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The U.S.-Canada Open Skies Agreement: Three Years Later[1]

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On February 24, 1995, the governments of Canada and the United States signed the "Open Skies" Agreement allowing both Canadian and American air carriers the right to establish direct links between any pair of cities located on either side of the border. This agreement led to an opening of air space that comes within the scope of the general movement towards free trade with our main trading partner. While the agreement itself impacted on both transborder air cargo traffic and air passenger traffic, this study focuses on the latter.

Within three days of the agreement, the U.S. Department of Transportation announced 17 new city-pair routes for U.S. carriers, of which five routes had no previous direct service. By the end of 1995, sixteen American and Canadian airline carriers had introduced new services under the terms of this agreement.[2] By August 1997, a total of 79 new routes were established between Canada and the U.S. (20 of these routes were subsequently discontinued). Canadian carriers established 29 of these new routes, and American carriers established fifty. Within the same time period, Canadian carriers converted a total of 28 routes from charter to scheduled.[3,4]

The U.S.-Canada Open Skies Agreement

1. **Canadian Carriers.** Immediate access by Canadian carriers from any point in Canada to any point in the U.S.
2. **U.S. Carriers.** U.S. carriers subject to a three-year transition period for access to Toronto-Pearson, and a two-year transition period for access to Montreal/Dorval and Vancouver International. All other points in Canada available for immediate access by U.S. carriers
3. **Access to Takeoff and Landing Slots.** Access to Washington National Airport (previously considered a domestic airport by U.S.), 14 new slots in New York LaGuardia, and 10 new slots at Chicago O'Hare. During transition period. Slots can be sold only to other Canadian carriers or traded for other times and will not be subject to the usual use-it-or-lose-it rules.
4. **Pricing.** No longer a requirement to file fares.
5. **Code Sharing.** Permit code sharing between Canadian and U.S. airlines, with some restrictions on inter-country code sharing during transition period.
6. **Dispute Resolution.** Mechanism for high-level meetings if differences arise, with possible use of an international panel if agreement violated.

In This Issue...

Feature Article

Trends

[1] This paper was presented at Statistics Canada's Economic Conference in 1999.
[2] Elliot, Geoffrey, Canada-US Open Skies. Nov. 28, 1995, West Sussex, UK: Canada-United Kingdom Colloquium Into the 21st Century with UK & Canadian Transport.
[3] Source: Aviation Statistics, Statistics Canada.
[4] Charter flights cannot be sold directly by an air carrier and may be subject to any of the following: advance booking and advance purchase of ticket, minimum stay, minimum fare, and operational restrictions. As a consequence, many routes that were previously designated as charter routes were converted to scheduled routes after the signing of the pact.

The agreement has stimulated competition among North American carriers for what remains today as the largest transborder air passenger market in the world.[5,6] It has also provided air travellers with direct, non-stop services between cities that could only be previously travelled via connecting flights, including services between the capital cities of the two countries. Simultaneously, it has improved access by Canadian travellers to the large international hubs of the U.S. Northeast and the Pacific and increased the potential use of Canadian hubs as international gateways to and from North America. While the outcome of the agreement on companies' long-term market shares remains to be seen, short-term changes in market share are already evident.

Traditionally, most trade in air routes has been and continues to be governed by bilateral agreements. As international trade has become increasingly liberal, so have these bilateral air agreements, hence the name "Open Skies". As more and more countries enter into Open Skies agreements, there is an important need to investigate their impact on signatory countries. It is difficult to separate the impact of these agreements from the effects of other changes impacting on the

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5 U.S. Department of Transportation, Monday, January 5, 1998, http://www.dot.gov/briefing.htm. According to International Civil Aviation Organization (ICAO) estimates, the transborder air passenger market between Canada and the United States was the largest of its kind in the world in 1994, leading the group with 10.8 million passengers. The U.S.-Japan and United Kingdom-U.S. markets ranked second with 10.7 million passengers each.

6 Baldwin, Gordon G. and Ed Robinson, 1996. *Measuring the Canada-United States Aviation Passenger Market: How High is UP*? In Transportation Research Forum, 38th Annual Meeting Proceedings, San Antonio, Texas.

Methodology

Data Source

There are a number of data sources for measuring air passenger traffic between Canada and the United States. For purposes of this analysis, data from both Statistics Canada's International Travel Survey (ITS) and from the Aviation Statistics Centre are used. To use the ITS, we use the "border count" method taken from Canada Customs returns, and link it with the ITS. The ITS gathers information on expenditures and other characteristics of travellers, by origin and destination. Canadian customs officers distribute questionnaires to a sample of travellers on arrival (non-residents) or on return (Canadians). Data are collected on, among other things, length of stay and type of transportation.

Aviation Statistics Centre data on the percentage distribution of transborder traffic by city are obtained from the **Air Passenger Origin and Destination, Canada-United States Report**, Table 2, and include traffic volume distribution based on total inbound and outbound passengers. New routes information was obtained from data compiled by of the Aviation Statistics Centre.

Universe

For this analysis, ITS data consider travel between Canada and the United States to include only travel by Canadian and American residents on scheduled or charter flights. Some Canadian and foreign residents pass through the United States to return to or come to Canada. These persons have been excluded since, in many cases, they are travelling on aircraft operated by foreign companies that are not directly affected by the "Open Skies" agreement. These passengers made up about 14% of the transborder air travel market in 1997. During their transborder travel, Canadian and U.S. residents can use other than Canadian and/or U.S. airlines or coupons that may be exchanged for free travel. This travel has been excluded since it does not produce any revenue for U.S. or Canadian carriers. In 1997, these trips represented 6.4% of all travel on commercial airlines between Canada and the United States.

Variables

The ITS consists of quarterly questionnaire interviews which provide a variety of data on passengers, such as the purpose of the trip and expenditures on international transportation by the carrier's country of residence. It is important to note that business travellers, in this paper, are defined as those travellers whose primary purpose for travel is for business reasons. This does not imply that they travel by business class, which has a higher class of fare than economy class or discount economy. The paper uses data on the international component of transportation expenses for return airfares of all Canadian and American travellers who have declared having used air travel to enter Canada. The cost of transportation reported may include fees paid to travel agencies, cruise charges, and various applicable sales taxes and charges. Both Canadian and U.S. carriers incur such costs, so there is no impact on the market share analysis. Lastly, we treat international transportation expenses paid to carriers as a proxy of the revenues received by the company.

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Note of appreciation

Canada owes the success of its statistical system to a long-standing partnership between Statistics Canada, the citizens of Canada, its businesses, governments and other institutions. Accurate and timely statistical information could not be produced without their continued cooperation and goodwill.

airline industry, including changes in economic conditions, weather patterns, new aircraft technologies, and events such as airline strikes. There are still, however, certain types of questions that we can answer in order to begin an examination of the potential impact of these agreements.

With respect to the U.S.-Canada Open Skies agreement as it pertains to air passenger traffic, the following questions need to be examined. What are the terms of the agreement as they relate to air passenger travel? What were the new transborder city-pair routes that came into existence following the signing of the agreement? What were the market shares that U.S. and Canadian companies cornered after the three-year transition period of "Open Skies", and what was the composition of these shares? What is the possible impact of the agreement on various stakeholders?

Bilateral Trade in Air Traffic: The "Open Skies" Agreement

The International Civil Aviation Organization (ICAO) founded in 1947 is civil aviation's version of The General Agreement on Tariffs and Trade (GATT), which was founded in 1944 to co-ordinate international trade policies. ICAO, however, is unlike GATT in many respects. There is no "most favoured nation" trade principle when it comes to negotiating the rights to air routes and no multilateral system for dispute settlement. Access to another country's domestic markets is limited strictly to those consumers on transborder routes.[7] Negotiations, by and large, are bilateral and are influenced by the leverage and power of individual countries. This leverage comes from factors such as market size, population, economic strength, population density, and strategic location.

While international air traffic agreements have been traditionally bilateral in nature, the agreements themselves have typically negotiated route rights. The governments who own these rights designated or subcontract these rights to individual carriers resident in the countries that were party of the agreement. More liberalized bilateral air agreements came to be known as "Open Skies" agreements, in that they opened up access to air routes between the signatory countries. The U.S. led the movement towards "Open Skies" following deregulation of its domestic market in 1978. The increased use of Open Skies agreements can be seen in the increasing number of signatory countries and agreements. In 1997 alone, Canada signed or amended many bilateral air agreements, and the U.S. signed 15 new Open Skies agreements, more than in all previous years combined. The U.S. Secretary of Transportation, Rodney Slater, stated "that it was his goal to reach Open Skies, or be on a definitive path to Open Skies, with virtually all major trading partners by the year 2000".[8] Liberalized air transport blocs, or "continental" Open Skies are in various stages of planning and implementation in North America, Europe, and Asia. In North America, there are the Canada-US "Open Skies"[9] and the Mexico-US Open Skies (1988) agreements. The EU member states have had transborder Open Skies bloc since 1993, and a single European airline market policy was scheduled to be implemented in 1998. [10]

The previous U.S.-Canada bilateral air agreement was negotiated in 1966, with its last revision in 1974. It limited airline access to city-pair routes, and limited designation of a route to one carrier per route on nearly all the routes. There were 28 routes for Canadian carriers and 44 routes for U.S. carriers. In addition, the agreement regulated fares. The 1995 Open Skies agreement was inevitable in light of the domestic deregulation of U.S. (1978) and Canadian (1988) air traffic and the push by the U.S. for more liberalized bilateral air traffic agreements. "Open Skies gave all US and Canadian based airlines the right to compete and operate transborder routes between any Canadian and American city with no limits on capacity or frequency, and allowed airlines to set their own fares with no interference from either government. It was free trade in transborder air transportation."[11]

Some of the advantages that had accrued to American air carriers from the combination of the U.S.-Canada Open Skies agreement and strategic airline alliances are being lost with the recent proliferation of Open Skies agreements. Under old-style bilateral air traffic agreements with their negotiation of route rights and designation of carriers, specific U.S. carriers, for example, lacked access to certain destinations outside North America. By forming alliances with Canadian carriers, these U.S. carriers were able to take advantage of the U.S.-Canada Open Skies agreement and expand the range of travel services to their customers by taking advantage of the networks of their Canadian partners. At the same time, this strategy led to an increase in passengers and revenues shared by both alliance partners. As the U.S. signs more and more Open Skies agreements, the benefits of this aspect of alliances is somewhat diminished as these U.S. carriers begin to offer direct service from their own hubs, instead of through connecting flights at the hubs of their Canadian partners.

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7 *"Another difference is that international trade is about the ability to sell goods and services from one country, in the domestic market of another. This access to markets, taken for granted in international commerce, is given the pejorative name cabotage in the world of civil aviation. Cabotage remains a dirty word among the practitioners of air policy. There is little enthusiasm to open up that Pandora's box except here in the European Union, and then only for EU based airlines." Elliot, Geoffrey, 1997. Liberalization of North American and Global Air Transport.* Institute of Economic Affairs 5th Annual Conference on The Future of Air Transport, pp 3-4.

8 U.S. Department of Transportation, Monday, January 5, 1998, http://www.dot.gov/briefing.htm.

9 While the current Canada-U.S. bilateral agreement was an "Open Skies" agreement for Canada from February 1995. However, it was not an "Open Skies" agreement for the U.S. until the completion of the three-year transition period in February 1998 due to flight and frequency restrictions faced by U.S. carriers in Vancouver, Toronto and Montreal.

10 Oum, Tae, Hoon, 1996. *Some Key Issues in the Increasingly Competitive Airline System*, Journal of Transport Economics and Policy, Vol 30, No 3, 1996, pp 233-236.

11 Elliot, Geoffrey, 1997. *Liberalization of North American and Global Air Transport*. Institute of Economic Affairs 5th Annual Conference on The Future of Air Transport, p 5.

New 1995/1996 Routes

In January 1995, Canadian and U.S. carriers offered a total of 67 transborder routes with direct service between a Canadian and U.S. city (Table 1). By year-end 1996, there was a net addition of 59 new routes, all scheduled services, and 28 charter service routes that had converted to scheduled. Of the total of 79 new services established since the signing of the pact, 20 had been discontinued. All the charter conversions were Canadian air carrier routes and 23 of the 59 new routes were Canadian air carrier routes. Of the 20 new routes discontinued by the end of 1996, six were Canadian carrier routes.[12]

If we examine the top 15 Canadian and U.S. cities in terms of volume of transborder air passenger traffic on an origin-destination basis, we observe those cities whose rank changed significantly after the signing of the agreement (Table 2). Vancouver replaced Montreal as the 2nd ranked city by 1996; both Ottawa and Washington moved up their ranking; and Tampa fell. Of the 59 new transborder routes that were still in place at the end of 1996, Toronto and Vancouver were in 17 of these city-pairs, Montreal was in 10, New York and Ottawa in 6, and Washington in 5. In fact, only 11 cities in these 59 city-pairs were not in the top 30 cities by volume of transborder air passenger traffic (the same cities were in the top 30 in all years between 1992 and 1996). Furthermore, the agreement provided for direct access to Washington National Airport, which was considered a domestic airport prior to the agreement. These new transborder routes played a significant role in the changes in rank noted above.

[12] Source: Aviation Statistics, Aug. 29, 1997 and Pustay, Michael W., 1997. The Long Journey To Free Trade in Transborder Airline Services. Paper presented at the Annual Meetings of the International Studies Association, Toronto.

Table 1
Canadian City of new Transborder City-Pairs, 1996

Canadian City	Old routes	Net new routes (B+C-D)	Charter[1] conversion	New routes (B+C)	Canadian carrier (B)	U.S. carrier (C)	Discontinued new routes (D)
Total	**67**	**59**	**28**	**79**	**29**	**50**	**20**
Toronto	24	17	11	18	10	8	1
Montreal	15	12	2	17	6	11	5
Vancouver	10	15	5	21	4	17	6
Calgary	9	7	4	7	5	2	
Ottawa	3	5	1	5	2	3	
Winnipeg	2	2	2	3		1	1
Edmonton	2	1	1				
Halifax	1	1	2	3		3	2
Regina	1	1		1		1	
Fredericton		-		1			1
Quebec		1		2	1	1	1
Saskatoon		1		1		1	
Moncton		-		2	1	1	2
Saint John		-		1		1	1

[1] *Pre-agreement Charter routes converted to scheduled routes.*
Source: Aviation Statistics Centre, Statistics Canada, special tabulations.

Table 2
Top 15 Cities by Transborder Air Passenger Volume

City	Rank 1992	Rank 1993	Rank 1994	Rank 1995	Rank 1996	Percent of Traffic 1992	Percent of Traffic 1993	Percent of Traffic 1994	Percent of Traffic 1995	Percent of Traffic 1996
Toronto	1	1	1	1	1	21.2	20.9	21.2	20.6	19.6
Vancouver	4	4	4	3	2	6.3	6.7	6.5	7.5	8.6
Montreal	2	2	2	2	3	9.2	9.3	9.3	9.3	8.3
New York	3	3	3	4	4	7.3	7.1	7.3	7.0	6.8
Los Angeles	5	5	5	5	5	5.0	4.7	4.5	4.7	4.5
Calgary	6	6	6	6	6	3.8	3.8	4.0	3.9	4.0
San Francisco	7	8	8	8	7	3.2	3.0	3.1	3.1	3.2
Chicago	8	7	7	7	8	3.0	3.3	3.4	3.3	3.0
Ottawa	13	13	13	11	9	1.7	1.7	1.8	2.0	2.3
Miami	9	9	9	10	10	3.0	2.7	2.6	2.3	2.1
Boston	10	10	10	9	11	2.8	2.5	2.5	2.5	1.9
Washington	15	15	16	13	12	1.3	1.3	1.3	1.6	1.7
Edmonton	12	12	11	12	13	2.1	2.1	1.9	1.8	1.7
Orlando	20	17	20	18	14	1.0	1.1	1.0	1.1	1.5
Tampa	11	11	12	14	15	2.4	2.2	1.9	1.6	1.5
Total						**73.3**	**72.4**	**72.3**	**72.3**	**70.7**

Sources: Air Passenger Origin and Destination, Canada-United States Report and, Aviation Statistics Centre, Statistics Canada, Cat. No. 51-205-XPB.

Travellers

Residence of North American travellers arriving in Canada

In 1997, Canadians made up 57% of the Canada-U.S. air passenger market and Americans 43% (Table 3). Canadians make up a larger portion of the air passenger market in both the business and the non-business categories, though the difference is largest in the latter group. The figures are not all that surprising considering that Canadians vacation more in the U.S. than the converse, particularly Canadians vacationing in U.S. sunspot and casino destinations.

Despite the dominance of Canadians in the air passenger market, the share of American travellers increased significantly over the 1993 to 1998 period driven largely by non-business travellers. While "Open Skies" undoubtedly had an impact on this increase, it is quite likely that the increasing share of American non-business travellers was influenced by the strong U.S. economy and the increased purchasing power of the U.S. dollar in Canada.[13]

Most dramatic, however, was the increase in air passenger travel following the signing of "Open Skies". Both in terms of volume (over 980,000 additional passengers arriving from the U.S. into Canada) and in terms of growth (over 15%), the single largest annual increase occurred in the 1996 calendar year.

While there were more Canadian air passengers overall, it is in the category of non-business travel that Canadians largely dominated the market. In fact, in 1997 more than three out of five transborder travellers travelling for reasons other than business were Canadians. There was a relatively steady growth in Canadian transborder business travel from 1993 to 1997, as compared to the decline in non-business travel prior to "Open Skies" and its increase following the pact.

Among American transborder air travellers, until 1997 the class of non-business travellers grew more rapidly than the class of business travellers. Apart from 1996, American business travellers comprised a larger volume of air passenger traffic to Canada than American non-business travellers did. The growth in U.S. non-business travellers was highest in the year following "Open Skies", while the business traveller class grew the most in the two years following the signing of the pact.

Air Carriers

Revenue Shares

In 1997, Canadian and U.S. air carriers flying transborder routes shared revenues of over $4.7 billion. Total revenues increased substantially, from $3.1 billion to over $4.7 billion in the four year period, for a growth of over 50%. Between 1993 and 1997, the market share of Canadian carriers grew by about 5 percentage points of the total

[13] The Canadian dollar experienced a decline from $0.78 U.S. in 1993, to $0.73 from 1994-1996, to less than $0.65 in the third quarter of 1998.

Table 3

Distribution of air Passagers by Main Trip Purpose and Nationality

	Year					1st and 2nd Quarters			
	1993	1994	1995	1996	1997	1995	1996	1997	1998
Air Passagers in '000s									
Canadians	3,714	3,556	3,662	4,279	4,347	1,989	2,441	2,454	2,330
Americans	2,358	2,467	2,777	3,141	3,275	1,184	1,399	1,423	1,559
Total	**6,072**	**6,023**	**6,439**	**7,420**	**7,622**	**3,173**	**3,840**	**3,877**	**3,889**
Air Passagers in %									
Canadians	61.2	59.0	56.9	57.7	57.0	62.8	63.6	63.3	59.9
Americans	38.8	41.0	43.1	42.3	43.0	37.2	36.4	36.7	40.1
Percent	**100.0**	**100.0**	**100.0**	**100.0**	**100.0**	**100.0**	**100.0**	**100.0**	**100.0**
Share of Air Passenger by main trip purpose									
	Percent					Percent			
Business Travel									
Canadians	23.8	25.4	24.9	23.6	22.5	26.4	24.0	22.5	24.9
Americans	22.1	22.6	23.1	21.5	22.7	23.5	20.4	22.3	21.8
Total	**45.9**	**48.0**	**48.0**	**45.1**	**45.2**	**49.9**	**44.4**	**44.8**	**46.7**
Non-Bus. Travel									
Canadians	37.4	33.7	32.0	34.1	34.5	36.3	39.5	40.8	35.0
Americans	16.6	18.3	20.0	20.8	20.3	13.8	16.1	14.4	18.3
Total	**54.0**	**52.0**	**52.0**	**54.9**	**54.8**	**50.1**	**55.6**	**55.2**	**53.3**

Source: International Travel Survey.

market, from 39.3% to 44.3% (Table 4). The growth in transborder air passenger travel meant that by year-end 1997, Canadian carriers earned more in revenues than their U.S. counterparts did in 1993, although U.S. carriers continued to earn more on transborder routes than their Canadian counterparts.

The growth in the Canadian market share is an indication that under "Open Skies", Canadian carriers are implementing strategies that are gaining them an increasing share of the growing pie of transborder revenues. Another noticeable variation in the Canadian and U.S. market groups is in terms of distribution of travel by main purpose. Table 5, which is discussed in a later sub-section, shows that Canadian carriers expanded revenues from air passengers travelling mainly for business purposes.

If we examine revenue shares by main purpose of travel (business and non-business), we see that U.S. carriers have obtained the largest revenue share – fare revenues from air passengers travelling mainly for business purposes. Canadian carrier revenues from business travellers remained the lowest share of revenues until 1997 (Figure 1). This is particularly noteworthy given that Canadian business travellers outnumber American business travellers. It can be explained by the fact that U.S. carriers have been able to attract a significant portion of Canadian business travellers, although Canadian carriers have improved their performance with respect to this component of the domestic market. In the 1993-1997 period, U.S. business fare revenues grew from $1.2 billion to $1.6 billion, while Canadian business fares grew from $0.5 billion to $1.1 billion, the largest growth in this decomposition. United States non-business fare revenues grew from $0.7 billion to $1 billion, as did Canadian non-business fares in the same period.

Growth in the revenue share from non-business fares was roughly comparable from both Americans and Canadians. However, business fares grew significantly during this period, with Canadian business fares growing the most rapidly following Open Skies. This may have been, in part, due to the strategy of at least one Canadian carrier in catering to the more lucrative business market by establishing more short-haul direct routes, catering for savings in time rather than money (e.g. Toronto-Washington). The new 50-seat Regional Jet served many of these routes. The smaller size of the 50-seat jet guaranteed a lower financial break-even capacity, which was reduced further by serving the more profitable business travellers. Despite the much larger share of revenue from American business travellers, the growth in these revenues was quite similar to the growth in revenues from Canadian business travellers.

Table 4

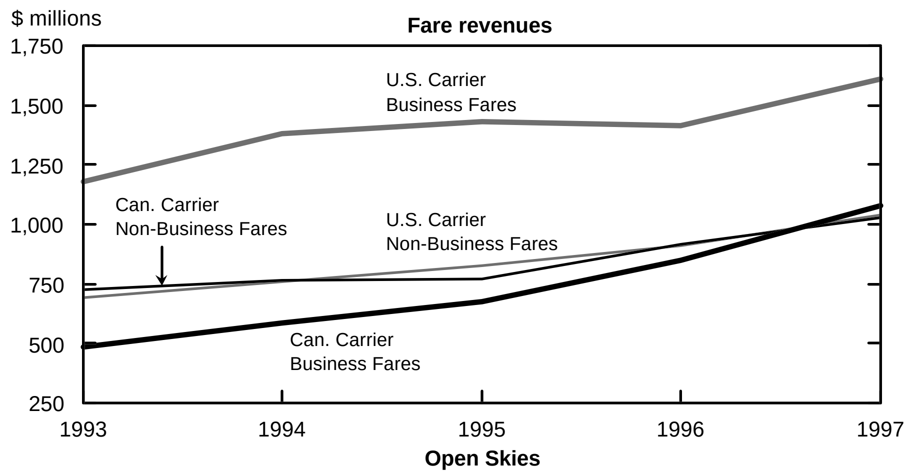
Revenue Shares of Air Carriers

	Canadian Carriers	U.S. Carriers	Total Carriers
1993			
Revenue ($millions)	1,210	1,866	3,076
Share (%)	**39.3**	**60.7**	**100.0**
1994			
Revenue ($millions)	1,349	2,140	3,489
Share (%)	**38.7**	**61.3**	**100.0**
1995			
Revenue ($millions)	1,449	2,261	3,710
Share (%)	**39.1**	**60.9**	**100.0**
1996			
Revenue ($millions)	1,764	2,325	4,089
Share (%)	**43.2**	**56.8**	**100.0**
1997			
Revenue ($millions)	2,106	2,647	4,754
Share (%)	**44.3**	**55.7**	**100.0**

Source: International Travel Survey.

Figure 1

Air Carrier Fare Revenues, in Million of Dollars, by Nationality of Carrier and Main Trip Purpose of Traveller



Passenger Shares

The impact of the Open Skies agreement on transborder air traffic was almost immediate. The growth in Canadian air carrier traffic was larger than the growth in U.S. air carrier traffic, thereby increasing the market share of passengers taking Canadian carriers (Figure 2). While the proportion of travellers that chose Canadian carriers was growing, so was the pie of transborder air travellers – ensuring that carriers of both countries saw an increase in their air passenger travellers. In 1993 and 1994, 5.6 million Canadians and Americans entered Canada by air. After Open Skies, this figure grew to 6.1 million in 1995, 7 million in 1996, and 7.1 million in 1997. Despite the dominance of U.S. carriers in passenger market share, their share declined after the signing of the agreement. In 1993, close to 900,000 more transborder travellers chose a U.S. carrier over a Canadian carrier. By 1997, this difference dropped to about 250,000 travellers.

On a quarterly basis, U.S. carriers saw a year-over-year increase in their air passenger traffic for most quarters following the signing of the pact. With the exception of the first quarter of 1998, Canadian carriers experienced an even more dramatic increase in their air passenger traffic with an increase of over 40% from the second quarter of 1995 to the second quarter of 1996, (Figure 3). The one-quarter decline that occurred in the first quarter of 1998 may have been the consequence of the Ice Storm of January 1998, which affected eastern Ontario and western Quebec reducing air traffic flows to and from Montreal and Ottawa.

Figure 2

Transborder Passenger Traffic Entering Canada

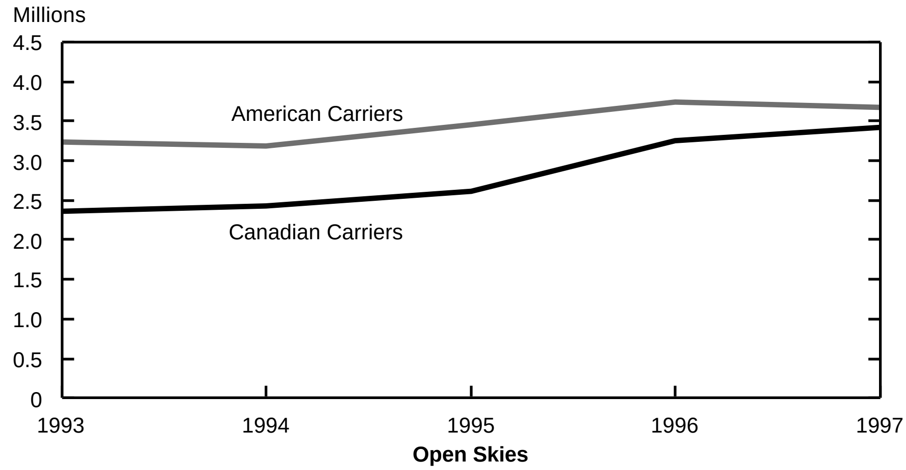
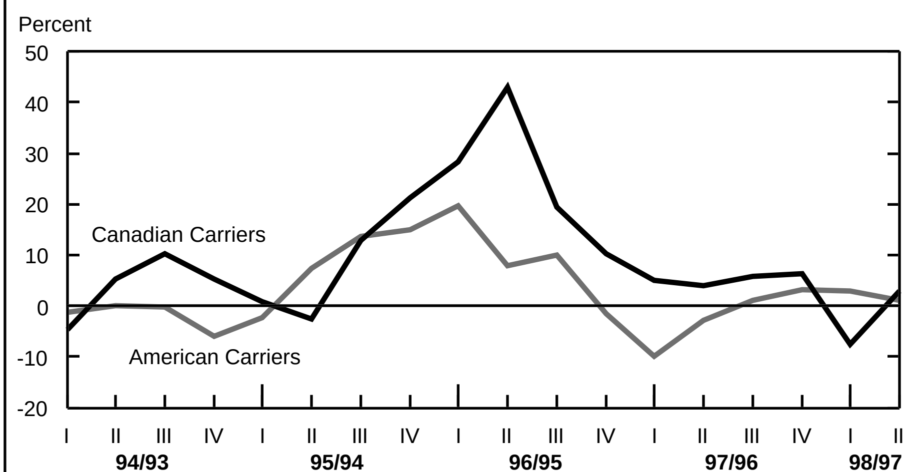


Figure 3

Percentage Growth in Air Passenger Traffic by Nationality of Transborder Carriers



Distribution of Carrier Revenue Shares by Main Trip Purpose

The composition of revenue by main trip purpose remained relatively unchanged in the 1993 to 1997 period (Table 5). However, when we examine this composition from the nationality of the carriers, a different picture emerges. Revenue from non-business travellers remained relatively unchanged for both Canadian and U.S. carriers. However, Canadian carriers increased their share of revenues from business travellers, while U.S. carriers registered the opposite.[14]

The Trend in Average Revenues/ Average Fares

Average revenues per traveller fell for both Canadian and U.S. carriers in the year following the signing of the Open Skies agreement. This fall in revenue, however, was reversed by the second quarter of 1996 after which average business fares/revenues grew quite significantly, particularly for U.S.

[14] Most carriers applied at least one of the following two strategies. Some carriers established transborder spokes from their domestic hubs to take advantage of the potential demand for passengers seeking the convenience of more direct service between transborder city-pairs. Others set up services between transborder hubs to take advantage of the domestic and overseas networks of their airline alliance partners. The former strategy was used by at least one domestic carrier, which set up several new routes to cater to transborder business travellers attracted by the new non-stop transborder flights. Recent technological changes in aircraft engineering helped establish this strategy, both here and in Europe, where new 50 seat jets could serve short-haul flights with a smaller financial break-even capacity (capacity measured in seats).

carriers. Average revenues for both classes of travellers increased from 1996 onwards (Figure 4); though non-business fares for Canadian carriers stayed relatively stable exhibiting mainly seasonal variations. This may have been a result of several factors, including the general health of both the Canadian and U.S. economies. Following the signing of Open Skies, U.S. airlines were generally regarded as price setters in transborder fares, and with a booming U.S. economy, U.S. airfares, in general, rose from 1996 onwards, driving up fares in both countries. The declining Canadian dollar may have increased this trend when airfares were converted into current Canadian dollars, though this was unlikely to have happened till after 1996 (the value of the Canadian dollar remained at $0.73 U.S. from 1994 till 1996).

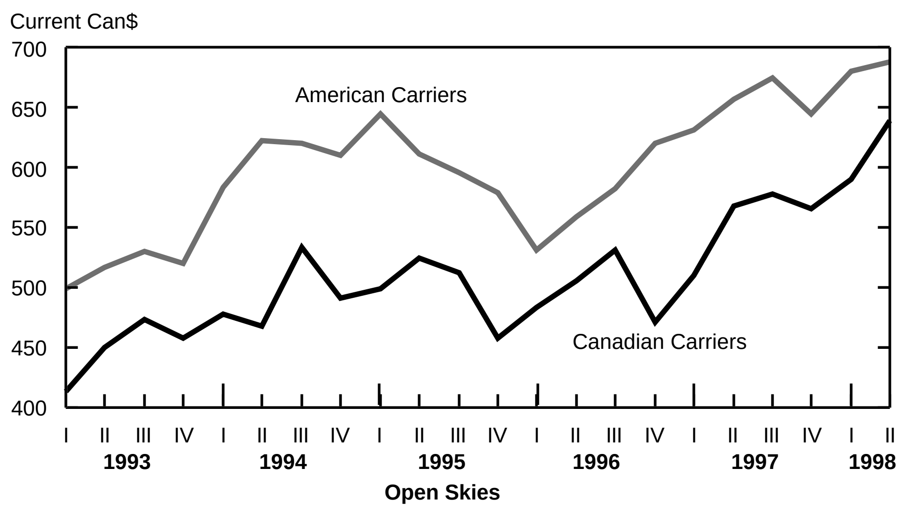
The International Travel Survey does not allow us to accurately asses changes in origin-destination travel patterns. As a consequence, the extent to which changing average airfares are due to changes in travel patterns as opposed to changes in airfares cannot be assessed. The impact of changes in new aircraft technologies may have also played a role in the changes in average airfares. The introduction of new 50 seat jets made many direct routes profitable at lower break-even capacities than larger jets were capable of sustaining. These jets, such as the Canadair Regional Jet, allowed air carriers to provide more direct non-stop services between transborder cities to business travellers, many of whom may have travelled at the higher business-class fares. The extent to which this phenomenon contributed to increasing average business fares is unknown. Thus, while we can make statements about movements in average airfares following the signing of Open Skies, evaluating these movements in terms of their benefits to travellers could be misleading.

Table 5
Distribution of Air Carrier Revenue Shares

	1993	1994	1995	1996	1997
	Percentage				
Canadian Carriers					
Business	16	17	18	21	22
Non-Business	24	22	21	22	22
Total	**40**	**39**	**39**	**43**	**44**
U.S. Carriers					
Business	38	39	39	35	34
Non-Business	22	22	22	22	22
Total	**60**	**61**	**61**	**57**	**56**
Canadian et U.S Carriers					
Business	54	56	57	56	56
Non-Business	46	44	43	44	44
Total	**100**	**100**	**100**	**100**	**100**

Source: International Travel Survey.

Figure 4
Average Business Fares Increase



Benefits of the Pact

Travellers…

Travellers clearly benefited from the new routes introduced by Open Skies. While there were some new routes that were discontinued, there was still a significant net gain (59 new routes by the end of 1996), including some transborder city-pairs which saw direct air passenger service for the first time (e.g. Toronto-Washington, Ottawa-Washington). These new direct service flights provided significant convenience to travellers, particularly those travellers whose needs were previously met only by making connecting flights to their destination cities. For example, the new Ottawa-Washington non-stop service is now an 80-minute flight, as opposed to the previous three-hour indirect flight via a U.S. hub.[15] In addition to the convenience of new direct services, greater access by Canadian passengers to the hubs of the American Northeast, the South and the Pacific allowed them to take advantage of a greater range of outbound international flights.

15 Elliot, Geoffrey, 1995. Canada-US Open Skies. West Sussex, UK: Canada-United Kingdom Colloquium Into the 21st Century with UK & Canadian Transport.

However, the net benefit to Canadian travellers of changes in terms of average fare movements remains unclear. Many factors may have effected changes in average fares. These include changes in the market composition of air travellers by main purpose of trip (business versus non-business), changes in the market composition of class of travel by business travellers (business class, economy, discount economy), changes in the exchange rate, and changes in economic conditions. A more accurate assessment would require examining changes on the ranges of fares (business, economy, and discount) for each city-pair.

Carriers…

Air carriers benefited from Open Skies in their ability to compete for the lucrative U.S.-Canada transborder traffic – a traffic volume that has ensured its status as the highest transborder air passenger traffic in the world. The market of transborder travellers has itself grown following the signing of Open Skies. The benefits that accrued to Canadian carriers are evident in their increased share of this growing pie. The total share of travellers choosing Canadian carriers has increased after the signing of the agreement. More importantly to carriers, their share of revenues increased from 40% in 1993 to 44% in 1997, largely due to their ability to attract more passengers travelling for business reasons. In the same four-year period, the proportion of all transborder travellers choosing Canadian carriers for their business travels rose by 8 percentage points, from 16% to 23%.

Other Impacts…

There are other impacts of the agreement not analyzed in this paper. The agreements' provision for code sharing also provided significant advantages for both passengers and carriers. Each airline is assigned a unique two-letter code, and traditionally, an airline ticket lists this code and the flight number associated with the segment of a flight provided by a particular carrier. Code sharing allows airlines to use each other's codes, a practice that has increased after Open Skies with the growth of airline alliances. In addition to the ability to provide market presence without the substantial cost-outlay of ground staff, sales agents and the like, code sharing increases the convenience of computerized booking systems. It also "…allows airlines to connect traffic from foreign cities, which they do not fly to, with their flights."[16] Code sharing has, however, introduced its own problems. Because one airline lists another airline flight as its own, that flight is listed twice in computer reservation systems (once under each airline code) and more times if connections are involved. This makes it difficult to know how to appropriately attribute market shares on code shared flights – particularly when passenger's tickets are used to obtain information on the carrier.

Conclusion

The Canada-U.S. Open Skies agreement was part of the trend to liberalized air travel, which began with the deregulation of the domestic U.S. air travel industry in 1978. This agreement, like most Open Skies agreements, provided for free trade in transborder air passenger and air cargo travel. While it did not introduce foreign competition in the domestic air travel market, it still provided some clear benefits for both Canadian passengers and Canadian carriers.

After the end of the transition period of the "Open Skies" agreement between Canada and the United States, this analysis shows us that air traffic has increased in both countries, thus consolidating the Canada-U.S. transborder market as the largest in the world. Although Canadian companies seemed to have gained ground in the sales and passenger markets, it is still too soon to know if they maintain or increase their market shares in face of stiff competition from the big U.S. carriers. Only after more time has passed and long-term market shares and fares have been established will it be known how well Canadian companies and travellers are doing under the agreement. [17]

For a complete listing of the references in this article contact Monique Beyrouti, Editor-in-Chief (613-951-1673; fax: 613-951-2909; monique.beyrouti@statcan.ca)

[16] Park, K. Namgyoo and Dong-Sung Cho, 1997. The Effect of Strategic Alliance on Performance, Journal of Air Transport Management. P 156.

[17] Complicating this analysis is another issue that requires more detailed investigation. The increased use of code sharing on transborder routes has had serious implications for analysis of market shares. The revenue allocation formulas for code shared flights vary greatly depending on the agreements signed by carriers who are involved in the code shared flights. The analysis in this paper assumes that in code shared flights, all the revenue goes to the operating carrier and none to the selling carrier. If the true allocation of revenue between Canadian and U.S. carriers on code-shared flights differs significantly from this allocation on transborder flights not using code sharing, market shares of passengers and revenues by nationality of carrier will not be accurate.

TRENDS

Characteristics of International Travellers
1998

Tourism businesses enjoyed a record-breaking year in 1998. Buoyed by strong American tourism, almost 19 million international tourists came to Canada in 1998, the highest annual level in the 26 years that travel data have been collected.

In total, 18.8 million international tourists made overnight trips to Canada during 1998, up 6.8% from 1997. The majority, about 14.9 million, came from the United States, up 11.1%. This strong increase in American overnight travel offset a 7.1% decline in overseas visits to Canada, which fell from 4.2 million in 1997 to 3.9 million in 1998.

Overnight American travel to Canada in 1998 represented the highest level recorded, breaking the previous 13-year record set in 1986 - the year of the World Exposition in Vancouver. Furthermore, the number of Americans visiting Canada surpassed the number of Canadians travelling to the United States by 1.5 million travellers, the first time this has occurred since 1988. A booming United States economy, strong American consumer confidence and a cheaper Canadian dollar were key factors in the growth in American tourism.

Tourism from the United States increased in almost all regions of Canada during the summer of 1998. Ontario recorded the largest increase in American visitors (up 12.4%), followed closely by British Columbia (up 11.9%). American travellers made fewer overnight visits to the Yukon and Northwest Territories (down 5.4%) during 1998.

American overnight visitors injected $6.7 billion into the Canadian economy in 1998, up 25.2% over the previous year. They spent about $450 per trip, up 12.5% from a year ago. Americans spent $925 million or 38.7% more on other expenses, for example shopping and souvenirs, the highest increase of all the spending categories. The low value of the Canadian dollar no doubt encouraged many visitors to shop in Canada. The majority of their tourism spending ($2.7 billion) went towards accommodation, up 29.8% compared with 1997.

American travellers continued to take more flights to Canada (up 12.4%), maintaining the trend that began with the implementation of the Open Skies agreement. Air travel has climbed steadily from 2.4 million trips in 1994 to approximately 3.6 million in 1998. The vast majority of Americans still drove to their Canadian destinations (9.4 million), an 11.9% increase over 1997.

In terms of overseas travel, the 3.9 million visitors from countries other than the United States spent $4.5 billion in 1998, 1.2% less than in 1997. The reduction in Asian travel to Canada deepened in 1998 with 19.0% fewer visitors. This followed an 8.9% decline from the previous year. Overnight visits from Europe declined marginally (down 2.2%) despite the appreciation of many European currencies against the Canadian dollar. Travel from Central and other North America jumped 14.3% in 1998, largely due to influxes (16.7%) of Mexican tourists to Canada.

Much of the decline in overseas visitation was due to a 14.1% drop in the number of visitors travelling to Canada via the United States. Direct overseas arrivals, which now represent 63% of all overseas traffic, decreased just 2.4% in comparison. These visitors are a significant market for Canada, as they tend to stay longer and spend more per trip than those arriving from the United States.

Provincially, the strongest gains in overnight visits from countries other than the United States in 1998 occurred in Alberta (up 19.1%) and British Columbia (up 16.2%). However, 1998 levels still remained well below those recorded in 1996 for these two provinces. Large in fluxes in travellers from the United Kingdom, Germany and France were largely responsible for the growth in overseas visitors.

Meanwhile, overnight trips by Canadians to the United States declined 11.2% to 13.4 million in 1998, the lowest annual level since 1987. On the other hand, Canadians made a record 4.2 million over seas trips (up 5.9%), preferring traditional European destinations such as the United Kingdom, France and Germany.

TRENDS

International Travel Account

First quarter 1999 (preliminary)

The international travel account deficit fell to $182 million during the first quarter of 1999, its lowest level in more than a decade, on the heels of record spending by American travellers in Canada.

Between January and March, Canadians spent $182 million more outside the country than foreigners spent here, down from $411 million in the fourth quarter of 1998. The first quarter deficit was the lowest since early 1988 when it reached $364 million.

Canadians spent nearly $4.1 billion outside the country during the first quarter of 1999, while foreigners spent $3.9 billion in Canada.

Travel deficit with the United States lowest in more than a decade

The increase in spending by United States residents travelling to Canada was the main contributor to the decline in Canada's overall deficit with the other countries of the world. American travellers spent a record $2.4 billion in Canada during the first three months of 1999, up 4.6% from the previous quarter. At the same time, Canadian spending south of the border declined 2.3% to just under $2.5 billion.

The result was a deficit with the United States of only about $11 million in the first quarter of 1999, down from $177 million in the previous quarter and the lowest level in the last 10 years. The booming U.S. economy, strong American consumer confidence and the cheaper Canadian dollar were likely major factors in the record American spending on this side of the border.

During March alone, Americans made a record 1.4 million overnight trips to Canada, exceeding the number of Canadians travelling to the United States. The number of overnight trips by Americans visiting Canada has been exceeding the number of Canadians travelling to the United States since February 1998.

Note to readers

Unless otherwise stated, quarterly data in this release are seasonally adjusted. Amounts are in Canadian dollars and are not adjusted for inflation.

Receipts represent spending by foreigners travelling in Canada, including education-related spending and medical-related spending. Payments represent spending by Canadians travelling abroad, including education-related spending and medical-related spending.

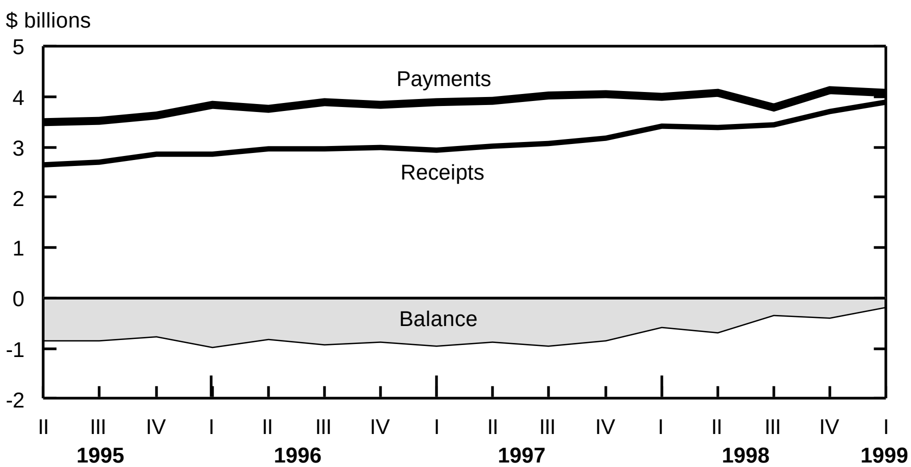
Overseas countries are countries other than the United States.

Record spending by travellers between Canada and overseas countries

Despite the 2.3% decrease in the number of overnight trips to overseas countries, Canadians spent a record $1.6 billion in overseas countries, up 1.2% from the previous record set in the fourth quarter of 1998. Meanwhile, spending by residents of overseas countries in Canada rose 6.0% to a record $1.5 billion. The number of overnight trips by overseas residents increased 4.6% from the previous quarter to 1.1 million.

Consequently, Canadians spent $171 million more in overseas countries during the first quarter of 1999 than overseas residents spent here, the ninth consecutive quarterly deficit with overseas countries. This level was a sharp decline from $234 million in the previous quarter.

Canada's international travel account deficit down to lowest level in over 10 years



TRENDS

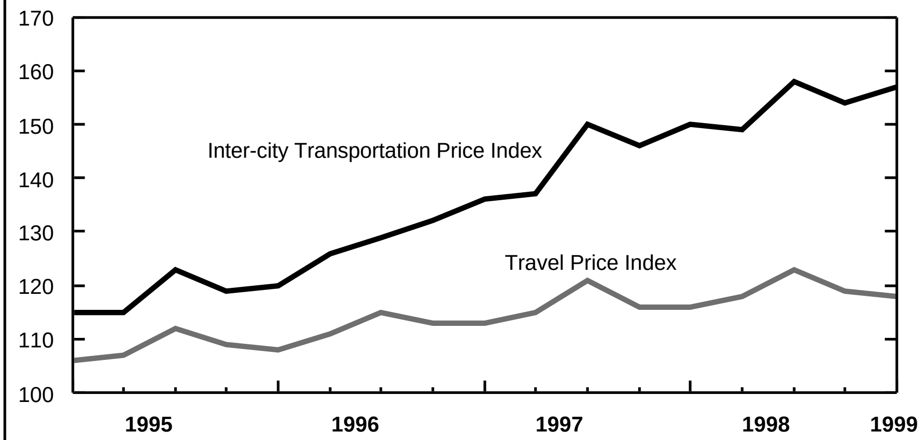
Travel Price Index
First quarter 1999

The TPI rises 2.3% from the same period last year

The Travel Price Index rose 2.3% over the same period last year. Although prices of most TPI components went up, inter-city transportation contributed most to the increase. In the first quarter of 1999, accommodation costs climbed 4.5% and automotive vehicle rental costs rose 3.2%. Automotive vehicle operating costs fell 1.6% during the same period.

In comparison, the CPI advanced 0.8% over the same quarter last year.

Inter-city Transportation Price Index and the Travel Price Index, by Quarter



Source: Tourism Statistics Program.

The Travel Price Index (TPI) and its Components
(not seasonally adjusted, 1992 = 100)

Components of the TPI	First Quarter 1999	% Change: Fourth Quarter 1998	% Change: First Quarter 1998
Inter-city transportation	157.1	1.8	4.9
Local and commuter transportation	122.7	0.3	1.4
Rental of automotive vehicles	117.0	-1.8	3.2
Operation of automotive vehicles	111.4	-1.0	-1.6
Traveller accommodation	111.4	-6.6	4.5
Food purchased from stores	110.7	1.7	1.7
Food purchased from restaurants	111.4	0.5	1.6
Served alcoholic beverages	107.6	0.5	0.6
Alcoholic beverages purchased from stores	112.2	0.6	0.6
Spectator entertainment	125.8	0.5	4.1
Clothing	105.1	0.9	0.5
Footwear	105.1	-1.4	2.5
Clothing accessories and jewellery	97.6	-0.7	0.2
Clothing material, notions and services	111.6	0.5	1.9
Medicinal and pharmaceutical products	107.1	0.2	2.4
Personal care	108.1	0.4	1.5
Photographic equipment	95.8	-0.6	-4.9
Photographic services and supplies	100.3	0.4	3.5
Operation of recreational vehicules	107.3	-0.7	-1.1
Audio discs and tapes	107.6	2.1	1.3
Use of recreational facilities and services	118.6	0.7	2.3
Reading material and other printed matter	122.0	1.1	0.7
Tobacco products and smokers' supplies	72.3	0.1	3.3
Travel Price Index (TPI)	**118.2**	**-0.6**	**2.3**
Consumer Price Index (CPI)	**109.2**	**0.3**	**0.8**

Sources: The Consumer Price Index, Cat. No. 62-001-XPB; and the Tourism Statistics Program.

Note to readers

The Travel Price Index (TPI) is an aggregate index of the goods and services used by travellers in Canada. Price movements are derived from the detailed Consumer Price Index (CPI) series.

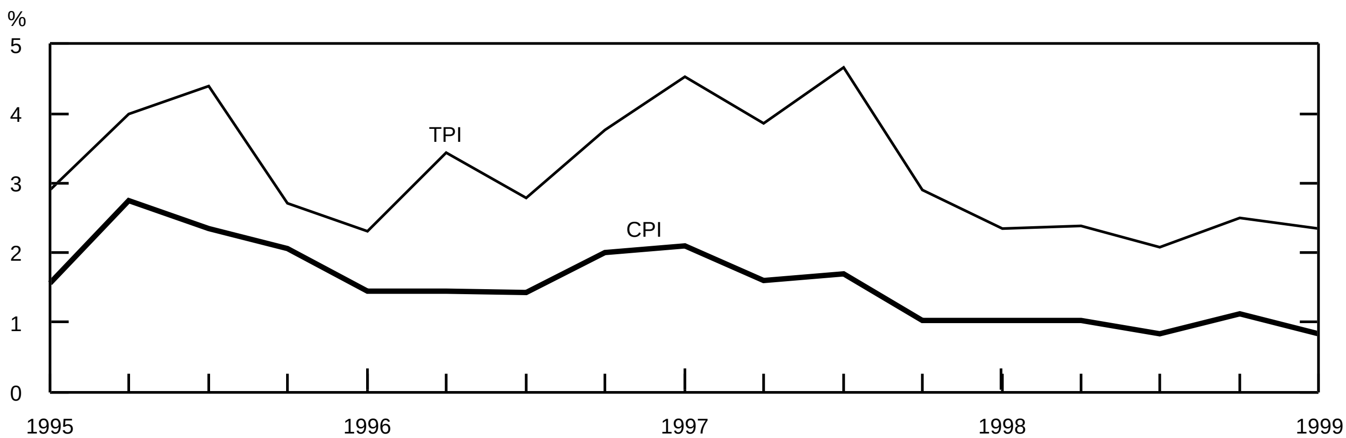
A technical report on the Travel Price Index is available from the Tourism Statistics Program at (613) 951-1673.

The TPI drops 0.6% from the previous quarter

In the first quarter of 1999, the Travel Price Index was 118.2. Travellers paid more in the first quarter of 1999 than the previous quarter for inter-city transportation and food, among other components. However, lower costs for accommodation and automotive vehicle rentals more than offset increases in the other components, resulting in a total drop of 0.6% in the TPI between the fourth quarter of 1998 and the first quarter of 1999. During the same period, the cost of consumer goods included in the Consumer Price Index (CPI) rose 0.3% over the previous quarter.

Data on the Travel Price Index are now available on Cansim, matrix 2510.

Quarterly Percentage Change in TPI and CPI from Preceding Year



TRAVEL INDICATORS

	First Quarter		% Change
	1998	**1999**	
VISITORS TO CANADA (000s)			
From United States	7,403	7,605	2.7
One or more nights visits	1,803	2,012	11.6
- By auto	1,071	1,165	8.8
From Overseas	521	564	8.3
One or more nights visits	502	547	9.0
Top Seven Countries:			
United Kingdom	107	118	10.3
Japan	68	67	-1.5
France	49	51	4.1
Germany	36	39	8.3
Australia	23	26	13.0
Hong Kong	25	23	-8.0
Taïwan	16	20	25.0
CANADIANS OUTSIDE CANADA (000s)			
To United States:	9,809	8,711	-11.2
One or more nights visits	3,040	2,882	-5.2
- By auto	1,455	1,318	-9.4
To Overseas (one or more nights)	1,395	1,461	4.7
INDUSTRY			
Airline passengers (Level I) (000s)	5,547	5,423	-2.2
Airline passenger-km (Level I) (000,000s)	13,792	14,325	3.9
PRICES 1992 = 100 (not s.a)			
Travel Price Index	115.5	118.2	2.3
Consumer Price Index	108.3	109.2	0.8
- Restaurant meals	109.6	111.4	1.6
- Inter-city transportation	149.7	157.1	4.9
- Renting and leasing of automotive vehicles	113.4	117.0	3.2
- Gasoline	100.5	94.8	-5.7
ECONOMIC			
Gross Domestic Product, 1992 prices (s.a.) (000,000s)	712,685	731,227	2.6
- Amusement and recreation (000,000s)	7,672	7,973	3.9
- Accommodation and food services (000,000s)	18,858	18,789	-0.4
Personal disposable income per capita (s.a.)	18,206	18,453	1.4
LABOUR (000s)			
Labour force (s.a.)	15,515	15,896	2.5
Unemployed	1,338	1,246	-6.9
Employed	14,177	14,650	3.3
- Accommodation and food services (not s.a.)	905	894	-1.2
EXCHANGE RATES (in Canadian dollars)			
American Dollar	1.43035	1.51133	5.7
British Pound	2.35455	2.46845	4.8
Japanese Yen	0.01117	0.01299	16.3
German Mark	0.78644	0.86772	10.3
French Franc	0.23469	0.25872	10.2

(s.a.) seasonally adjusted.