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REMARKS PREPARED FOR DELIVERY BY DEPUTY SECRETARY ALAN BUTCHMAN TO THE INTERNATIONAL AIR TRANSPORTATION CONFERENCE, BOSTON, MASSACHUSETTS, MAY 3, 1978

I am pleased to be here tonight, in this distinguished company and among so many people dedicated to the growth and safety of air transportation.

The proceedings of this conference make two things very apparent.

1. In its 75th year, aviation is a thriving, growing industry -- on the leading, not the trailing edge of new technologies; and

2. The international aspects of air transportation loom larger and promise to become increasingly important to aviation's future.

For my part in your 1978 International Air Transportation Conference, I will leave the technologies of microwave landing systems, wind shear prevention, wake vortex systems and the other marvels of the technician's art in your very capable hands. I want to focus instead on several matters of policy that must be resolved if we are to put those technologies to work, dealing with today's problems and meeting tomorrow's needs in a world made continuously smaller and more intimate through aviation.

COMPETITION

There is something highly significant happening in the aircraft manufacturing, electronic and air carrier industries: they are becoming more competitive.

We have just concluded a long and spirited competition between the U.S. developed time reference scanning beam (TRSB) microwave landing system and the British doppler system. As you know, the 60 ICAO countries meeting in Montreal last month endorsed the U.S. system as the world's standard.

Eastern's recent $775 million order for 23 European A-300 Airbus aircraft ...ked the first time in nearly 20 years that a foreign-built airplane has been

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selected by a major U.S. airline. Largely on the strength of that purchase, a European consortium is now promoting the smaller B-10 version of the A-300 and two new transports -- the 130-seat JET-1 and the 160-seat JET-2 -- in the world airline market.

The competition for international air travelers is also intensifying. Nineteen seventy-seven, as you know, was a record year for air travel. The world's scheduled airlines carried 514 million passengers, up eight percent over 1976. Revenues increased 12 percent. This year promises to be even better. Since the Freddie Laker Skytrain and Super Apex discount fares were not introduced until September of last year, the substantial impact of those competitive fares will not be reflected fully uuntil the 1978 traffic and profit figures are in.

The point is, competition is escalating, in the international as well as in the domestic markets, stimulating growth and raising load factors. We have always believed in competition in America, and we believe competition at the international levels will prove to be a healthy influence for aviation progress.

Competition is the keystone of the regulatory reform legislation now in Congress. It is the driving force in the U.S. airline industry's new prosperity. And it is central to our international air transportation philosophy.

REGULATORY REFORM

The Administration's decision last year to support airline regulatory reform and other programs to allow more competition in the marketplace is part of a broad policy to simplify government regulation and increase competition.

The full cost of government regulation of our economy is hard to pin-point, but it is high -- for business, for the taxpayer and ultimately for the consumer. A recent study for the Congressional Joint Economic Committee estimated the cost to be in the billions. We want to reduce the cost by eliminating regulatory restraints where they no longer serve a useful purpose. President Carter has called passsage of meaningful aviation regulatory reform one of the most important anti-inflation issues now before Congress. The Senate acted last month to support reform by an overwhelming 83 to nine vote.

The issue is now in the House where, during a pre-Easter recess mark-up session, the Public Works aviation sub-committee voted a substitute bill which -- in our judgement -- would not be good legislation. That proposal has since been amended by its sponsors, but as it now stands in the House, the compromise bill contains few meaningful provisions.

In other words, it's a reform bill in name only. And while it makes almost no provisions for phasing out regulatory controls by permitting increased competition in the industry, the bill as now written passes a death sentence on the CAB, calling for its demise in five years -- which would leave the airlines, presumably, suddenly and totally unregulated.

I don't think there is any way Congress is going to let that happen. In fact I don't think the reform movement can be denied. There is too much momentun, too much logic and too much need for constructive change. The airlines, in fact, have tasted the fruits of competition and most of them like it.

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U.S. AIRLINE INDUSTRY -- RETURN TO PROSPERITY

Under the less-restrictive regulatory policies of the present Civil Aeronautics Board, U.S. carriers chalked up a record year in 1977. The airlines carried 240 million passengers, an eight percent growth over 1976, and ended the year with an estimated $740 million in earnings. The 11 U.S. trunk carriers alone boosted their 1976 profits by 82 percent, to $584 million.

Industry executives attribute much of the growth in traffic, and profits, to the wave of "supersaver" and other discount fares which induced travel and improved load factors. The load factor for domestic flights in March reached 61 percent, compared to 55 percent a year earlier.

In other words, the carriers have made the pleasant discovery that competition <u>can</u> be good for business. Promotional fares have filled a lot of seats that otherwise would fly empty. The airlines have found that you can cut fares and still operate at a profit. I think it's also plain to see that the pressure for regulatory reform has had a decided effect both on the CAB's ratemaking practices and the airlines' fare policies. As the carriers have experimented with fare reductions of 40 and, in some cases, 50 percent and found that the lower rates generate more revenue than they cost, the CAB proposed last month that such fare cuts -- up to 50 percent -- be permitted without prior agency approval.

Perhaps the industry has been too timid in the past, not believing its own traffic projections. In the '60's the airlines over-invested in new equipment, vastly increasing capacity but doing little to stimulate new traffic. Today's better profits are largely the result of the industry's success in structuring discount fares to make better use of existing capacity.

Moreover, the potential for further growth appears excellent. Bill Seawell of Pan Am noted recently that more money is now spent worldwide on tourism than for armaments. And the latest FAA aviation forecasts indicate that travel on U.S. airlines will increase by 80 percent in the next 10 years, to 420 million passengers by 1989. In other words, air travel may double in little more than a decade.

The phenomenal growth in air transportation is not limited to the U.S. trunk carriers alone. The local service and commuter industries had record years in 1977. As I have already noted, it was also a banner year for international air travel. And the potential for growth is perhaps greater in the international area than in any other segment of the air transportation industry.

INTERNATIONAL AIR POLICY

It has not always been so.

We've traveled a hard and sometimes rocky road in international air transportation policy over the past eight years. The issue has been debated in three separate Presidential policy reviews, and the preferred direction of U.S. international policy has not always been clear or distinct.

The situation today is different. We have developed the framework for an international air policy, we have coordinated that policy throughout the Executive branch, and we now seek to join with the rest of the world to develop a workable, reasonable pattern for air travel in mature markets. We want a policy that is fair to the travelers and one that assures there will be a U.S. airline industry able to serve the market, able to grow to meet the demands of the market, and able to compete vigorously in that market under rules that are fair and reasonable for all the various interests involved.

One point fundamental to the development of current U.S. international air transportation policy is the recognition that both scheduled and charter services compete for the same basic market. We believe that this competition is healthy, and that if it is allowed to take place it will result in more efficient and lower cost air transportation. Fares and rates will find their own levels, based on competition in the market place, and these levels will allow efficient and well-managed airlines to be profitable and economically healthy.

As leading aviation authorities have noted, to impose economic regulation on air transportation it's necessary to regulate both rates and capacity, or neither. A system that's half slave and half free can't be effectively regulated without creating economic inefficiencies which, in turn, require even more regulatory patchmaking. And trying to force this kind of regulation on a system that is inherently dynamic and competitive results in a crazy-quilt pattern that serves nobody.

The United States' position is clear. We will not accept capacity regulation. We intend to work to minimize rate and fare regulation -- or at least to ensure that the marketplace is competitive enough to make sure that competition, and not government edict, keeps fares low and services efficient. Our objective is to provide the greatest possible benefit to travelers and shippers. Our bilateral agreements are and will be negotiated with that purpose in mind, and our intent is to focus on the major international air markets as the best means of demonstrating our commitment to that basic principle.

Over the years, the United States has stood almost alone in the world for the principle of competition in the international marketplace. We believe that a competitive policy has several benefits. First, from a governmental viewpoint, encouraging airlines to be both competitive and profitable is better than a policy of government subsidy. Subsidy is expensive for governments. However it may be rationalized, no government wants to pour endless capital into an enterprise which, properly managed and developed, could be self-supporting. The world airlines' projected financial needs through 1987 may total $70 billion. All governments are hard-pressed to find enough resources to cover their expenses and none should have to allocate scarce economic resources to their airlines on so large a scale.

Second, a nation's interest in the prosperity and self-sufficiency of its airlines is better served by a policy of market expansion and growth than by a policy of protectionism.

Third, by offering more services to the public, the international air transport industry can stimulate traffic growth, generating new markets and produci[ng] increased revenue both for their airlines and for related industries such as tourism. We've seen it happen in the domestic market, both scheduled and charter, and the international potential is even greater.

Let there be no mistake. We cannot and do not seek competitive advantage. What we want, and believe is fair, is competitive equity. We do not believe that market capacity should be divided equally, according to some arbitrary standard, but we do hold that each country's airlines should have an equal opportunity to compete for business. Market share is best determined by passenger choice.

I might note, in this regard, that U.S. flag carriers do not dominate the international market. Our international airlines last year carried 19.5 million passengers, or less than four percent of the world total.

In our international negotiations today we are striving for a competitive system that serves these specific objectives:

1. Encourages innovative pricing and fare flexibility to meet the needs of different consumers;

2. Liberalizes charter rules;

3. Reduces or removes capacity restrictions;

4. Eliminates discriminatory or unfair competitive practices;

5. Permits mutliple U.S. airlines in international air markets; and

6. Encourages greater access to international markets by permitting more non-stop service points and improves the integration of domestic and international airline services.

These objectives reflect our commitment to an expanding low-fare interntional aviation system based on competitive market forces. Let me emphasize here that it has never been U.S. policy to seek these objectives at the expense of another nation or its airlines. We believe in reciprocity. Our strategy, however, is to trade competitive opportunities rather than restrictions, and to make concessions only in return for progress toward competitive objectives and a fair marketplace. We continue to believe that protectionism is self-defeating -- that benefits flow from promoting, not shutting off, new avenues to lower cost air transportation -- that competition promotes operational proficiencies, performance and profits.

Before leaving this subject, let me just note that there are obvious connections between our objectives in the area of international policy and our support for aviation regulatory reform. We could not, in good conscience, plead for increased competition in international markets and at the same time reject the concept at home. We cannot seek international fare flexibilities and greater route freedoms, and deny domestic reforms that would permit the same benefits to U.S. citizens. The importance of consistency in our international and domestic aviation objectives has been recognized by the Senate, and will prevail -- I am confident -- in the final reform legislation voted by the Congress.

NOISE REDUCTION AND NEW EQUIPMENT

Finally, I want to say just a few words about the airlines' need for new aircraft and the industry's prospects for financing those purchases.

Several factors are involved. One, present fleets -- particularly those of the biggest U.S. carriers -- are getting old. The average age of one airline's planes is 11 years -- and while aircraft of that vintage are safe and serviceable, they are not as fuel-efficient or as quiet as newer models.

A second factor is capacity. After years of surplus capacity, demand is now increasing and airlines contemplating new routes do not want to be late in placing orders.

A third factor is noise reduction. Current regulations require that the entire U.S. commercial air fleet be brought into compliance with revised noise standards by 1985. About 75 percent of the 2100 jet aircraft now in use do not meet the established standards. To assist the carriers in cutting jet engine noise we support a bill now before Congress that would provide a special supplementary funding mechanism for the replacement or retrofit of the non-complying aircraft. That bill would establish a two percent environmental surcharge on passenger travel and air freight -- essentially a ticket tax -- to help pay the costs of retrofit and replacement. At the same time the current taxes paid into the Airport/Airway trust fund would be reduced by the same amount, for a zero net effect on the cost to the air traveler and shipper. We would prefer a $2 surcharge on all international departures, and permit foreign carriers to set up escrow accounts to be used for new aircraft procurements or retrofit expenditures.

While it might appear from the improved profit picture that the airlines are capable of financing their own equipment needs, it must be remembered that we are talking about a very large investment -- perhaps $25 to $40 billion domestically -- over the next 10 to 12 years. Airline analysts seriously doubt the industry's ability to generate the necessary financing internally.

The supplementary funding program we are recommending, together with regulatory reform, will help establish the new foundations of confidence needed by the airline industry to restore lender support, and by the manufacturers to spur aircraft development.

The result, we believe, will be more jobs in the aircraft industry, a strengthening of U.S. aerospace exports (which last year contributed $9.2 billion to our balance of trade), and new airliners that will be quieter, cheaper to operate and up to 40 percent more fuel-efficient.

CONCLUSION

Air transportation has grown tremendously -- and is still a growth industry -- because it satisfies a universal need. We have the technologies to make air commerce even more popular and ever more successful -- by making flight more convenient, more affordable and safer. Competition between companies and between nations is producing better products and better air service. Our task is to see that institutional progress keeps pace with today's marketing and technical developments, so that international air transportation is not hindered from achieving the great destiny so clearly ahead.

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