Air Passenger Transport In The APEC: Regulatory Impacts and Prospects for Asia Pacific Integration

Massimo Geloso Grosso
The OECD Trade and Agriculture Directorate

Abstract

This study aims at assessing the prospects for a more liberal air passenger transport regime in the Asia Pacific region under the auspices of the Asia Pacific Economic Cooperation (APEC). The decades-old bilateral air services regime has been under pressure to reform for several years. Notwithstanding the critical role that international air transport plays in the ongoing integration of Asia Pacific economies, the airline industry remains one of the region’s most heavily regulated. Estimates from the gravity equation employing the Air Liberalization Index (ALI) developed by the World Trade Organization (WTO) Secretariat find a positive and statistically significant relationship between relaxing bilateral air services restrictions and air passenger traffic. The results hold for a wide range of specifications controlling for fixed effects, different sample sizes, and for all variants of the ALI. The preferred specification, the Anderson and Van Wincoop (2003) equation, provides the most conservative estimates. Prior to taking account of general equilibrium effects, the results imply that if APEC economies eased air transport restrictions to double the ALI scores with their aviation partners, both within and outside the APEC region, traffic would increase by 4.5%.

- **JEL Classification:** F13, F15, L93
- **Keywords:** Air transport, Asia Pacific, Trade Policy

*Corresponding address: Massimo Geloso Grosso; Tel: +33(0)145248924; Fax: +33(0)144306163; E-mail: massimo.geloso-grosso@oecd.org; Postal address: 5 rue de Marronniers, 75016 Paris. ©2012-Center for Economic Integration, Sejong Institution, Sejong University, All Rights Reserved.*
I. Introduction

Air transport services’ development as one of the most dynamic recent growths in all sectors in the transport industry has proven vital to the international trade of both goods and services. Air conveyance often represents the only viable means of transport to remote, peripheral regions and landlocked countries, particularly in the developing world in light of more limited land transport infrastructure. International transport is considered a prerequisite for the development of tourism, accounting in developing countries for nearly 80% of international tourist arrivals (UNESCAP, 2005). Air transport is also at the core of developments in transnational production and just-in-time supply management, and a key determinant in meeting the demand for time-sensitive products, such as perishable goods, textiles and clothing, and electronics.

The Asia Pacific region has seen solid expansion in air passenger transport, notwithstanding the intervention of recent external events, currently accounting for over a quarter of world traffic (see Figure 1). The rapid growth of Asian airlines, which in the past accounted for a tiny share of world traffic, has brought about considerable changes in the structure of the international industry. Hong Kong, China, and Singapore, although featuring a non-existent domestic market, rank very high in the world in terms of international traffic. China has experienced burgeoning growth; it is already the fifth largest passenger market and is projected to become in the next two decades the second largest aviation market in the world. According to the International Civil Aviation Organization (ICAO), 11 APEC economies are in the top 20 list in terms of international operations.

The Asia Pacific region is also predicted to become the largest world air transport market in the near future, in light of its growing economic importance, population, and geography. The region has experienced the highest GDP growth rates during the last decade or so, driven by China’s robust growth. As a whole, APEC’s GDP experienced an average annual increase of 4.9% between 1995 and 2005 (CAPA, 2007). The relatively long distances in the region, its many islands and slow development in alternative transport modes, such as high speed trains, make air transport the most practical means of travel. Considerable air service connectivity potential remains, given that only a few APEC economies have multiple hub systems. For example, Indonesia, in addition to its archipelagos, has dozens of cities with more than one million people, but its international connectivity remains at relatively low levels (PATA, 2007).