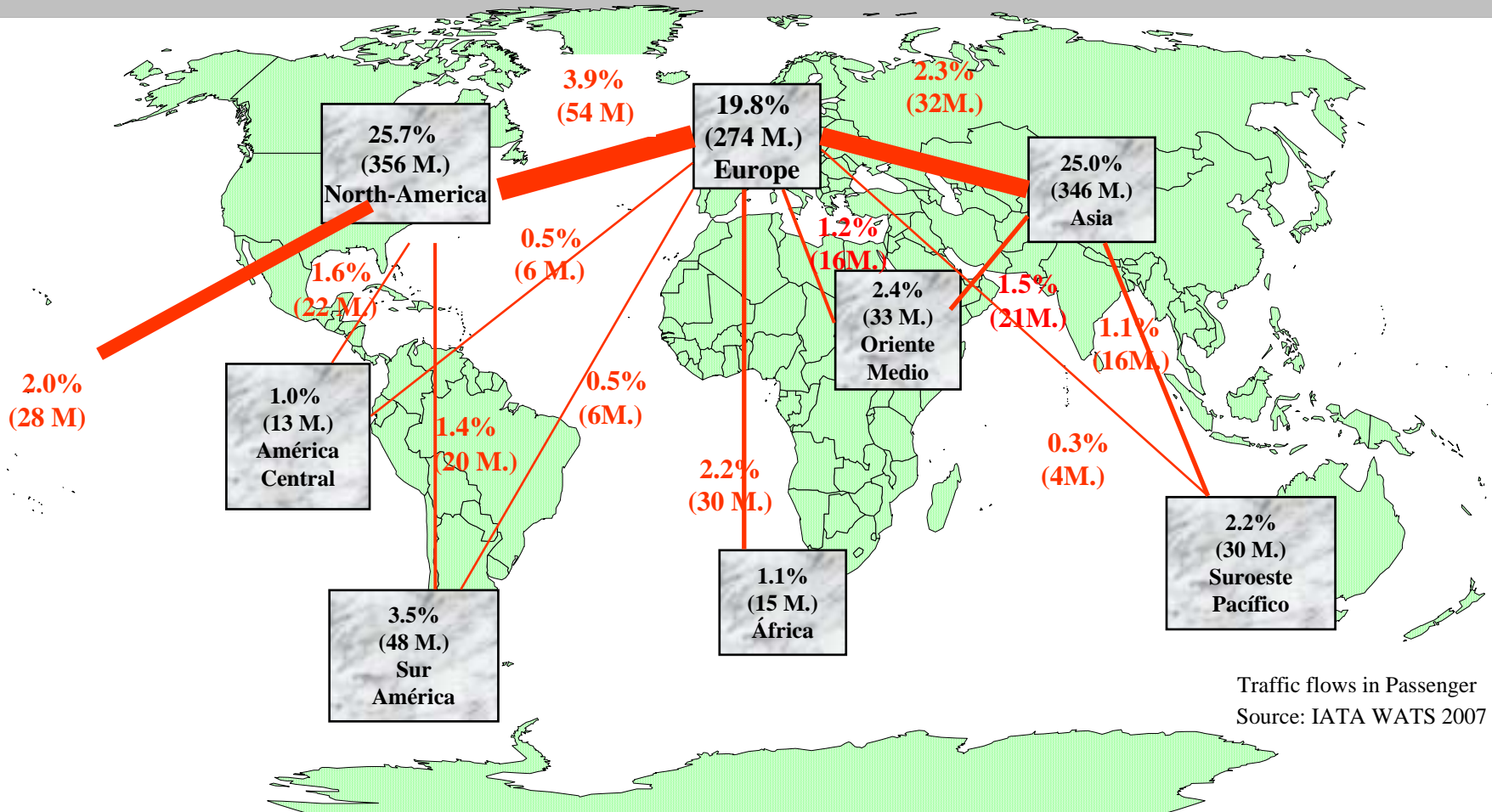
source: Press releases and other specialized magazines

Consequences of Liberalisation: A Historical Perspective

- ✓ Process of consolidation already in place: Air France-KLM, Lufthansa-Swiss and Tap-Portugalia, Delta and Northwest ... and may continue with Alitalia, BMI, Austrian, Aer Lingus, Spanair and SAS
- ✓ LCCs have also participate in this process (Easyjet-Go, Ryanair-Buzz and Air Berlin-LTU)
- ✓ Consolidation process in North-Atlantic scale might be delayed some time due to different reasons:
 - **Current limitation to foreign ownership of American carriers (25%) and European (49%). These constraints will probably not be released until American carriers are able to lead this process showing sign of strength ⁽¹⁾**
 - **Up to now these consolidation processes have only involved carriers within the same region**
 - **There is normally a time gap between a market deregulation and the beginning of consolidation on the new area created.**
 - **Although Alliances model to obtain further synergies seems to vanish, this processes will be extended in the North-Atlantic area until proper conditions for integration are in place.**

(1) Combinations such as recent Delta-Northwest may occur in the medium term in order to cope with higher fuel prices, improve efficiencies, increase international presence and fund long-term investment in the business.

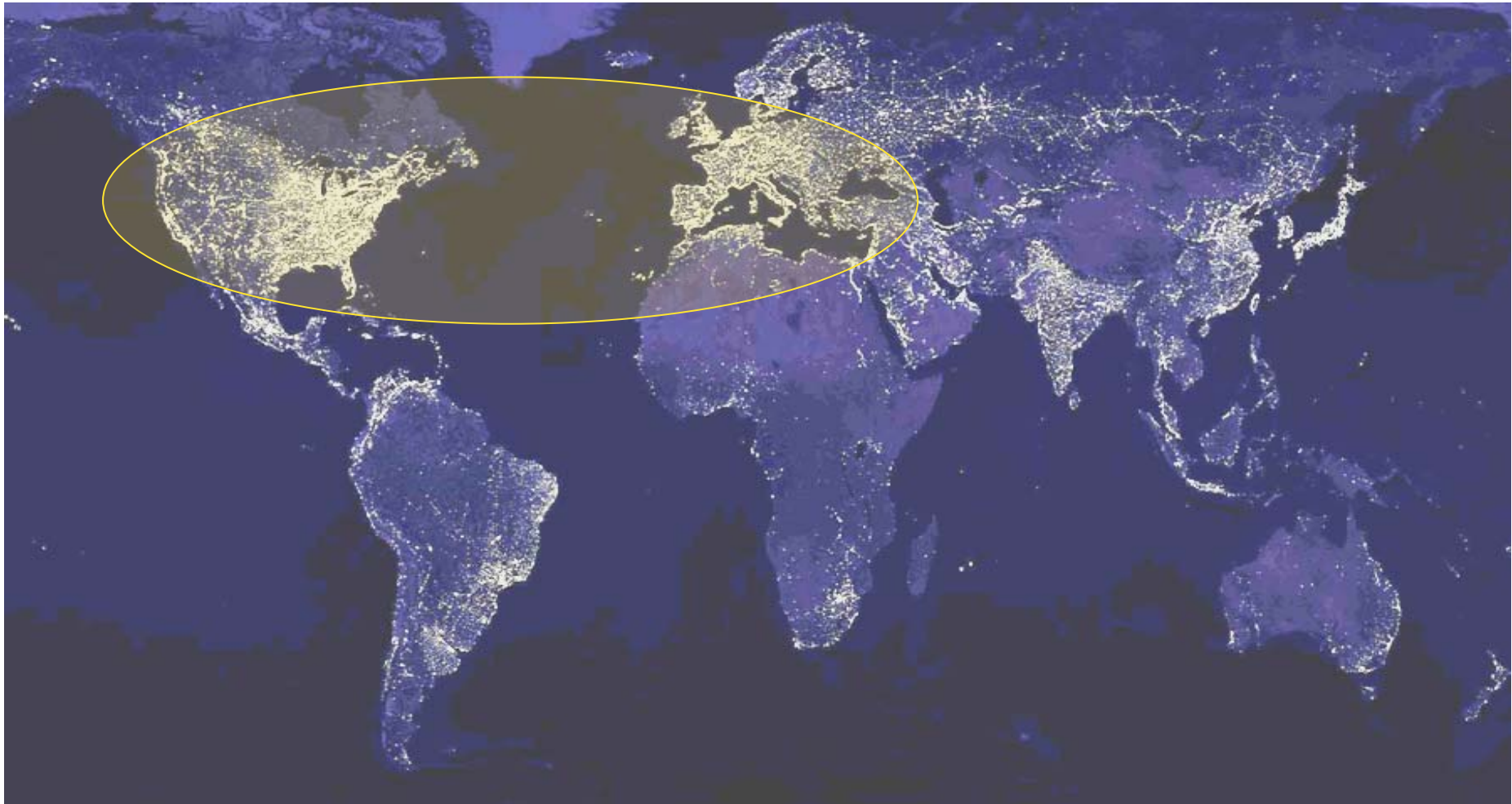
North Atlantic Open Skies



North-Atlantic region (Long-haul traffic + Intra-Europe + Intra-USA) accounts for almost 50% of the total world-wide passengers.

More than 50M pax travelled along the transatlantic corridor during 2007

North Atlantic Open Skies




Regarding GDP during 2007,
Europe and USA account for more than 59% of the total world wealth
(*Global insight WMM 2007*)



North Atlantic Open Skies

- ✓ The Air Transport Agreement between the EU and the US **is the first agreement covering longhaul intercontinental flights.**
- ✓ As it has happened from the late seventies, the process of deregulation **will inevitably bring new players to the market ; New LCCs** and consolidation processes may occur.
- ✓ The current restriction on foreign ownership will have to be released so that North-Atlantic consolidation process is possible.
- ✓ The current treaty will inexorably **produce an increase of traffic and competition** (see next slide)
- ✓ Presumably **the liberalization of North-Atlantic region will have a cascade effect in other world regions.** In the next 5-10 years Mid-Atlantic, South Atlantic and Far East will follow the trend.



North Atlantic Open Skies: Increase Of Traffic And Competition

- ✓ From the first day of the application of the Agreement numerous new flights between EU and the US have taken off to new destinations. **In April-June 2008 number of flights will be 8% higher than 2007.**
- ✓ Transatlantic services will increase particularly in those Member States where there have been restrictions so far: **In LHR alone, flights to the US are increased by 18 dailiy (more than 20%)**
- ✓ More than **400 daily flights are operated between the EU and the US** in April 2008.
- ✓ Airlines are making use of the opportunity to operate transatlantic flights from outside their home country: **Air France is operating from London to Los Angeles.**
- ✓ Many airlines make use of the extended codesharing and alliances opportunities. **Sky Team partners AF-KL, Delta and Northwest have applied for a four-way-joint-venture, oneworld has appllied for ATI**



North Atlantic Open Skies: SWOT Summary from Airline perspective

THREATS

- Deregulation will bring new operators to this market (new LCCs + new global airlines as the result of consolidation)
.....Only most efficient will survive!

OPPORTUNITIES

- New opportunities in the field of cooperation, joint ventures, and code-sharing
- The process of consolidation already started could be expanded in a major scale with transatlantic combinations.

STRENGTHS

- Deregulation will liberalize the market, and allow operators to increase services in the existing routes (LHR), open new routes, and offer reduced fares to customers.
- Standardized measures concerning safety regulation

WEAKNESS

- Foreign ownership limited in USA and Europe ; not expected to be released until US operators improve their financial situation..
- Cabotage rights still not allowed.

Restructuration of Flag Carriers

OPEN SKIES

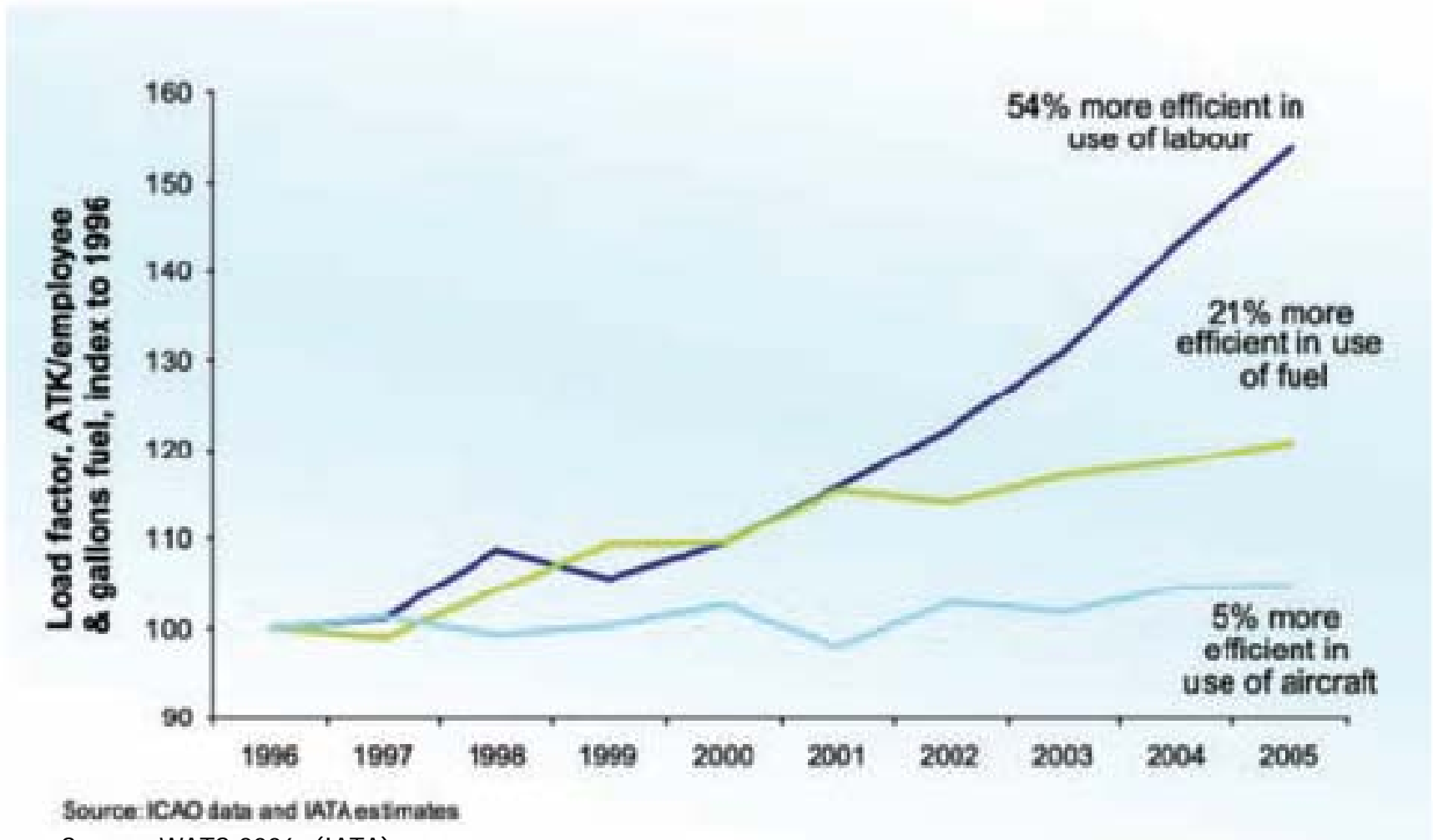
	End 2000	End 2006	Change % 2000-2006
American Airlines	112,3	71,0	-36,8
United Airlines	101,8	51,9	-49,0
Delta	72,3	45,7	-36,8
Northwest	54,4	31,3	-42,5
Continental	48,1	42,5	-11,6
US Airways	42,1	20,8	-50,6
<i>Sub-total US</i>	431,0	263,2	-38,9

Europe

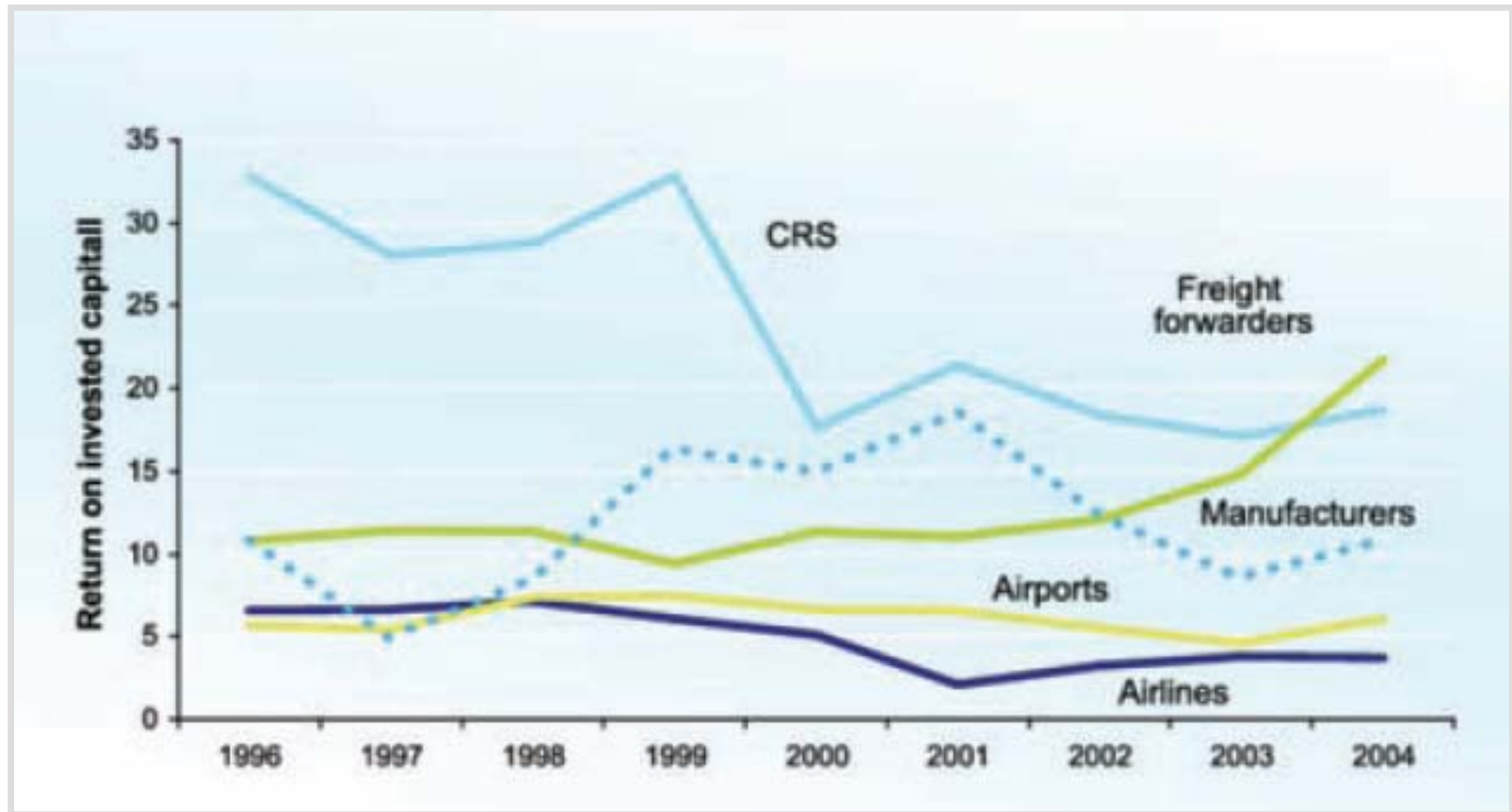
Air France	56,4	60,0	6,4
British Airways	55,3	46,2	-16,5
KLM	27,5	25,7	-6,5
Iberia	26,8	25,0	-6,7
Alitalia	21,7	19,7	-9,2
<i>Sub-total Europe</i>	187,7	176,6	-5,9

Flag carriers have been obliged to reduce labour costs
due to exogenous (Sep/11th) and endogenous circumstances

Efficiency improvements



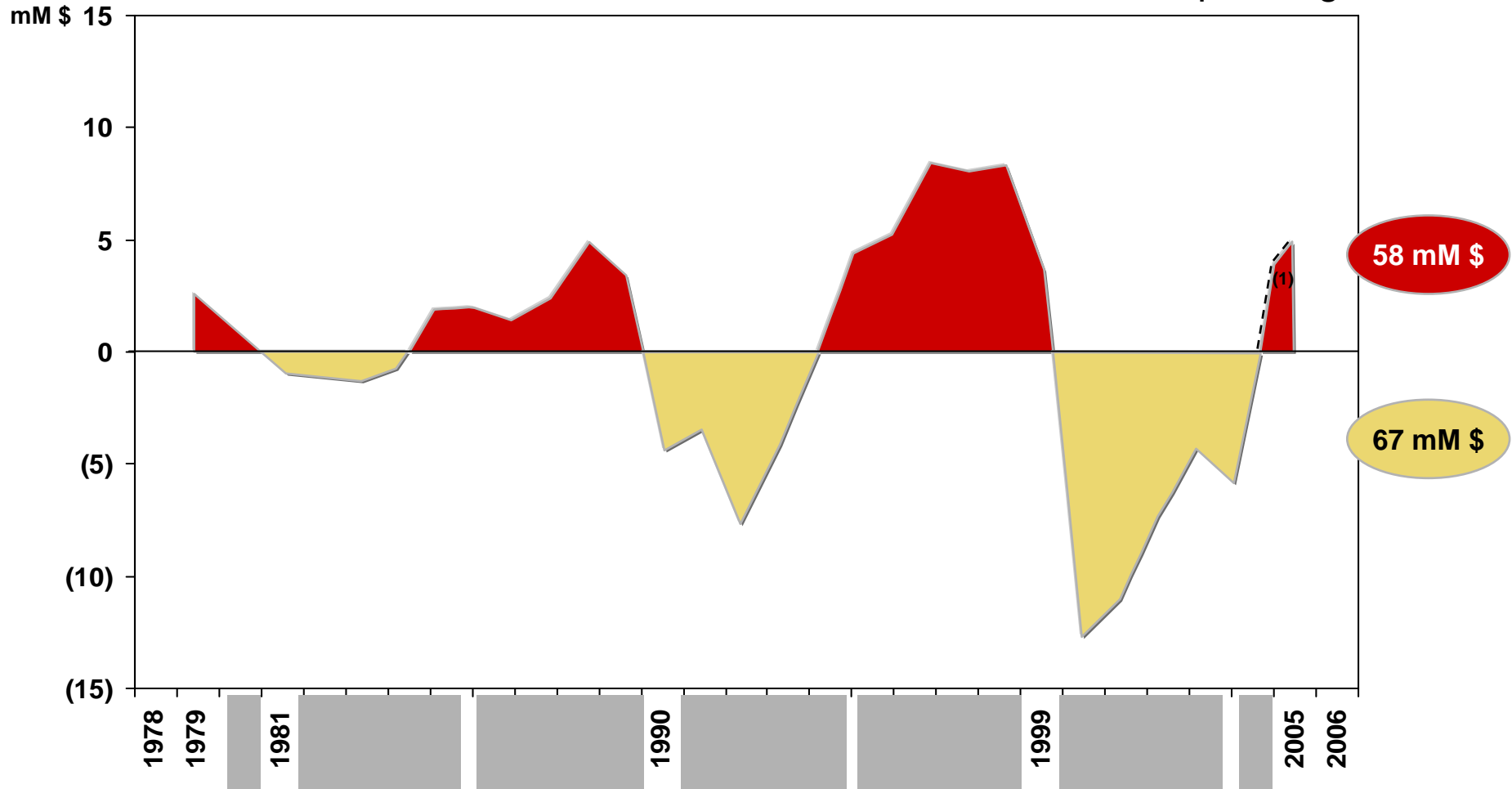
Air Transport Profits Evolution



FUENTE: WATS 2006. (IATA)

Cyclical and low profit sector

Operating Results



**Deregulation processes have removed barriers to entry
but still are high barriers to exit**

Impact of Open Skies for IB

- ✓ Iberia has to **play a major role in** the process of **European consolidation** model.
- ✓ **The Treaty** will open new opportunities in the field of Joint Venture, Alliances and Code-sharing. It **will allow for a deeper relation with strategic partners**: American Airlines through ATI, and a stronger cooperation with British Airways on transatlantic routes.
- ✓ **In the long term the cascade effect on other regions such as Mid-Atlantic and South-Atlantic will benefit Iberia** (strong presence in this market). The liberalization in this area will however force Iberia to cope with new players, and therefore be more efficient in cost.

In the new liberalized markets, no player will be able to survive in the long term, unless, it will be able to improve its efficiency and to reduce the level of basic costs of production

(close to those attained by the leader)



End of Presentation

Thanks for the attention