

ASEAN Research Digest

SPECIAL EDITION

CIL

Research Partner:

Centre for International Law
National University of Singapore



IN THIS ISSUE

VOLUME 3 | ISSUE 1 | AUGUST 2016



ASEAN NEEDS TO ADOPT BASE STANDARDS ACROSS THE REGION AS FIRST STEP TOWARDS HARMONISATION

Lifting-the-Barriers Report 2015: Air Transportation

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OVERVIEW



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SERVICES &
CAPITAL MARKETS



TOURISM

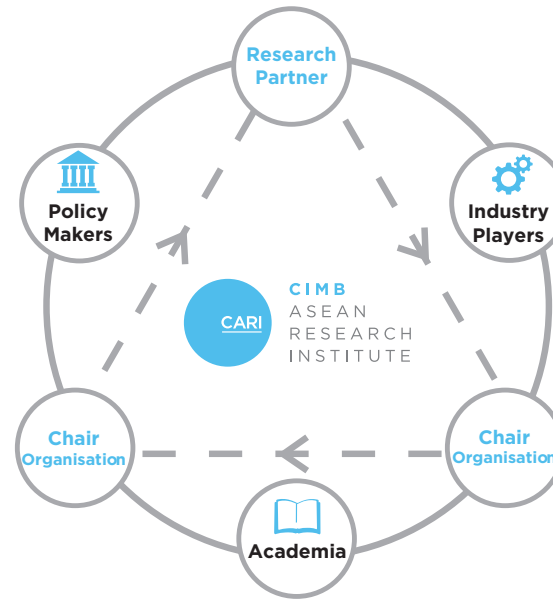
Research objectives:

The CIMB ASEAN Research Institute (CARI) in collaboration with the ASEAN Business Club (ABC) launched the Lifting-The-Barriers Initiative (LTBI) in 2013 as an integrated year long research platform involving core research as well as stakeholder engagement.

The objective was to adopt a vertical approach by means of identifying bottlenecks and barriers hindering free trade of prioritised sectors in the context of the ASEAN Economic Community (AEC).

The LTB Initiative 2015 targets six identified sectors which have pressing relevance to the business landscape in ASEAN and will play a major role in the successful formation of the AEC. The six sectors were Retail, Healthcare, Infrastructure, Air Transportation, Financial Services & Capital Markets and Tourism.

RESEARCH STRUCTURE



Two leading **ASEAN corporations** were selected to champion each sector, providing the direction and experiential insight into their industry. The input from these champions, or chair organisations, were key to understanding the issues faced by industry stakeholders and to develop the recommendations as part of the discourse.

CARI's Research Working Committee and its Strategic Advisors also worked closely with each of the six nominated Research Partners in producing these reports.

The Research Partners were either top management consulting firms or academic institutions who provided the technical knowledge and quantitative analysis required.

METHODOLOGY

The **Lifting-The-Barriers Initiative (LTBI)** is divided into four phases.

PHASE I

PRELIMINARY RESEARCH

Core research and compilation of qualitative and quantitative input from targeted sectors.

PHASE II

ABC FORUM



LTB Roundtables



Plenary Sessions

PHASE III

LTB REPORTS

The final outcome, a set of white papers, for ASEAN policy makers and community to effect real changes in the region.

PHASE IV

FINDINGS SOCIALISATION

The findings from the LTB reports will be prioritised and presented to various stakeholders including policymakers.



ASEAN NEEDS TO ADOPT BASE STANDARDS ACROSS THE REGION AS FIRST STEP TOWARDS HARMONISATION

Title of Study: Lifting the Barriers Report: Air Transportation
By: Centre for International Law (CIL) **Published by:** CARI, May 2015



BACKGROUND

Research objective:

Research objectives: To highlight the critical items that government and industry players must address as ASAM is further developed beyond 2015. In particular, the report focuses on the nascent state of technical/regulatory integration and the need to accelerate its development.

- ASEAN has the ambitious plan of establishing an ASEAN Single Aviation Market (ASAM) among the ten member states.

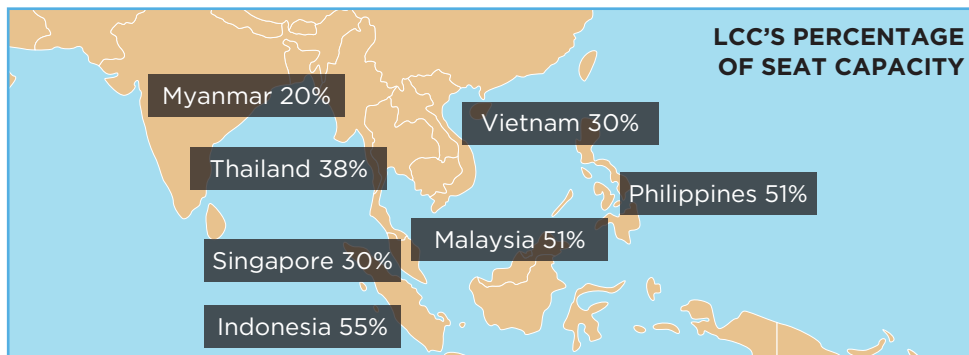
ASAM GOALS:

- ▶ LIBERALISE AIR TRANSPORT SERVICES IN ASEAN
- ▶ CREATE A SINGLE INTEGRATED MARKET FOR THE AIRLINE INDUSTRY

- The initial deadline for ASAM was the end of 2015 but much remains to be done for the economic/market integration of the aviation sector, while the work on technical/regulatory integration is still at its early stages.
- The post-2015 period will therefore tackle both unfinished and new matters.

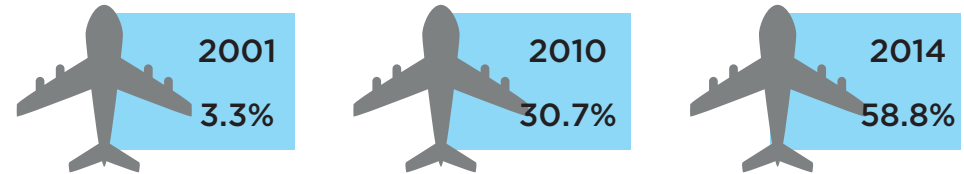
THE BIG PICTURE: THE CHANGING FACE OF ASEAN AVIATION

- The dynamics of ASEAN aviation is evolving rapidly.
- Low-cost carrier (LCC) operations now account for more than half of all airline seat capacity in Indonesia, the Philippines and Malaysia.

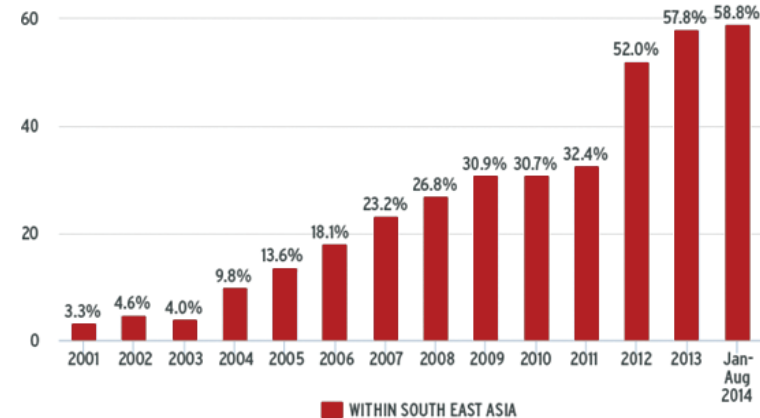


Source: CAPA – Centre for Aviation

- The market share of LCCs on intra-ASEAN routes alone rose to 58.8% of all seats offered in 2014, up significantly from 30.7% in 2010 and only 3.3% in 2001.



Market Share Of LCC On Intra-Asean Routes (% Of Seats, 2001-2014)



- In terms of actual seats offered, LCC capacity in ASEAN, both intra- and extra-ASEAN flights, has increased eight-fold (800%) over the last 10 years, from about 25 million seats in 2004 to nearly 200 million in 2014.
- Over the same period, the full service carriers' capacity grew by only 45%, from about 180 million seats in 2004 to 260 million seats in 2014.

Seat capacity, intra- and extra-ASEAN flights

	2004	2014	Increase
LCC	25m	200m	800%
Full Service	180m	260m	45%



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- The LCC share of capacity is expected to increase even more dramatically in the next decade, particularly for the short-haul intra-ASEAN routes.
- As of early 2015, six of the world's ten busiest international LCC routes are in ASEAN, with Singapore-KL and Singapore-Jakarta being the top two routes.

ASEAN's top 10 LCCs ranked by seat capacity: 19-25 January 2015

Rank		Airlines	Total Seats
1	JT	Lion Air*	1,083,194
2	AK	AirAsia	550,260
3	5J	Cebu Pacific Air	366,997
4	FD	Thai AirAsia	338,040
5	QG	Citilink	230,760
6	DD	Nok Air	218,204
7	QZ	Indonesia AirAsia	198,360
8	VJ	VietJet Air	156,060
9	D7	AirAsia X	122,148
10	TR	Tigerair	120,240

Note: Lion Air capacity data includes flights operated by regional subsidiary Wings Air
Source: CAPA – Centre for Aviation & OAG

- ASEAN aviation now faces **congestion problems** due to the increased air traffic, affecting facilities ranging from terminal and runway capacity to airspace management, as well as the supply of skilled labour.
 - ▶ The aircraft manufacturer, Boeing, projected in 2014 that the Asia-Pacific region alone will require 216,000 new pilots and 224,000 new maintenance personnel for the next 20 years.
 - ▶ The ASEAN LCCs alone have more than 1,000 aircraft on order between them. New joint venture airlines like Malindo, Thai Lion Air, Thai VietJet Air and NokScoot have also ordered aircraft and started operations.
 - ▶ As ASEAN airlines order more planes, the infrastructure and human capital constraints can only get more acute.
- At the same time, the **regulatory landscape remains highly fragmented**, increasing the costs of complying with the relevant rules.
 - ▶ ASEAN member states (AMS) continue to apply their own national rules over airlines and flights in their airspace, resulting in airlines having to adhere to multiple technical standards, certifications and inspections.
 - ▶ Regional co-operation in customs, immigration and quarantine (CIQ) procedures is also lacking, resulting in uneven rules and enforcement.



KEY FINDINGS

- The pressures on infrastructure and human capital have largely been caused by the huge spike in new flights made possible by the increasing economic liberalisation of the region's skies but investments in infrastructure and human capital have not kept up with the aviation boom in ASEAN.
- Neither has there been convergence in national laws and standards to create a more integrated and cost-efficient regulatory regime.
- These two points represent the two main barriers that the ASEAN aviation industry faces today.

MAIN BARRIERS	
1	Lack of infrastructure and human capital
2	Lack of technical and regulatory integration between AMS

TECHNICAL INTEGRATION: TOWARD AN ASEAN REGULATOR?

- ASAM should eventually steer towards creating a common ASEAN regulator to oversee technical matters.
- The benefits of harmonised technical standards and a single regulator include:
 - ▶ increased reliability of regional monitoring and compliance,
 - ▶ reduction of duplication and costs,
 - ▶ enhancement of the overall effectiveness of aviation regulation.
- The challenges to a single regulator include:
 - ▶ ASEAN member states' concerns over loss of sovereignty,
 - ▶ disparity in economic and technical capacities between members.
- However, progress can be achieved in a phased, gradual manner if there is political will among governments and strong industry-government co-operation.

First Steps

- The first step of the process could be to form a body or committee comprising the civil aviation authorities of the member states.
- This would be similar to the Joint Aviation Authorities (JAA) arrangement adopted in the European Union before the JAA evolved to become today's European Aviation Safety Agency (EASA).
- A responsive JAA-type arrangement that directly involves the civil aviation authorities can complement and improve upon the current ASEAN institutional procedure that negotiates through numerous bodies, including the ASEAN Transport Working Group (ATWG), the Senior Transport Officers' Meetings (STOM) and the ASEAN Transport Ministers' Meeting (ATM).



ASEAN NEEDS TO ADOPT BASE STANDARDS ACROSS THE REGION AS FIRST STEP TOWARDS HARMONISATION

- The JAA would not be a regulator and therefore would not enact common standards for the AMS. Instead it would assist the AMS in the harmonisation process to allow for “**mutual recognition of equivalent standards**”, meaning that the member states would continue to enact and apply their own national standards but the JAA body would work to reduce their differences, making them broadly equivalent to allow for mutual recognition.
- This approach raises several critical questions as to how to structure the harmonisation efforts:

Questions regarding harmonisation efforts	
1	<p>Should ASEAN aim for a unified US Federal Aviation Administration (FAA)-style of regulation or a model that is more flexible akin to the EU’s European Aviation Safety Agency (EASA)?</p> <p>A: The EU model might be more relevant since ASEAN comprises several countries with different regulatory systems.</p>
2	<p>Should the initial JAA-style effort begin with a core group of more advanced countries before extending it to other AMS?</p> <p>A: If yes - this pre-supposes a broad EU-style approach of harmonising standards first among a core group and then expecting the other states to adopt the standards. If no - the JAA body would develop equivalent standards at the outset for all member states to adhere to. This would have to have “lowest common denominator” base levels to accommodate varied capacity levels.</p>
3	<p>What minimum base levels should member states peg their national standards to?</p> <p>Here, the authors expect the JAA body to develop procedures for the following related areas:</p> <p>A:</p> <ol style="list-style-type: none"> Setting out the base standards or harmonised regulations against which the national standards would be compared to; The implementation of the national standards by individual member states in a manner that is consistent with the base standards or harmonised regulations; The constant monitoring of this implementation to ensure consistency with the base standards or harmonised regulations; and The provision for the JAA to recommend corrective measures and for the member states to adopt these measures in the event of non-compliance.

Areas of Technical Regulation

- ASEAN also needs to decide the areas of technical regulation that the mutual recognition process can cover. Issues range from straightforward matters like air crew licensing to complex ones like air traffic control and airspace management.
- The authors recommend the JAA body should target the following areas in the initial stages :

Suggested areas of technical regulation	
1	<p>Crew/personnel licensing and training organisations</p> <ul style="list-style-type: none"> ▶ If pilot training schools would comply with base standards, a pilot’s licence issued in one AMS would be recognised in other AMS. ▶ Overall, the demand for aviation professionals could then be managed and met on a regional, rather than national basis.
2	<p>Safety and maintenance programmes</p> <ul style="list-style-type: none"> ▶ If AMS implement base standards on aircraft safety and maintenance, an inspection conducted by one member state authority would be accepted by the other AMS. ▶ A centralised information system could record and disseminate the results of inspections to secure immediacy and transparency in the system.
3	<p>Flight operations</p> <ul style="list-style-type: none"> ▶ Base standards on operations could also be developed, including standards on the rules of the air, procedures on pilots receiving meteorological information, flight crew duty times, communications and navigation equipment, maintenance programmes, flight documents, responsibilities of flight personnel and the security of the aircraft against unlawful acts.
4	<p>Air Traffic Management</p> <ul style="list-style-type: none"> ▶ This is a more complex issue that even the EU states have not yet managed to integrate fully into a single sky with a common regulator. However, initial steps can be taken to harmonise protocols relating to flight information regions (FIRs), better coordination in handing over control from one FIR to another, and emergency back-up air traffic control by neighbouring states when a member state’s system fails.



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Legal Agreements

- Whether the JAA approach is adopted among a core group of states first or region-wide at the outset, a **formalised legal agreement** would be needed to set out the mutual recognition procedure, including technical annexes that lay out the specific base-level standards for each category of regulation.
- Many of the relevant standards have already been laid out by the International Civil Aviation Organization (ICAO) in the form of Standards and Recommended Practices (SARPs) contained in the Annexes to the Chicago Convention on International Civil Aviation, to which all ASEAN member states are party.
- It is the **implementation** of these standards that varies across states.
 - ▶ ICAO does allow states to deviate from the SARPs as long as the ICAO is notified but the reality is that some states do not notify ICAO of their deviations, and disparities become common and entrenched.
 - ▶ A regional effort such as that described above would ensure consistent implementation across member states.

Role of the Industry

- The role of industry is critical to the process of harmonising standards due to the expertise and experience.
- The body that represents most major airlines, the **International Air Transport Association (IATA)**, possesses great expertise on technical and regulatory issues.
 - ▶ IATA recently established a voluntary safety audit programme - the IATA Standard Safety Assessment (ISSA) - for carriers such as LCCs which are typically not IATA members.
- The authors recommend convening an initial high-level industry meeting to bring together all ASEAN airline CEOs and IATA to discuss concrete steps for advancing the region's technical integration agenda.
- If the various ASEAN airlines lead the way and find consensus on what is meaningful and practicable for their own regulation, they can then convince their respective governments to give priority to the issue and provide a huge momentum for the governments to act.
- After all, technical integration benefits all airlines, be they full-service or low-cost carriers.

ECONOMIC INTEGRATION: SETTLING UNFINISHED BUSINESS

- The ASAM process of liberalising market access for ASEAN member states' carriers into each other's market is currently limited to the so-called third, fourth and fifth freedom rights.

The Nine Freedoms of the Air

- | | | |
|---|---|--|
| 1 | The right to fly over a foreign country, without landing. | |
| 2 | The right to land in a foreign country for non-traffic purposes. | |
| 3 | The right to fly from one's own country to another. | |
| 4 | The right to fly from another country to one's own. | |
| 5 | The right to put down and to take on traffic in a foreign country coming from or destined to a third country. | |
| 6 | The right of transporting, via the home country of the carrier, traffic moving between two other countries. | |
| 7 | The right to fly between two foreign countries without any stop in home country. | |
| 8 | The right of transporting traffic between two points in a foreign country on a service | |
| 9 | The right of transporting traffic in a foreign country on a service performed entirely within the foreign country, which originates or terminates outside of foreign country. | |

Source: International Civil Aviation



ASEAN NEEDS TO ADOPT BASE STANDARDS ACROSS THE REGION AS FIRST STEP TOWARDS HARMONISATION

Market Access

Latest developments

- At the time of publication of the LTB report, Indonesia, Laos and the Philippines had yet to ratify several protocols of the ASEAN aviation agreements. The countries have since ratified the agreements, bringing the region a step closer to an actual ASEAN open sky.
 - **Indonesia and Laos** finally ratified the 2010 Multilateral Agreement for the Full Liberalisation of Passenger Air Services (MAFLPAS) in **April 2016**.
 - **The Philippines** was the last to sign protocols 5 and 6 of the 2009 Multilateral Agreement on Air Services (MAAS) in **February 2016**.
 - Indonesia was the last of the AMS to ratify Protocols 1 and 2 of the 2009 Multilateral agreement for the full liberalisation of air freight services (MAFLAFS) in **July 2015**.
 - However, Indonesia, Laos and the Philippines still restrict access to their markets as a whole due to congestion and competition concerns.
 - ▶ Indonesia has limited access to five designated airports:
 - Jakarta Soekarno-Hatta (Jakarta)
 - Medan Kuala Namu (North Sumatra)
 - Surabaya (East Java)
 - Denpasar (Bali)
 - Makassar (South Sulawesi)
 - ▶ Laos limits Thai carriers' access to Vientiane and Luang Prabang
 - ▶ The Philippines limits access to Manila Ninoy Aquino Int'l on the grounds that the airport is not capable of handling a surge in demand.
- Source: [ch-aviation](#), [The Jakarta Post](#) and [Flight Global](#)

- Until recently, ASEAN's limited third, fourth and fifth freedom created a disadvantage for ASEAN carriers in the region's negotiations with third countries.
 - ▶ As shown by the ASEAN-China agreement, Chinese carriers can operate from any point in China to any point in ASEAN while ASEAN carriers can only operate from their own national home points to any point in China.
- With its own treaty now in place, ASEAN should now be in a position to conclude more advantageous aviation agreements with Dialogue Partners, including the European Union, the United States, India, China, Japan, and Russia.
- Even after all ASEAN member states have ratified the agreements of ASAM, their airlines will still have to begin and end their flights in the home state's points.
 - ▶ For example: a Thai carrier will not be able to station planes in Indonesia to connect Jakarta and Manila (i.e. the "seventh freedom").
 - ▶ At best, it can only connect Jakarta and Manila with operations beginning and ending in Bangkok, its home point.
 - ▶ As such, it can operate a **Bangkok - Jakarta - Manila - Jakarta - Bangkok route, which is a fifth freedom operation** that starts and ends in Bangkok, but that enjoys traffic pick-up rights in Jakarta in both directions.



- Such fifth freedom operations are controversial in ASEAN because the Thai carrier in this example would be servicing a "V"-shaped geographical route, as opposed to a linear or straight line route.
 - ▶ The practical effect of a V-shaped route is that most or all the passengers getting on board in Bangkok will likely be bound for Jakarta and a full new load of passengers will be taken on in Jakarta for Manila, effectively turning the operation into a seventh freedom operation.
- Yet, such operations are permitted by the ASEAN agreements which explicitly state that there are no directionality or capacity conditions on fifth freedom flights.
 - ▶ Since they are wholly consistent with the goal of ASAM, all member states should give approval when any ASEAN airline requests authorization for such fifth freedom operations.
- The seventh freedom must thus be addressed explicitly in the post-2015 period and allowed to flourish.
 - ▶ To begin with, all fifth freedom routes, as illustrated above, must be permitted without restriction and regardless of their route path.
 - ▶ In time, pure seventh freedom routes should also be allowed, as it is essential for a single aviation market project like ASAM to include the seventh freedom.
- In conclusion, the ASAM cannot stop at third, fourth and fifth freedom rights only. If it does, the ASAM will remain restricted and become "single" only in name.
- Its important to note that even if all ASEAN member states were to accept all the above agreements, slot constraints at congested airports remain a huge problem which must be resolved separately.



Ownership and Control

- There are still significant barriers to ownership and control of airlines in ASEAN.
- Typically, all ASEAN carriers must be **“substantially owned and effectively controlled”** by their own nationals, meaning that stakes owned by foreigners must be less than 50%.
- To address this, the ASEAN agreements have introduced the **“community carrier”** concept, which allows any member state to designate an airline as long as it is substantially owned and effectively controlled by one or more ASEAN member state.
 - ▶ For example: this means that Cambodia can designate an airline that is 40% owned by Thai interests, 40% by Vietnamese interests and only 20% by Cambodian interests. Since substantial ownership and effective control lie within the family of ASEAN interests, it would not matter that there is minority (or even zero) Cambodian interests.
 - ▶ Of course the designating state will still have to exercise effective **regulatory control** over the community carrier (e.g. safety and security).
- The community carrier concept currently exists only on paper because the ASEAN agreements provide that the community carrier, once designated, **must still obtain the consent of each member state to which it wishes to fly.**
 - ▶ New joint venture airlines in ASEAN have all employed the traditional 51:49 ownership rule, following the model of the more established AirAsia and Jetstar joint ventures.
- In the post-2015 period, **this protectionist barrier must be removed** so that community carriers can be freely established to exercise all rights available to them within ASEAN.
- Even if this matter is resolved, an ASEAN community carrier will only be able to fly within ASEAN. The moment it wishes to fly to another country outside ASEAN it would have to satisfy the substantial ownership and effective control requirements contained in its designating state’s bilateral air services agreements with the external country.
- ASEAN member states need to collectively adopt new air services agreements with third countries that recognise the designation of ASEAN community carriers, such as the ASEAN-China agreement does.

CONCLUSIONS

- There must thus be **greater investments in infrastructure and human capital** to keep up with the additional planes entering the ASEAN market and **technical/regulatory integration must take place** in the subsequent phase of ASAM to complement economic liberalisation.
- In sum, the post-2015 ASAM agenda must pursue the following to ensure a truly single aviation market in ASEAN.

Recommendations

- | Recommendations | |
|-----------------|--|
| 1 | On infrastructural and human capacity <ul style="list-style-type: none"> ▶ Facilitating cost reduction and efficiencies for all airline operations, be these full-service or low-cost. ▶ Committing to overcome infrastructural (airport terminal, runway and slots) constraints as well as the shortage in skilled human capacity. |
| 2 | On technical integration <ul style="list-style-type: none"> ▶ Establishing a Joint Aviation Authorities (JAA)-type body to drive the adoption of base standards. ▶ Adopting a formal legal agreement on mutual recognition for certifications, licenses, permits, approvals and other forms of documentations that are aligned with the relevant base standards. ▶ Establishing procedures to ensure consistent implementation, monitoring and enforcement. ▶ A high-level industry meeting among ASEAN airline CEOs and IATA should be convened to identify what kind of technical integration would benefit all of them. ▶ A wide-ranging “scoping” study should be conducted to compile the various national standards that exist to identify the material disparities. |
| 3 | On economic integration <ul style="list-style-type: none"> ▶ Pursuing market access liberalisation beyond third, fourth and fifth freedom operations to include seventh freedom rights. ▶ Lifting restrictions on “community carriers” so they can operate without having to secure the consent of each destination state. ▶ AMS need to negotiate with third countries as a unified bloc and to ensure that ASEAN community carriers are recognised for operations to those countries. ▶ ASEAN member states need to begin recognising seventh freedom rights for fellow member states’ carriers to operate externally (i.e. extra-ASEAN) to third countries. |

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