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THE EFFECT OF REGULATED COMPETITION ON THE AIR TRANSPORT INDUSTRY

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For the past several years the air transport industry has been the subject of a great debate. For the most part, it has been a one-sided debate with rather broad assertions and contentions being made before Congress, the Civil Aeronautics Board, and the public. These broad assertions have sought to prove that there has been a concentration of air traffic in the hands of a few “grandfather” carriers who, as a result of that concentration, have enjoyed “excessive profits.”

This article will demonstrate how wrong these contentions have been. It will show, briefly, the reasons for the enactment of the Civil Aeronautics Act of 1938; the nature of air transport regulations; the record of certificated air transportation under regulation of the Civil Aeronautics Board; the contributions of certificated air transport to national defense and the postal service; the prevailing extent of intense competition in domestic and international air transportation; the fact that there is neither concentration nor monopoly in certificated air transport today and little prospect that it can be expected in the future; and the fallacious reasoning behind any doctrine designed to substitute unlimited right of entry for the prevailing and proven philosophy of regulated and restricted competition under the Civil Aeronautics Act.

The Nature of the Business of Air Transportation

Before discussing the record of certificated scheduled air transportation in detail, it would be well to look at the general nature of the business. For, as one of the most—if not the most—precisely regulated of all public service industries, scheduled air transport submits to certain restrictions and must discharge certain obligations.

The industry is regulated not only as to basic policy but, as will appear shortly, as to the innumerable details of its daily business. And,
in addition to its general obligation to be of public service, the industry has specific obligations to the commerce, the postal system and the national defense.

The regulations and the obligations both exist because Congress, some 17 years ago, determined that a scheduled air transport system must be created to meet a public need. The administration of the law governing the development of the scheduled air transport industry was entrusted to a federal agency, the Civil Aeronautics Board.

One of the general objectives set was that the industry must be of general public usefulness. It is the task of the industry to provide a universal air service—service not just for passengers, but for mail and goods; service not just for the large cities, but for the country's smaller communities. In brief, the duty of the industry is to develop air transport. A second objective was that the industry must be competitive. A third objective was that the industry must become strong and self-sustaining.

How the objective of developing air transport has been served can be told in the growth of traffic, the addition of schedules, the introduction of new equipment—the production of more and more service at less and less cost to the public. How the objective of becoming more competitive has been served is conveyed in many ways: in the story of parallel services being established; in the vigor of the competition as reflected, to some extent, in the lusty promotional campaigns and the large volume of advertising sponsored by the industry. The drive for self-sufficiency is reflected in the fact that subsidy is a smaller and smaller proportion of industry revenues and, in recent years, has annually required a smaller appropriation, despite greatly increased service.

Two additional general observations may be made before going into detail. One is that, in addition to actually being the world's most competitive air transport system, if not the world's only competitive system, the American-flag airlines compete with the great foreign-flag systems. It is worth noting that this competition is no longer restricted to the international routes. Under established government policies, foreign-flag airlines are given traffic rights which compete, directly and indirectly, with our domestic airlines. And, through special procedures, the foreign-flag airlines may receive hearings and decision far more rapidly than is possible for our own airlines.

The second general observation is that, although this country's scheduled air transport has, as the figures show, discharged its obligation to be of service to the commerce, the postal system and the national defense, as yet it has not fulfilled completely the promise it has held out for its investors. The measure of the industry's increased usefulness is to be found in gross traffic figures, in gross revenues. But the measure of its strength for the future is found partly in its net income. And the increase in net income has not been commensurate with the increase in grosses.
REGULATED COMPETITION

THE BACKGROUND AND PHILOSOPHY OF THE
CIVIL AERONAUTICS ACT OF 1938

At the outset, it should be made perfectly clear that the Civil Aeronautics Act of 1938 was a carefully considered statute which was designed to create a system of regulated competition for commercial aviation. At the time of the passage of the Act, its sponsor in the House, Representative Clarence F. Lea, pointed out that the Act was necessary because "the industry has reached the point where unbridled and unregulated competition is a public menace . . . ."¹ It was not surprising that the will of Congress changed the nature of the unrestricted competition previously inherent in air transportation and statutorily prohibited it for the future. Prior to and since the Act of 1938, other public service enterprises had or have been placed under public regulation, which meant that they were removed wholly or in part from the workings of a free enterprise system and from the play of unrestricted competition. This was not applicable only to those public utilities which we know as natural monopolies. This same type of economic control was applied to radio and television and, in the transportation field, to our railroads, our truckers, our bus companies and our pipelines as well as our airlines.

The purpose of this approach resulted from the understandable conviction that, in many circumstances, unchecked and unrestrained competition was harmful to the community. Certainly, the history of air transportation before 1938 gave further validity to this contention.

When Congress passed the Civil Aeronautics Act, the financial situation of the air carriers had become so chaotic as to shake the faith of the investing public in their financial stability and to prevent the flow of funds into the industry. Fifty per cent of the $120,000,000 of private capital that had been invested in the air transport system before 1938 had already been lost. Congress was aware of the history of "boom and bust" which had made the railroad industry a chronically sick industry. In 1938, when the Civil Aeronautics Act was passed, one-third of all railway mileage was in the hands of receivers or trustees.

The Civil Aeronautics Act was enacted to provide unified regulation of the air transportation industry in accordance with a comprehensive and long-range program based on sound economic principles. Congress intended to prevent uneconomic and destructive competition and wasteful duplication of services. The Senate Committee which reported the bill which eventually became the Civil Aeronautics Act put the matter succinctly:

"Competition among air carriers is being carried to an extreme, which tends to jeopardize the financial status of the air carriers and to jeopardize and render unsafe a transportation service appropriate to the needs of commerce and required in the public interest, in the interests of the Postal Service, and of the national defense."²

¹ 83 Congressional Record 6407, 6507 (1938).
Accordingly, any evaluation of commercial aviation today and of the Civil Aeronautics Act of 1938 must be against a background of the purposes of the Act and the recognition that the Act enunciated a doctrine of restricted competition. Whether that Act has been successful, whether there is any validity to the contentions recently made by a handful for limitless freedom of entry, and whether the nature of the service suggested by new entrants and applicants would serve the public interest must be considered in the light of the Act's philosophy.

Whether or not air transportation is a public utility in the same sense that gas and electricity and telephone companies are, it should be clear from the preceding brief exploration of the basic thesis underlying the Civil Aeronautics Act that it probably is the most precisely regulated of all public service industries. Indeed, the Civil Aeronautics Board has concluded that the "Statutory provisions of (the Civil Aeronautics Act) the legislative history, and decisions under the Act plainly establish that air carriers are to be regulated as 'public utilities' as that term is generally understood." 3

It should be sufficient to point out that the nature of existing legislation imposes upon airlines which are certificated a substantial quantum of regulatory responsibility. As will be pointed out, the powers of the Board over air carriers, all of whom are by definition "common carriers," are, as the Civil Aeronautics Board itself stated, "consistent with and similar to those normally applicable to regulated public utilities." 3

In order to enter air transportation, you must be certificated by the Board. In order to receive a certificate, you must show not only that your service is in the public convenience and necessity but that you are fit, willing and able to perform it. A certificate, when issued, specifies the cities you may serve and the extent to which you can vary from the stringent requirements set out in that certificate.

Once an applicant has been certificated, he may not suspend service without Board approval nor abandon any service without permission granted by the Board after hearing and argument. However, the Board, after a hearing which it, itself, may initiate, may alter, amend, modify or suspend a certificate.

Airline prices are regulated. Individual and joint rates must be reasonable and non-discriminatory. All rates, classifications and rules must be published and uniformly observed. Tariffs believed to be unlawful can be suspended. Adequate service must be provided. A carrier cannot discriminate among persons, cities or types of traffic. A carrier certificated to carry the mail, although paid for it only on a compensatory basis, must carry that mail with a priority over all other traffic—despite the fact that mail travels more cheaply than people. If the Post Office Department prescribes additional mail schedules, a carrier must adhere to such prescriptions.

3a Hearings on S. 2647, op. cit.
There is no phase of an air carrier's operations which is not regulated. Consolidations, mergers, acquisitions of control, purchases, leases and contracts to operate the properties of other carriers or other persons are subject to approval, all of this after Board hearing and all of it subject to the caveat that approval will not create a monopoly in restraint of competition. Interlocking directorates are subject to approval. Every pooling arrangement, even if it involves the joint use of a loading ramp or a gate position, is subject to Board approval.

Accounts and records must be kept on Civil Aeronautics Board-prescribed forms. Periodic and special reports must be filed. The records of every airline are subject to regular Civil Aeronautics Board inspection and audit. An air carrier is subject to the labor provisions of the Railway Labor Act. Above all, an air carrier is subject to Civil Aeronautics Board investigation into the management of its business, its practices, its methods of competition, and anything else at the will of the regulatory agency.

The foregoing requirements have been cited briefly to illustrate the nature of the business in which certificated air carriers are engaged. It is important to appreciate that, to a very great extent, the advantages granted by certification in the public interest are balanced by the obligations of enfranchisement.

THE RECORD OF CERTIFICATED AIR TRANSPORT SINCE THE PASSAGE OF THE ACT OF 1938

The Civil Aeronautics Act, like others before it and since it, created a bipartisan regulatory agency, whose members are appointed by the President with the advice and consent of the Senate. It has the unquestioned responsibility to make decisions in the public interest and the public convenience and necessity.

A logical question is the extent to which, since 1938, the doctrine of regulated competition has produced, under CAB guidance, a sound air transport system, with particular reference to its competitive flavor and the absence of monopoly. Perhaps this question can be answered best by citing the record of certificated air transport—one shared mutually by the Civil Aeronautics Board and the regulated airlines.

The 17-year period since the passage of the Civil Aeronautics Act has not been one of undisturbed expansion. The development of air transportation, airlinewise and aircraftwise, has been handicapped by World War II and, more recently, by the hot/cold war of 1951-1955. So, it really is not fair to say that this progress in commercial certificated air transportation should be measured against a yardstick of a full or continuing 17-year period.

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In 1938 the Board was handed a route structure which it started to work on between 1938 and 1940. This was the initial testing period. Before too long, the airlines went to war. Within six months after Pearl Harbor, 50 per cent of the total fleet of commercial aircraft was used in, and as auxiliary to, the Air Transport Command and the Naval Air Transport Service. Within that same six months' period, a third of the total complement of certificated airline personnel went to work for some arm of the Defense Establishment.

From 1946 to 1949 came the postwar adjustment, with an economic recession suffered by the airlines while the rest of the country was enjoying unparalleled postwar prosperity. Due to manufacturing delays, it was not until 1950 that new equipment can be said to have really replaced the workhorse DC-3. Then, the airlines were able to begin to dig in and to move toward the stability for which they have been striving since regulation came into being in 1938.

Regulation has benefited air transportation. It has benefited the country. Regulation was authorized with a trinity of purpose as set forth in the Civil Aeronautics Act—to serve and develop the commerce of the United States, to facilitate the postal service, and to benefit the national defense.

The Contribution to the Furtherance of the National Defense

The contributions of commercial aviation to the national defense are now history. This was not an accidental occurrence. The ability of the certificated airline industry to assist at the outset of World War II was the direct result of the planning and the thinking done by the then certificated airlines of the United States, cooperating through their trade group, the Air Transport Association. Reginald Cleveland, who tells the story of this great wartime achievement in *Air Transport at War*, has this to say:

"Literally within minutes after the Japs struck at Pearl that Sunday, the Air Transport Association was in touch with General Marshall, Chief of Staff of the United States Army; with General Arnold, Chief of the Army Air Forces; and with Admiral Towers in the Navy Department. The headquarters of the Air Transport Association opened instantly and remained open approximately twenty-four hours a day through the whole war period. When, prior to noon of December 7, the regular channels of government communications failed properly to function and other channels had proved inadequate for federal needs, the FBI operated through the headquarters of the Association."\(^9\)

And, despite all the claims that are made that commercial air cargo carriage was invented after World War II, it should be noted, as Mr. Cleveland points out, that the development of this area of air carriage was stimulated and initiated by airlines' joint undertakings.

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\(^9\) *Air Transport at War*, Cleveland, p. 5, Harper & Brothers (1946).
"Colonel Gorrell (the first President of the Air Transport Association) next convinced the War Department that a survey should be made of cargo requirements within the domestic United States. . . . The objective of this survey was to develop a real cargo service for the Army . . . ."\(^{10}\)

It may be helpful to suggest briefly some specific instances in which the certificated airlines of the United States substantiated the faith of the Civil Aeronautics Board and the U. S. Government in their operations. As Mr. Cleveland so picturesquely states in his book:

"When Rommel's Panzers had General Auchinleck backed up on the African desert so he could almost hear the boatswain's whistle on the admiral's flagship at Alexandria, it was transport flight that saved the day. The Eighth Army commander had anti-tank guns and shells but the shell fuses had been lost in transit. A plane in the United States was pulled off its regular run, loaded with fuses hastily assembled in New York and sent on its way across the Atlantic. The freshly revitalized artillery cracked the hide of the Afrika Corps' famed armored legions and saved the gateway to the East."\(^{11}\)

Add to this the pioneering of the South Atlantic routes by certificated international U. S. carriers, the daily operation over the previously insurmountable Himalayan "Hump," and the astronomical airlift of the certificated airlines operating under contract with the Air Transport Command and the Naval Air Transport Service. The figures are set out in this same volume:

"At the end of our third year in the shooting war the sum of miles flown by the airlines under contract to the ATC and NATS on overseas routes amounted to more than \(2\frac{1}{2}\) billion. Ton-miles flown in carrying cargo to foreign theaters of war were more than 600 million. Transport-miles flown on foreign routes were nearly 250 million and transport-hours racked up overseas, 1,400,000."\(^{12}\)

Air Transport's contribution to the national defense is continuing and current. Today, in 1955, as a result of planning by the Joint Chiefs of Staff, the airlines have created a Civil Reserve Air Fleet consisting of about half of their modern 4-engine fleet—fast transport aircraft capable of non-stop over-ocean flight. These 290 airplanes are already partly modified for military operations and are subject to call—*with their crews*—within 48 hours.

The Civil Reserve Air Fleet represents an investment of \(\$400,000,000\). It would cost the government about \(\$300,000,000\) a year to keep it in operation on a stand-by basis. And its combined airlift—more than two billion ton-miles annually—is nearly ten times greater than the capacity of the civil air fleet which performed with such distinction in World War II.

\(^{10}\) *op. cit.*, p. 59.
\(^{11}\) *op. cit.*, pp. 90-91.
\(^{12}\) *op. cit.*, p. 98.
Contributions to the Development and Enhancement of the Postal Service

The first scheduled air services in the United States were exclusively mail services. There were no passenger or freight revenues to help defray the cost of these services. In a tradition as old as the Republic, the total cost was borne by the government so that the public might have faster mail service. And for some time after passenger and cargo business had started to develop, mail remained a major source of revenue for the airlines.

Today, mail pay is no longer a form of subsidy. The rate for carrying the mail is simply compensation for the service performed. This mail rate is determined by the government after full and open hearings. Today, mail revenue constitutes only 3.5% of the total airline revenues of all domestic air carriers. And of the cost of each 6 cent air-postage stamp, 1.01 cents go to the airlines as payment and 4.99 cents go to the United States Post Office Department.

Recently, the Post Office Department started a new experiment in improved postal service for the public—sending first-class mail on a space available basis between certain points in the United States. In the first year of the experiment, senders of letters saved nearly ten billion hours of delivery time and hundreds of millions of letters reached destination an average of 11½ hours sooner than if they had moved by surface means. The airlines received $0.003 of a penny from each 3 cent stamp covering a letter which traveled by air under the experiment—the Post Office realized 2.97 cents.

In 1954, close to 1,400,000,000 letters were flown, an increase of over 564% since 1938. They were flown into 543 domestic cities, contrasted with the 183 receiving such service in 1938. In 1954, the government received about $98,000,000 in postal revenues from domestic letter air mail, and paid out only $16,500,000 to the airlines for those letters carried by air—or 1.18 cents to the airlines for every 7.01 cents paid by the public to the government for letter air mail.

The international mail and subsidy picture is somewhat different. Almost without exception, it is an important element of national prestige for a country to have an airline carrying its flag abroad and, if possible, into the United States, the principal source of air traffic. However, more than prestige is involved since these other nations, many of whom are our allies, consider that an effective air transportation system in being is an arm of the national defense, and available in the event of a national emergency.

Vigorous and intense competition exists in international air transportation and will continue to exist, not only among certificated airlines of the United States but between United States carriers on the one hand and the many nationally-owned and nationally-subsidized foreign-flag carriers of other nations. In the postwar years 1946-1953, the wholly-owned airline entities of Great Britain, France, the Netherlands, Belgium, Canada, Argentina, Scandinavia, Switzerland, Vene-
zuela and Brazil received a total of $778,000,000 in subsidy from their governments in direct cash, government stock payments, government loans, and value of equipment provided.

In the face of this kind of subsidized foreign competition, the international airlines of the United States have reduced their reliance on subsidy so that such revenues will amount to 4.8 per cent of total revenues in fiscal year 1956. In addition, in 1954, the money required to operate the total U. S. airline system was $1,294,000,000. Of that sum, the government put up about $67,000,000, the airlines put up $1,227,000,000. For every dollar of the $67,000,000 put up by the government to ensure air service where it was needed in 1954, the airlines developed $5.39 in return for the government. In addition, the airlines paid federal gas and oil taxes of $16,000,000 for their share of the use of the federal airways system, although it is calculated that only $12,500,000 would have covered their share for the maintenance and operation of this system.

Further, in the year 1954, the airlines developed revenues for the federal government. The certificated scheduled airlines paid federal income taxes of $67,300,000; the certificated scheduled airlines paid miscellaneous excise taxes of $2,000,000; the certificated scheduled airlines accounted for transportation excise taxes of $120,000,000; the certificated scheduled airlines created total postage revenues for the Post Office Department of $171,700,000—or a grand total of $361,000,000.

Benefits to the Foreign and Domestic Commerce

Next it will be well to note some of the benefits which have accrued, as the Act intended, to our domestic and foreign commerce and trade in the form of more service, improved service and intensified competition.

1. Regulation Has Developed U. S. Domestic, International and Overseas Air Transportation

An important measure of the growth in usefulness of certificated air transport service is in the increase in the number of revenue passenger-miles operated—that is, the number of miles over which paying passengers were carried. The revenue passenger-miles operated by American-flag carriers on both domestic and international routes increased from a half billion (533,052,000) in 1938 to 20 billion (20,511,600,000) in 1954. This is an increase of more than 39 times, or almost 4,000 per cent. The number of seat miles operated, which represents the number of seat miles offered for sale to the public, increased from 1,067,558,000 in 1938 to 33,140,000,000 in 1954. This is an increase of almost 32 times the operation in 1938.

The number of passengers carried increased from 1½ million (1,536,111) to more than 35 million (35,184,000). For every passenger carried in 1938, the certificated airlines in 1954 carried 23. Cargo transportation increased from 2,550,000 ton-miles in 1938 to 347,000,000 ton-miles in 1954. The total airline revenues from traffic other than mail increased from $33,600,594 in 1938 to more than one billion
dollars ($1,289,000,000). During this time, the total number of airplanes in use by certificated airlines increased from about 300 to 1,500—a fivefold increase.

The number of certificated airlines has increased from 22 to 59 in 1954. Miles of authorized airline routes have increased many times. Much of the increased milage reflects the creation and addition of air carriers and competition between the points served.

2. Regulation Has Improved Service

Statistics and maps alone do not reflect the innovations and the high quality of services which are the hallmarks of American air transportation. It was the American air carrier who first conquered the barriers of oceanic distance and who accustomed the domestic traveling public to the convenience of stewardess service, to complimentary meals, and to standard credit arrangements for transportation.

Not only have the American airlines led the world in luxurious and safe airline equipment, but also the airlines offer a truly nationwide transport service. The traveler can go into the ticket office of any certificated airlines in the United States and buy a ticket to any of the 543 cities in the United States served by an airline, and to any place abroad. The magnitude of such an undertaking is evidenced by the vast number of facilitating agreements and arrangements among the airlines of the United States which were necessary to permit any ticket agent of one to issue tickets valid upon any of the others, to use standard ticket and baggage forms and uniform reservation and ticketing procedures, and to reduce service costs in handling traffic.

If the traveler wishes to go to a city other than the 543 cities served by the airlines, he can make arrangements in the airline ticket office for airplane taxi service from the airline point, or rent a car at the airline point to travel to the off-line point of his destination. He can use his airline credit card to charge all of these transportation services.

Substantially similar service is available to travelers wishing to go to any point in the free world served by airlines. Thus, a traveler in Grand Island, Nebraska, can buy an airline ticket that will take him to New Delhi, India, or Melbourne, Australia, and can check his baggage from that point through to his destination.

This same type of national and worldwide service is also offered by the airlines in transporting cargo. A shipment tendered to an airline in Bangor, Maine, will be accepted for delivery at any airline point in the United States and moved to destination on a single air waybill. Door-to-door service is offered throughout the United States. The tariffs governing not only the air transport service but also the pick-up and delivery service are available in a single book, readily available and useful to shippers and consignees. By the same token, a shipper in Grand Island, Nebraska, can send air freight to Djakarta, Indonesia, and can get the only air waybill he needs when he tenders the shipment at Grand Island.
These worldwide services are possible by virtue of working agreements not only between the airlines in the United States but also between practically all of the airlines in the free world. They are intelligible to and honored by air carriers employees in Topeka, Kansas, or Karachi, Pakistan.

Probably the air service system is the only direct carrier system offering such a worldwide service. The benefits of this worldwide service are enhanced by a comparison with the normal international movements of cargo. A shipment from Grand Island to New Delhi by surface carrier would involve one or more transactions from Grand Island to New York, at least a second transaction—and a second transportation document—for the water carriage from New York, and a third transportation arrangement would have to be made when the shipment arrived at Bombay. These transactions in air transportation are reduced to one, and these services are possible by virtue of a vast number of intercarrier agreements reviewed by and subject to the approval of the Civil Aeronautics Board.

This progress was made possible by the fact that air transport is a regulated public service industry. The keystone of this regulation is the certificate requirement. Under it, and before authority to operate may be granted, an applicant must show a need for service, in the public interest, and a fitness and ability to operate the service.

3. Regulation Has Increased and Intensified Competition and Prevented Monopoly

a. The Domestic Route Systems

Two maps illustrate the increase in the route miles in the United States. The first map, figure 1, shows the routes authorized in August, 1938, and the second map, figure 2, shows the routes authorized at the end of 1954. The number of cities served increased from 183 to 543.

Even this does not show the full extent of the routes currently operated. First, the map does not show the duplicate services between many cities. For example, over the route between New York and Chicago, four carriers currently operate; similarly, over the route between Washington and Chicago, four airlines operate; and over the route between New York and Los Angeles, three airlines provide service.

Secondly, this map does not show the interchange services. Between Miami and Los Angeles, a passenger can board an aircraft at one point and fly through to the other, in the course of which he will travel over the routes of the three airlines in the same aircraft. There are currently 12 of these interchange arrangements, which provide a service comparable to an additional through route.

b. The International Route Systems

Three maps graphically illustrate the extent of the increase in competition in international operations.
In 1938 there were two short routes into Canada, a bare segment into the Caribbean and Mexico, one route along each coast of South and Latin America, and a route to the Philippines and Hong Kong via the Central Pacific. In 1954 note the extensive U. S. flag competition across the Atlantic and Pacific to Europe, the Middle East, India, Japan, in the Caribbean and down through all of Latin America.

The third map shows the concentration of foreign-flag lines to gateway points over the Atlantic, the unbelievable number of foreign carriers in the Caribbean and Latin America (not all the smaller ones are shown), and the surprising number of foreign-owned airlines competing with our carriers for the thin traffic over the Pacific to the Orient and Australasia.

This last map of foreign-flag competition, figure 5, does not show the recently-inaugurated operation of West Germany's Lufthansa. Nor does it show the extent to which the grant of air rights, by our government, to foreign-flag lines diverts transcontinental air traffic. To date, Scandinavian Air Lines alone has been authorized to fly the polar route and carry passengers all the way from the West Coast without their having to use U. S. carriers to reach East Coast debarkation points. The British, Australians, Japanese and Germans are currently negotiating for similar authority.

In addition to the fact that there are few routes in the international system which are operated exclusively by any one U. S. flag carrier, there is the additional fact of competition between United States carriers, on the one hand, and carriers of foreign countries, on the other.

c. Traditional Transportation Patterns

Traditionally, in order to provide transportation to as much of the public as possible, regulation has been required. In 1953, service was provided to over 540 airports in the domestic United States. Fifty-five out of every 100 passengers who used air transportation came from only 15 of those 543 airports. Some 528 airports accounted for the remaining 45 per cent. It is clear that, if there had been no regulation, the quantity of service and the extent to which service has been provided to different and less populated areas of the United States would have been curtailed substantially. Or, to put it differently, an overwhelming majority of the cities to which the airlines provide service just do not generate enough traffic to warrant operations if air transport were not regulated and was subject only to the rules of the "free" market place.

Existing traffic patterns within the United States require regulation. It is evident to anyone who analyzes the airline service to the 48 states that the quantity and extent of the service now existing would be impossible without regulation. Regardless of the number of passengers enplaned or the number of cities served, between 70 and 90 per cent of all traffic generated within a particular state comes from one or two cities.
As an example, in 1953, 13 airlines served 18 cities in New York State and yet 80 per cent of the traffic was developed out of the New York City airports. As further examples, note the following: in California, although 36 cities were served, 85 per cent of the traffic was out of Los Angeles and San Francisco; in Florida, although 21 cities were provided service by 5 airlines, 71 per cent of the traffic developed in Miami and Jacksonville; in Michigan, with service being provided to 18 cities, 80 per cent of the traffic originated in Detroit; and in Illinois, 96 per cent of the passengers at 11 cities in the state were enplaned at Chicago.

It is surprising to some that trunk carriers as well as local service carriers provide service to the smaller cities in the United States. The trunk lines are able to do this because the losses sustained at these marginal cities, which also deserve the advantages of air transportation, are compensated for by the revenues developed at the greater traffic-producing areas—most of which, for long-haul-carriage purposes, are highly competitive. Figures submitted by the Civil Aeronautics Board for six of the largest domestic trunk lines show a substantial quantity of what the Board called “marginal or loss points”: American Airlines with 23 such points served of the 61 on its route system; Delta-C&S with 28 points of its total of 48; Eastern with 40 of its 81 points; National with 21 of its 30; TWA with 18 of its 51; United with 35 of its 61.18

d. The Nature of the Development of a Balanced, Competitive, Self-Sufficient Trunkline System

Against this record of demonstrated progress are advanced many arguments which suggest that competitive opportunity in the industry has been reduced rather than expanded in the face of an unlimited air carrier market.

One of the arguments frequently advanced is that the trunkline industry has contracted from 16 carriers which existed in 1938 to just 13. Proponents of this view usually suggest that the 13 may ultimately become fewer. Of course, it is a possibility if, in the judgment of the Board, such contraction is necessary to maintain a strong air transport system, still competitive but better balanced. No one seriously contemplates or predicts that there will be a reduction to four or five trunks. However, there is every reason to believe that those which exist today will become better balanced and compete more effectively with one another.

In 1938 there were in existence a number of air carriers who were not very strong. In fact, it is wrong to call all of them in existence at that time trunk carriers. If, however, that categorization is used for 1938, it is only fair to say that the original 16 are now 26. For, although 16 “grandfather” carriers are now 13, there are an additional 13 domestic local service airlines of varying sizes, all of them substantially larger than a majority of the original “grandfather” carriers at the time of their certification.

18 Hearings, S. 2647, op. cit., p. 764.
From 1938 to date, the Board grappled with the problem not only of straightening out the grandfather systems but of expanding some carriers, duplicating the operations of other carriers, and merging and consolidating weak carriers into stronger carriers—all in the interest of increased service and reduced subsidy.

The basic problem was, and is, to increase competition while strengthening existing carriers to be self-sustaining in keeping with the will of Congress as expressed in the Act. The determination which had to be made was whether you introduce additional groups into the industry or whether you strengthen the carriers already in business as a matter of general public interest, and economy to the taxpayer.

Four striking examples of the extent to which regulation has increased competition, decreased subsidy, and provided for more effective competition and for better balance in the air transportation system is the job that was accomplished by the Board in the instances of Western Air Lines on the Pacific coast, National Airlines on the Atlantic coast, and Continental and Braniff in mid-America. Figure 6 shows the four lines as they existed in 1938 and figures 7 and 8 show them as they were in 1954. In 1938 National was a carrier with two unconnected southernly segments, one across the State of Florida and the other from Jacksonville to New Orleans. In 1954 National is a long-haul operator but has still not neglected the service it continues to provide to the smaller and less profitable cities on its system. In 1938 Western Air Lines had a thin route from Los Angeles to Salt Lake and then to Montana. The 1954 Western system, built over the years and which is responsible for removing the airline from subsidy and making it self-sufficient, illustrates how effective and intelligent regulation results in more service and less subsidy.

Continental Air Lines' system, at the date of the passage of the Act, was represented by a thin line and an even thinner route from El Paso to Denver with little in between of any traffic consequence. Today, Continental's efforts toward self-sufficiency have been materially assisted by extensions into the East as far as Kansas City, southeast to Houston and, most recently, by its acquisition of Pioneer, a local service carrier with a complementary route structure. In 1938, Braniff served the center of the country south from Chicago to Brownsville, with a thin segment from Amarillo to Dallas. Today, Braniff's reliance on domestic subsidy has been substantially reduced and it is providing more and better service with very little subsidy, as a result of the better balance developed over the years. It was permitted to absorb, and thereby insure the continued service of, the economically-threatened Mid-Continent Airlines.

The Board had the opportunity of developing these carriers and others into strong units free from subsidy, and creating competition in that way, or permitting additional groups to enter the business, leaving the weak perpetually impotent and overlaying new carriers on top of them. It rejected, as the Act dictates, the acceptance of a doctrine of
“competition for competition’s sake,” and took the course of developing both a competitive and a strong air transport system for the maximum public convenience and necessity, as the statute requires. Although details of the Board’s various decisions have been contested according to the interests of respective parties, on an over-all basis, the Board was clearly right—particularly when one reviews the progress of the trunk lines, which shows that the initial pioneering was pretty good.

e. The Extent of Competition in Air Transportation Today

The pretense that certificated air transportation is a monopoly is essentially an exercise in semantics. A scare word is employed to picture a situation which is far from monopolistic. On specific routes in the United States, there is more competition among the certificated airlines than exists in any other form of common carrier transportation, in addition to the competition from private carriers. Three airlines operate from New York to Los Angeles and from New York to San Francisco. Four airlines operate between New York and Chicago and Washington and Chicago. Three airlines compete between Boston and New York and New York and Washington. Three airlines compete between San Francisco and Los Angeles.

The important fact is that this duplicative competition exists essentially between those cities to which the monopoly-criers would like to fly. The discontented, who attack the existing system, are not interested in providing air service, now or in the future, to cities like Binghamton, New York; Springfield, Illinois; Tallahassee, Florida; Odessa, Texas; Ogden, Utah; Sacramento, California; Medford, Oregon; Topeka, Kansas; Harrisburg, Pennsylvania or any of the multi-hundred airports generating little traffic, but to which trunk line operations are supported by the revenues generated by the relative handful of large metropolitan areas.

Competitive duplication of service between the 50 pairs of U. S. cities ranking first in traffic volume increased from 45.9% before World War II to 92% in 1954, according to the airline passenger surveys of the Civil Aeronautics Board. Presently, there is competitive duplication by three and four carriers for over 61% of the traffic of these first 50 pairs of cities. Further evidence of the extent of competition and its intensity in air transportation was submitted by the Civil Aeronautics Board to the Senate Interstate and Foreign Commerce Committee, 83rd Congress, 1st Session, in connection with S. 2647, demonstrating conclusively the extent to which the Board, since 1938, has created extensive competition over substantially all of the principal traffic routes in the United States. A more specific example was submitted to the Air Transport Association by one of the largest carriers in the country. This carrier pointed out that, in 1938, only 11.44 per cent of the traffic between the pairs of cities then certificated to that carrier was competitively served; in terms of dollars and cents, of a total of one month’s revenues of $16,300,000, only $1,865,000 was
derived from competitive traffic. In 1955, over these same points, 90.96 per cent of the traffic is now competitively served; a sample month in 1955 shows that, of total revenues of over $28,000,000, better than $25,500,000 was derived from traffic between pairs of cities served by the aforementioned carrier and at least one additional air carrier.

f. Competition with Other Competing Forms of Transportation and the Future of the Common Carrier Market

Air carriers compete vigorously with one another. Even more important, air carriers are competing, in the travel market, with the railroads, steamships, bus lines and, most important of all, with private automobiles—shortly to be a source of even greater competition in the light of the proposed highway construction program.

It is important to look briefly at the nature of the common carrier market in the United States today. In 1946 the common carrier market amounted to a total of over 90 billion revenue passenger-miles. In 1954 that market—the rails, the buses, and the airlines—had declined to a little over 57 billion revenue passenger-miles. Figure 9 illustrates that decline. It is true that the airlines have increased their participation in this declining market—in fact, have created air travel where none existed before—but it is interesting to see where the greatest penetration of this market has been. In 1953 the airlines had a little over 71 per cent of the total common carriage over 1,000 miles. However, of the total of 532,000,000 passengers carried in common carriage in 1953, all but 6,900,000 or 1.3 per cent, traveled less than 1,000 mile distances, and 511,700,000 less than 500 miles. As shown by figure 10,
the airlines carried a relatively smaller percentage of the passengers traveling less than 500 miles than either the bus companies or the railroads.

Accordingly, when one talks about monopoly in air transportation, he should consider carefully the extent to which the entire market is still open to competition, rather than just a portion of it. These figures suggest that the area of greatest prospective penetration is not in those segments which the airlines have successfully penetrated to date but rather in the short-haul field. And, in the short-haul field, there can be no denying that the Civil Aeronautics Board, in its certification of local airlines (whose operating rights have now been made permanent by legislation), has provided for even more intense competition for that market. As equipment more suitable for penetrating the short-haul market is developed, competition no doubt will become even keener.

g. Specific Actions of CAB to Foster Competition by Certification, to Prevent Monopoly, and to Permit New Entry into Air Transportation

The “cry monopoly” approach has two basic weaknesses: first, it ignores the vast majority of the actions taken by the Board since 1938, many—if not most—of which have been adverse to the interests of the
"grandfather" carriers; second, it is based on misleading terminology and innuendo. This is especially apparent in the acceptance of the recurrent propaganda that the Civil Aeronautics Board has never certificated a new domestic "trunkline" carrier. The fact is that the CAB has certificated many new carriers, both domestic and overseas. Many others, such as Western, Continental, National and Braniff, have been converted into "trunk lines" by CAB certification: These charges are, at any rate, substantially refuted by a review of the Board's decisions over the years. The Board, since 1938, has:

Certificated Northeast to compete with American between New York and Boston;
Certificated National to compete with Eastern between New York and Florida;
Certificated Delta to compete with Eastern between Chicago-Atlanta and Miami;
Certificated Capital to compete with Eastern between New York-New Orleans; American between New York-Memphis; TWA between New York-Pittsburgh-Detroit;
Certificated Northwest (the smaller carrier) to compete with United between New York and the Pacific Northwest and between Chicago and the Pacific Northwest;
Certificated Colonial (a smaller carrier) to compete with Pan American between New York and Bermuda;
Certificated Western Air Lines to compete with United between Los Angeles and San Francisco and later extended Western to Seattle;
Selected Northwest for the North Pacific route in preference to Pan American;
Authorized Alaska Airlines and Pacific Northern to operate Seattle-Alaska services in competition with Pan American and Northwest, for the first time giving each of these carriers entry into the United States;
Authorized Delta-C&S and National to compete with Pan American in the Caribbean;
Selected local service carriers to operate throughout the country; the trunk lines were invariably excluded from this field of operation even though they fought hard to secure authorization, and despite the present and even greater prospective competition between the trunks and the local service airlines;
Certificated 4 air freight carriers (all former non-scheduled operators) to operate the best air freight routes in the country—over the violent opposition of the entire domestic trunkline industry;
Certificated Riddle Airlines (a former irregular) to operate a New York-Puerto Rico freight service;
Certificated Aerovias Sud Americana (a former non-scheduled carrier) to operate freight services between Tampa/St. Petersburg-Havana/Central America;
Certificated Mackey Air Transport and Midet Airlines (new carriers) to operate between Florida and the Bahamas;
Certificated Trans-Pacific Airlines (formerly non-scheduled) to operate alongside Hawaiian Airlines in the Hawaiian Islands;
Granted a blanket exemption to the Air Freight Forwarders against the solid opposition of the trunkline carriers;
Required the lowering of airline fares to four and one-half cents per mile in 1945;
Suspended certain proposed coach fares of trunk lines in 1948, thus preventing them from meeting non-scheduled fares for a considerable period of time;
Adopted increasingly drastic policies of disallowances in determining mail rates, resulting in the payment of lower mail rates to air carriers;
Imposed severe labor protective conditions on carriers involved in mergers and consolidations;
Disapproved acquisition of small carriers by large carriers in the cases of American-Mid-Continent; United-Western;
Increased the amount of territorial and international competition among U. S. carriers so that today there are two across the Atlantic; two across the Pacific; five into Latin America, including one all-cargo operator; three to Puerto Rico from the U. S., including an all-cargo line; four to Alaska; and three from the Mainland to Hawaii.

In contrast to these and many other actions which were usually taken contrary to the opposition of the certificated carriers in general or of the larger carriers in particular, conclusions as to “monopoly” are based on the isolated and misleading fact that the CAB has not certificated a “new trunk line.” In the final analysis all this means is that the CAB has not certificated a new carrier to duplicate the existing competitive services between the six or eight greatest traffic-producing cities in the country. Certainly, it does not prove the accusation that the CAB is, in any sense, monopoly-minded or “industry-dominated.”

If the CAB has fostered “monopoly,” how can the fact that it authorized four former non-scheduled carriers (one of whom found it unprofitable to continue to operate) to operate scheduled freight services between all of the major freight-producing cities in the country, one to operate to Puerto Rico and the other with extensive routes to Latin America be explained? This was done over the bitter opposition of the certificated carriers on the basis of a record which barely sustained the finding of public convenience and necessity. Operating results have proven the prematurity of the unbelievable optimism adduced in the Air Freight Case which led to these certifications. Even before this certification, the larger trunk lines had explored air freight and, today, are endeavoring to penetrate that market to an even greater extent.

And how does one explain the hundreds of other decisions where the CAB has authorized competition with the so-called “Big Four”? Certainly, National (then the smallest air carrier) held no hypnotic control over the Board when its route was extended into New York to compete with Eastern. Many other cases can be cited where the smaller, less powerful carriers were certificated for new routes by the CAB over the objection of the larger carriers.

The most significant factor in this whole debate of alleged “monopoly” is the fact that the Board inherited an air transportation network which was very much unbalanced in terms of size and economic
opportunity. A few carriers had the better routes—including the big-
gest cities and long hauls. Continuance of that situation would have
meant the sentencing of the small carriers to a permanent subsidy
status. Faced with this situation, the Board generally developed re-
gional carriers into trunklines, selected the smaller trunk lines to
operate the new competitive routes, and created a new class of regional
carriers known as local service airlines. At the same time, the Board
granted some route extensions to the large carriers, because they were
in a position to provide a large amount of one-carrier service in the
public convenience.

The net result of the Board's actions during the 17 years under the
Act has been to build up substantially all of the trunk lines to a
position where, although by no means wealthy, they are at least cur-
tently self-sufficient. At the same time, the Board has established a
system of competitive service over just about all of the major air routes
of the country. After the war, the addition of new carriers, many of
them former non-scheduled operators, took the form of granting cer-
tificates for which they applied to institute scheduled local service
systems.

There Is Neither Monopoly nor Concentration in
Certificated Air Transportation

Concentration is another one-word argument designed to prove
the existence of monopoly and establish the necessity for greater
"freedom of entry." This argument is based on the fact that, over the
years, the original trunkline carriers have participated in an air trans-
port economy which has expanded some 40 times. Pie charts and bar
charts are used to show the extent to which a few of the larger trunk
lines have been getting bigger and bigger and sharing, it is said, dis-
proportionately in the total amount of available commercial revenues.

Industrial concentration, even in unregulated businesses, is a phrase
of art. Such concentration leads to non-competitive results which
simply are not evident in the commercial air transportation system
today. Perhaps it may be worthwhile to look at some of the elements
of concentration very briefly in order to appreciate better the non-
concentrate situation in certificated air transport.

Thorstein Veblen noted 50 years ago some significant factors about
consolidation:

"In great measure the saving effected is a saving of the costs
of business management and of the competitive costs of marketing
products and services, rather than a saving in the prime costs of
production. . . . The amount of 'business' that has to be transacted
per unit of product is much greater where the various related
industrial processes are managed in severalty than where several
of them are brought under one business management. . . . The
greater the parcelment in point of ownership, the greater the
amount of business work that has to be done in connection with
given output of goods and services. . . . It is in doing away with
unnecessary business transactions and industrially futile maneuver-
ing on the part of independent firms that the promoter of combinations finds his most telling opportunity.”

The hallmarks of concentration are: reduced efforts to sell and the consequent reductions in expenditures in sales promotion; non-expanding markets; maintained or increased prices; static ingenuity and imaginativeness; little inventive progress; prevalence of mergers, consolidations and acquisitions; and excessive profits.

In air transportation, there have been only three trunk line mergers, acquisitions or consolidations since 1938 and, once the local service lines were shaken out of the formative stage as a going business, only one consolidation. This is in sharp contrast with the many mergers effected before the passage of the Civil Aeronautics Act, and with the Board’s rejection of a number of proposed mergers.\(^{15}\)

Competition between the airlines today benefits the public both in service and price. Further, the operating results of the domestic trunkline carriers, admittedly the most profitable segment in the industry, do not reflect that these airlines have enjoyed excessive profits or that their stockholders have received even a satisfactory return on their investment.

**Better Air Service at the Same or Lower Cost to the Consumer**

The aircraft being used by the certificated carriers is, perhaps, one of the best reflections of the kind of service being provided. Since the war, $884,000,000 have been spent in the purchase of operating equipment and in buying and developing transport airplanes. Anyone who has reviewed the whole picture will see what is causing it. One carrier will buy a fleet of then-modern equipment. Soon, with technological advances, he will find that his competitors have acquired or improved aircraft to out-compete him. He then buys newer, faster, more economic aircraft. That has gone on in rapid succession until now with the new DC-7’s and Super-G Constellations, transcontinental non-stop service, is provided with aircraft specifically designed for that purpose. This is probably the most outstanding mark of service improvement in recent years. No doubt similar aircraft will be flying non-stop over any ocean and between any continents in the not too distant future. One airline (Capital) is about to institute operations with British-made turbo-props and another (American) has just announced a $65,000,000 purchase of new American-manufactured turbo-prop aircraft.

These improvements in equipment have brought greater traveling comfort and greater reliability to the public, in most instances at no greater cost. Notwithstanding the fact that every cost an airline pays has gone up markedly since 1946, the actual prices charged by the airlines, unlike most other businesses, have held steady and now are


\[^{15}\] For example, note the following CAB orders denying proposed mergers, acquisitions or consolidations: E-1418, E-4540, E-4617, E-4472, E-5205, E-5594 and E-8146.
going down. The price to the consumer for coach service, which constitutes about 37 per cent of the total service being offered today by certificated airlines, is set at a lower unit price than was being charged back in 1938.

The Airlines Have Not Enjoyed Excessive Profits

It really makes very little difference what measures are used to assess the bigness of air transportation; this alleged bigness is not reflected in the profits turned by the airlines or in their operating results over any respectable period of time. The United States certificated airline industry grossed over a billion dollars in 1954, to be sure, but that, large as it may appear, is but a recent development. In addition, that billion dollar figure is merely a gross income picture and not a proper portrayal of the industry’s earning capacity, even in one of its most profitable years. Against a total sales gross of $1,412,000,000 in 1954, the industry showed a profit of only $69,000,000, which was about 4.8 per cent of the total product sold.

The industry’s affirmative financial operating results for 1954 are not symptomatic of equally good results over a very substantial period. Not so long ago, in 1946, the domestic trunkline segment of the industry suffered a net loss after mail pay of almost $6,000,000.

By 1947 conditions had become even more serious; losses after mail pay amounted to $20,000,000. The earned surplus of the domestic trunklines fell from $58,600,000 on December 31, 1945, to $10,300,000 on December 31, 1947. Long-term debt increased from $24,400,000 or 16 per cent of the net worth of domestic trunklines to $161,700,000 or 90 per cent of their net worth. Several carriers formerly on a compensatory (or non-subsidy) mail rate basis were in so dangerous a financial position that emergency subsidy relief had to be granted in the form of increased temporary mail rates. A total of thirteen emergency mail rate orders were issued during the fiscal year 1947. The Board’s report to Congress indicated concern over the “precipitous” drop in net earnings of the industry. In the Board’s own words in its 1947 Annual Report:

“There followed, in the wake of these losses and changed capital structures, aggravated financial difficulties in the case of some carriers, resulting in petitions for higher mail rates, drastic retrenchment programs, cancellation of equipment orders, incurrence of large amounts of debt, and, in one instance, the sale of a route.”

So critical was the situation that the Civil Aeronautics Board instituted investigations of the operations, management and route structure of five of the domestic trunkline carriers. The purpose of this investigation was to determine whether there should be any major amputations in the industry (which the Board had just expanded so rapidly and so extensively) by elimination of routes or mergers or consolidations or otherwise.

It was not until 1949 that there was some improvement in the financial condition of the industry; but it was still not on a financially solid basis. The domestic trunklines in that year operated at a modest profit after mail pay but would have suffered a loss of $31,600,000 without mail pay.

The simple fact of the matter is that, up until recently, the over-all record of earnings of the domestic trunklines, the most profitable segment in the industry, has been poor. Were it not for mail payments in the years up until 1950, the record would have been abysmal.

Happily, the 1954 figures of net operating income and profit for the domestic trunk lines can be regarded as almost wholly without subsidy since, in 1954, the subsidy paid to the trunk lines amounted to only 4/10 of 1 per cent of their total revenues—or about $4,600,000 in subsidy of total revenues of over $980,000,000.

It may seem that the industry has settled down. It seemed this way in 1946 but, following that, came the airline recession. Even if the industry has settled down, it has some time to go before it finds recognition in the financial markets of the country, where financial results over ten-year periods are the criteria for judging stability.

An example of an expansion which may or may not be healthy is illustrated by the fact that, since 1951, the domestic trunkline industry alone has increased its usefulness to the public by 60 per cent, in terms of revenue passenger-miles flown. Yet the net operating income of the domestic trunk lines—the most profitable segment in the industry—in 1954 was substantially the same as it was in 1951. In other words, as figures 11 and 12 indicate, the industry has sold 60 per cent more of its product but has netted no additional profits.
The industry must accumulate some reserves out of its earnings. This applies equally to the big airlines as well as the smaller airlines. It has been conservatively estimated that in the next ten years no less than $1,750,000,000 will be needed for new capital expenditures; likely this figure will be anywhere from 30 to 50 per cent greater. That money will be needed for the following programs: substantial replacement of the reciprocating engine fleet with a turbo-prop fleet; the introduction of a specially designed cargo fleet or a major conversion of the existing fleet to cargo types; the addition to, and—to a limited extent—the replacement of, the existing fleet with the helicopter or a convertiplane; the addition of a substantial fleet of jet aircraft; major capital expenditures for accompanying ground, flight line and airways equipment and facilities.

Where is that money to come from, particularly in the light of the competitive nature of an industry for a common carrier market which is declining and which will be harder to penetrate? Certainly, equity funds will not be readily available if there is a continuing dilution of present markets, if the Board were inequitably to create a new class of carriers privileged only to drain the rich revenues from a few top traffic-production points, and if earnings are to stay at levels too low to attract this equity capital.

One of the best indices of stability and profitability, on a sound continuing basis, is the place airline securities hold today in the capital
markets of the country. Even after 17 years of regulated operation, airline securities are not attractive to the institutional investor, to whom, in large measure, the airlines will have to look for their financing. Basically, the standards of the institutional investor are established by law or by investment committees; and the airlines, as a result of their record of instability (measured by dividend payments, among other things), cannot today meet these standards.

The current Security and Industry Survey of Merrill Lynch, Pierce, Fenner & Beane (May, 1955) categorizes no airline securities as "investment type" or "liberal income" types, cites only two as "good quality," and classifies nine others as "speculative." In discussing market prospects for the airlines as "relatively favorable" for the future, the report has this to say:

"The outlook for the air transportation industry is less clouded, looking ahead to the summer months, than for a good many years past but despite this fact most airline securities must still be regarded as inherently speculative holdings. The reason for this lies largely with (1) the high leverage factor inherent in airline operations as reflected by the fact that relatively small shifts in the 'load factor' (number of available seats occupied) bring about wide variations in the profitability of operations; (2) the speed of technological developments which makes for relatively quick obsolescence of equipment and requires substantial capital investments at relatively short intervals."

If the industry had enjoyed excessive profits, analyses of this type would not be made. Even if industry earnings had been stable over any period of time, the problem of external financing, to meet its
REGULATED COMPETITION

needs, would not exist. The domestic trunk lines constitute the most profitable segment in the industry. The money they keep out of gross is particularly important in a business which has grown so quickly and in so short a period of time and has been constantly subjected to the vicissitudes of an inflationary spiral almost since its inception.

Most economic data in air transportation is measured from 1938, the date of the passage of the Act. Its greatest development, however, has been since 1946. Since 1938 general cost trends have had, as previously indicated, a significant effect on air transportation. At the outset, in order to compete in the travel market, the value of the product had to be held within the range of the then present and prospective consumer. With costs for supplies (soft goods and, to an even greater extent, durable goods), food, and labor rising—92 per cent in consumer goods and 128 per cent in average airline pay checks since 1938—the basic fares have remained at the same low stable level and, in fact, the yield to the industry is going down, due to the increasing amount of coach scheduling. Figures 13 and 14 show that by contrast with rail and bus fares, airlines have kept the price line stable since 1938.

These economic trends have been general in nature. They apply to air transportation as a part of the general industrial and marketing economy, just as they apply to steel, automobile production, rail transport, electric and gas utilities, and other fields of industrial enterprise. The significant fact is that in few, if any, areas have products—particularly the better product the airlines sell today—been available to the consumer in 1954 for substantially the same price as they were available to the consumer in 1938. As mentioned previously, one of the reasons for this was the necessity that air transportation, from the outset, be made available and attractive to consumers with a choice of

INDEXES OF AVERAGE PASSENGER-MILE RECEIPTS
COMMON CARRIER INTERCITY TRAFFIC 1938-1953
1938 = 100

![Chart showing indexes of average passenger-mile receipts for common carrier intercity traffic from 1938 to 1953. The chart includes lines for air, bus, and rail indices, with air showing a stable trend since 1938.]
transportation media in an effort to penetrate the travel market in both the business and vacation/pleasure fields.

These general economic trends have been up—in terms of things bought, wages paid, and state and federal taxes assessed—as the value of the dollar declined. Essentially, these cost trends are outside the control of the industry, but it must be emphasized that the upward spiral before and since the war has undoubtedly hit the air transport industry harder than other industries, as specific instances will reflect.

Measuring the air transport industry from the date of the initiation of its regulatory controls, there has been little opportunity since 1938 to develop any healthful financial reserves. This is partially true because of the way in which cost trends have affected the industry directly.

The key to the industry's inability to provide for the proverbial rainy day is the picture of its inability to finance reequipment programs out of depreciation reserves, surplus or, finally, a combination of these and equity money. Equipment is the single biggest element of fixed cost. Of course, no one would suggest that, in a technologically dynamic industry, depreciation should or could pay all the bill for progress. Unfortunately, though the industry has looked elsewhere for financing, equity dollars to pay for reequipment have been hard to find and, in more instances than have been healthy, it has been forced to borrow in order to purchase this new equipment. Equipment
is costing more each year, as witness the $2,000,000 DC-7's and Super-G Constellations contrasted with the relatively inexpensive DC-3 of pre-World War II years. Coincident with the acquisition of new aircraft, there is always the necessity to acquire new airborne electronic devices and modern up-to-date ground equipment, which also have been affected by the inflationary spiral.

From 1946 to 1954 the industry had an excess of capital expenditures over depreciation of $268,000,000, figure 15. That had to come from somewhere, either internally or externally. Internally, the most important source was retained earnings. Even that is misleading, since many of the companies had no retained earnings. Actually, even with all retained earnings added to depreciation, there was still a total of $100,000,000 over and above both of them, which had to be drawn from external sources. This total would have been larger if, over the years, the industry had paid out the dividends normal for a growing industry at about 40 per cent of net to its stockholders.

It is not true that this industry has enjoyed excessive profits, particularly if you look at its net income after taxes as a percentage of operating revenues contrasted with the railroads, electric utilities and even motor buses. The picture of air transport is a picture of instability and low earnings. This is readily apparent when you compare the basic nature of that instability of earnings of the five major airlines with other regulated industries—20 railroads, the Greyhound Corporation, and 20 operating electric utilities. The electric utilities are in the 15 per cent bracket which causes an investor, when he sees the kind of coverage they have, the kind of margin or drop they could
have and still be in the black, to appreciate the stability of that industry. This stability enables them to go into capital markets and finance their expansion at favorable rates.

Even the railroads and buslines are more stable than the airlines. Figure 16 shows that airlines were the only ones in the red in 1947 and, in 1951, had a 7½ per cent net income as a per cent of operating revenues. In 1954, with the biggest boom in air traffic, they were below the 5 per cent level. To the contrary, the railroads were at 7 per cent and the buses substantially at the level of the airlines—both in contracting phases of their business.

Another evidence of instability is the effect of passenger load factor on the trunk line's net operating income. Load factor is a figure employed to show the percentage of space profitably utilized against space available—or the percentage of the product sold. As grosses increase, the rise or fall of load factor has a greater and more unstable effect on net income. In 1954 a 1 per cent change in load factor—in either direction, up or down—would have meant a change of $14,000,000 in profits.

The air transportation industry is peculiarly susceptible to fluctuations in traffic and even relatively minor fluctuations can have a sharp effect on its earnings. In 1949 the first reasonably normal period of airline operations since the end of World War II, the 16 domestic trunkline carriers earned less than $14,000,000 after taxes and only $20,600,000 before taxes. A change of 1 per cent in the average passenger load factor of the trunkline carriers in 1949 would have decreased the operating income before taxes of these carriers a total of $6,400,000 for the year. A change of 3¼ per cent in the passenger load factor would have wiped out trunk line profits in 1949. A 3¼ per cent change in load factor, in 1949, amounted to an average of less than two passengers on a 57-passenger Constellation aircraft. This would have meant, in effect, that a traffic decrease representing, for the entire industry, the equivalent of less than two passengers per Constellation schedule would have wiped out trunk line profits in 1949.

The industry, regarded as an entity and in the light of low and unstable earnings, has not the hallmark of excessive profits traditionally characteristic of monopoly or concentration.

UNRESTRICTED FREEDOM OF ENTRY WILL HURT, NOT HELP, THE DEVELOPMENT OF UNITED STATES DOMESTIC, INTERNATIONAL AND TERRITORIAL AIR TRANSPORTATION

“Freedom of entry” is a term of some currency these days in arguments about the role and policies of the Civil Aeronautics Board in regulating the nation's airlines. Applicants for new routes frequently claim that so-called “freedom of entry” should be a feature of the airline industry, and complain incorrectly that the Board has followed an ill-advised “closed door” policy of not certificating new domestic trunk lines.
But "freedom of entry" is only a catchword invented to advance particular interests, who have no intention that it be given general applicability. In other words, what the exponents of so-called "freedom of entry" seek is just enough "freedom of entry" to get their own coveted route awards, limited to the most lucrative traffic centers—and then let the door close behind them.

The simple fact is that "freedom" does not mean "freedom" when used by the "freedom of entry" advocates. No one seriously advocates freedom of entry, in the sense the words would seem to imply: namely, that anyone could start airline service over any route at will. But if "freedom of entry" does not mean "freedom of entry," what does it mean? Some of its spokesmen have used various qualifying words to preserve the emotional appeal of "freedom of entry" while not actually advocating it at all. They have used such terms as "regulated freedom of entry," "greater freedom of entry," "reasonable freedom of entry," "some freedom of entry," "some degree of freedom of entry," "some limitation of freedom of entry," "considerable freedom of entry," and "not absolute freedom of entry."

In terms of specific routes, the qualified concept of "freedom of entry" becomes even more restrictive. In terms of the "coast-to-coast and New York-Chicago and New York-Miami" routes, the number of carriers to be accorded "freedom of entry" would not be "15 or 20 or 30 . . . or anything like that" but "a number much nearer three, maybe four, or possibly even two." Thus, this application of "freedom of entry" to the few principal traffic-producing routes would mean denial of entry to 95 per cent or more of the 55 non-scheduled operators holding letters of registration or exemptions.

Those who have advanced the doctrine of unrestricted "freedom of entry" are interested in one and only one phase of air transportation—and that is the long-haul market to and between only the top cities and the top traffic segments. A single most outstanding example has been the application of a non-scheduled airline combine now participating in four pending route cases, whose application covers service

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17 This is abundantly clear from the four months of hearings on S. 2647 (the McCarran Bill), which proposed a complete revision of the Civil Aeronautics Act, before the Senate Committee on Interstate and Foreign Commerce in 1954. When the Committee's staff searched the records of the hearing, it found frequent illusion to "freedom of entry" but could find no support for "complete abandonment of the system of certificates of public convenience and necessity and return to a system of free and unrestrained competition." Aviation Study for Senate Committee on Interstate and Foreign Commerce, Sen. Doc. No. 163, 83rd Cong., 2nd Sess. (1955), p. 54.

18 Large Irregular Carriers Investigation, Docket No. 5132 et al., Testimony of Robert R. Nathan, Transcript, p. 29002.

19 The Civil Aeronautics Board has exercised its exemption powers granted in section 416 of the Civil Aeronautics Act to establish a category of air carriers who operate without a certificate of public convenience and necessity. Some of them are styled large irregular carriers and are authorized to engage in irregular and non-scheduled air transportation by a letter of registration issued pursuant to part 291 of the Board's Economic Regulation. Others hold special exemptions granted by the Board authorizing irregular and non-scheduled transportation and are known as irregular transport carriers.
to 21 cities, every one of which is in the top 30 revenue-producing cities in the United States. As indicated before, it is these strong routes which support the operations of even the largest carriers to smaller cities. But this is only part of the story. These sponsors of so-called "freedom of entry," who seek favor from the Civil Aeronautics Board and sympathy from the Congress, have also kept away from short-haul transportation of any kind. This reflects the economic truth that even high-density short-haul routes have not been productive of profit.

It is axiomatic, in transportation, that the greater the trip length, the lower the cost to the carrier, and the greater its profit. The Civil Aeronautics Board submitted statistics to show comparative trip lengths for certain non-scheduled carriers as contrasted with the average of the 13 trunks. In 1953 the trunks averaged 547 miles against the irregulars 1667.

What this all boils down to is the fact that "freedom of entry" is not the banner of any ideological crusade. It is not a realistic concept for the airline industry. It is merely a catchword employed for the age-old purpose of clothing personal aggrandizement in raiment of broader appeal. The question of having, or not having, one more air carrier on a given route should be decided on the merits of that route, not on sentiment about "freedom of entry." Such a decision, on the facts of each particular proposal, is by law the Board's job, and should be handled by the Board exercising its judicial functions after full hearing.

A most effective way to illustrate the specious nature of this doctrine of "freedom of entry" is to imagine the situation which would doubtless result if there were no regulatory limitation on entry. In order to be equitably applied, it would have to be uniformly applied. On the day that concept was introduced, every airline would tear up its time tables, disregard its certificates, forget that it has franchise responsibilities and do what business it pleased in the interest of greater profits and not public convenience. Airlines who had filed applications for particular routes would just start flying those routes and not await Board action. Carriers who had sought for years to eliminate restrictions would just fly over the cities to which they have been restricted. The industry, in such a chaotic struggle for survival, would then have to abandon service to roughly some 500 of the cities to which it is now certificated, and operate only between the 50 most profitable pairs of points.

Acceptance of the "freedom of entry" thesis expounded in pending applications before the Civil Aeronautics Board, would be tantamount to urging the creation of one or a number of new systems, draining the rich juice of the air transport network from trunkline carriers who would continue to be forced to serve thin segments. This would create an extremely unfair and uneconomic competitive situation and
dislocate the country's air transport network. It would not represent any new or additional competitive opportunity, reflecting itself in public good, but only a chance for a favored few really to enjoy excessive profits.

CONCLUSION

The purpose of this review of the Act and the progress of certificated air transportation was to readjust the perspective of the competitive situation in air transportation today. It is necessary, always, to recognize that the Civil Aeronautics Act of 1938 intended air transportation to be regulated as a public service industry just like public utilities.

The increase in airline traffic is not a reasonable measure of the increase in airline profits. Busy telephones, stand-by counters, and personal inconveniences are not the indices of economic health; certainly they are not evidences of monopoly or concentration. Beyond that, they are not necessarily reasons for opening flood gates, the result of which might well be to engulf our present airline economy, over-expand competitive opportunity, unbalance systems carefully constructed, jeopardize future capital investment and the technological development which flows from it, and result in service patterns which reduce air service now provided to more people in more cities by more airlines than was ever imagined.

In 1954 there were 59 certificated airlines, compared with the 22 which existed in 1938. These airlines have served well the objectives of the Act of 1938 in creating an airline system which, today, is the most efficient, most useful and most competitive in the world. It serves our commerce, our postal system and our national defense. It is a foundation of both our prosperity and our security.