What Is It? Should We Have It? How Much?

Competition in the Airlines

Edward M. Kennedy, Albert V. Casey, M. Lamar Muse, Edwin I. Colodny, and John E. Robson

JOHN CHARLES DALY, former ABC News chief and moderator of the forum: This discussion concerns an issue first confronted in the Federal Aviation Act of 1938, which established the Civil Aeronautics Board (the CAB) to regulate America's fledgling airline industry.

Both the House and the Senate are now considering legislation to reform CAB regulation—not to deregulate the industry, but to ensure competition through relaxation of controls over fares, routes, entry into the industry, and so on. Both Democrats and Republicans on the Hill have sponsored reform legislation. President Carter and former President Ford support it, as does a broad array of public interest groups. In opposition are most major CAB-regulated airlines and their financial advisors, as well as the industry's organized labor.

Each of our panel members will state briefly his views on the issue and then we will have a general discussion. First, Senator Kennedy.

EDWARD M. KENNEDY, U.S. Senate (Democrat, Massachusetts): There is broad support for the efforts that many of us have made in the Congress to lessen government regulation of the airlines—bipartisan political support, airline industry support and, most important, support from American consumers.

We want to take the heavy hand of the federal government out of economic regulation of the airline industry, to permit the travelers of this country to pay lower fares, and so eventually to benefit the American consumer. We want to permit greater flexibility for innovative firms to compete in the airline industry. And we want to continue air service to the smaller communities that are entitled to it.

Our proposals will ensure a substantial saving to the traveler. They will provide a greater opportunity for more Americans to travel who cannot do so now because of high fares. We believe that these proposals will reduce the presence of the federal government in an area of regulation where it doesn't belong.

ALBERT V. CASEY, president, American Airlines: We're not really talking about deregulation, but about re-regulation, a different way to regulate the air transportation system. The most striking evidence of this is the fact that even the drafters of the current proposal acknowledge that a larger regulatory staff and a larger CAB budget would be required. It seems quite clear that those increases would be accompanied by an increase in subsidy payments.

In order to protect against undue concentration and to safeguard the public interest we need a regulatory system that provides the order and stability that are essential if the airlines are to make the enormous long-term capi-

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tal commitments and absorb the huge fixed operating costs required to provide public service. Over the last four decades, we have used regulation to build a safe, convenient, coordinated, and totally integrated system, second to none in the world.

I simply do not accept the argument that we have to encourage competition to a greater degree than at present. There has not been a society in the history of the world that has not had to regulate its transportation. Transportation is a *quasi*-public utility that does not enjoy the ability to build an inventory. Thus, it must have responsible price regulation in order to protect its huge capital investments in terminals and equipment.

M. LAMAR MUSE, president, Southwest Airlines: Southwest Airlines, an intrastate carrier, has operated for some six years in an environment entirely different from that which Mr. Casey refers to. We have done very well, not only for ourselves, but also for the consumers and the citizens of Texas. We have expanded our markets dramatically by instituting low fares on our routes, and I am convinced our experience proves clearly that competition and the free enterprise system are far preferable to regulation by any federal bureaucrat.

EDWIN I. COLODNY, president, Allegheny Airlines: It has been said that the existing statute is ambiguous. Well, so is the U.S. Constitution, and we have not thrown it out. We should not throw out regulation and substitute chaos, but we should come up with some meaningful modernization of the statute, which the consumers, the public, the government, the cities, and the communities can live with.

The problem most of us have in assessing the proper degree of change is that we are charting a course into the unknown. Basically, there is nothing wrong with the statute; the problem has been in its administration. Most of the objectives of the reformers—more competition in certain areas of the system and fare experimentation—can be achieved without the drastic legislative surgery Senator Kennedy and John Robson support.

JOHN ROBSON, former chairman of the Civil Aeronautics Board: Having just presided over the law that is the centerpiece of this discussion, I am in sharp disagreement with Messrs. Colodny and Casey. I say we should reduce the powers of the Civil Aeronautics Board in a way that will leave management freer of the regulatory hand. I have held that position for several years, and I continue to believe it is in the interest of the public, as well as of the carriers.

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Over the last four decades, we have used regulation to build a safe, convenient, coordinated, and totally integrated system, second to none in the world. —*Mr. Casey*

MR. DALY: Mr. Casey, what would happen to investment capital for the airlines if the proposed new legislation should be passed?

MR. CASEY: The most important thing would be to have *some* legislation passed so as to remove the present uncertainty. Right now, the cloud of re-regulation is hanging over the financial markets. At least 85 percent of the aircraft in the United States used to be financed by the "big five" insurance companies. Today, because of the uncertainty, these companies simply will not invest in the aircraft we need.

In the next eight years American Airlines will need $2.5 billion just to replace aircraft that are getting older and to procure new aircraft to handle the expanded market. We will need another $1.4 billion to cover the aircraft we will have to replace because of noise legislation. Right now, there is absolutely no way that American will be able to finance these aircraft, and yet we have one of the strongest balance sheets in the industry.

MR. ROBSON: In American's in-flight magazine, which I happened to read as a customer recently, an article makes the point that only once in the last twenty-five years has the airline industry earned the 12 percent rate of return that is now allowed by the CAB. In recent testimony, one of the deans of the insurance company airline lenders said that the financial results of the airline industry have not been acceptable for the past twenty years. From 1969 to about 1975 not a nickel of private investment went into the airlines, except for a few carriers, because the airlines were in lousy financial condition. Most of the money now loaned and invested in the U.S. economy goes to businesses that are not regulated. Nothing in the financial history of the airline industry is worth shouting hosanna about. It's about time we changed that and tried to help the airlines help themselves.

MR. COLODNY: I do not disagree that the CAB has been niggardly in allowing adequate fare increases. But the cure proposed may, unfortunately, be worse than the disease, because the opportunity to earn adequate levels of profits under the proposed system may be available only to a very few larger airlines. One of the tremendous potential threats to U.S. cities is the concentration in a few carriers that will result under the proposed legislation.

Moreover, the CAB has not had an adequate fare policy. But that could be dealt with under the present law by appointing people to the board who feel that airlines are entitled to fair profits.

MR. MUSE: One comment of Ed Colodny's identifies the crux of the entire problem—the idea that the CAB has been niggardly about granting fare increases and so has prevented the airlines from making a reasonable profit. That is the thinking of the management of this entire regulated industry and of the CAB. But at Southwest, we are convinced that the way to make money in this business is to *lower* fares, not to *raise* them.

MR. DALY: Senator Kennedy, would you describe the main elements of your bill?

SENATOR KENNEDY: Basically we want to permit the greatest flexibility for downward adjustment in fares—to allow the industry itself to make the business judgments permitting a dramatic reduction of fares. Under the current proposal, airlines would be free to lower their fares 35 to 55 percent without government interference. This would provide a reasonable opportunity for the kind of travel incentives offered by Mr. Muse's airline in the southwestern United States, as well as by the new airlines in Florida.

The proposal would also provide for the entry of existing airlines into existing routes, while allowing qualified new carriers to move into routes as well.

In addition, there would be important guarantees of continued protection for smaller communities. One third of all the communities in this country have, over the past fifteen years, lost the service of CAB-regulated carriers. About two thirds have been picked up by smaller commuter carriers, which are not regulated. They think that they can profit—and they are not subsidized. It is very important for the American consumer to understand that, under our present system, the smaller communities may continue to lose service. The proposed legislation attempts to prevent that.

MR. COLODNY: According to Senator Kennedy, the proposal will hurt nobody and help everybody; but let's analyze some of the issues. First, let's talk about the question of fares. A recent survey published in *U.S. News & World Report* indicated that, of all industries in this country, the airlines are rated at the top in giving good value for the money.

Second, let's talk about the abandonment of cities. Between 1962 and 1976, half of the 157 deletions in local air service occurred in cities that generated fewer than five passengers a day. A quarter involved cities that are now being served by commuter carriers, just as Senator Kennedy favors. The remaining cities have alternative service, either at nearby airports or by codesignation with other points.

This country has spent $42 billion developing an interstate highway system that changed the pattern of air travel as no other expenditure ever has. It has made some airports obsolete. To claim that abandonment of those places indicates something wrong with the law is a misconception.

MR. CASEY: Of the million things I would like to mention, let me bring up just a couple. For one, I have sat through hours of discussion without hearing either the congressional staffs or the airlines devote five minutes to the extra energy that will be expended if we have additional competition. It is quite realistic to say that the airlines of the United States would expend at least 1 *billion* additional gallons of fuel in the first year of any form of free competition. That fuel, if used in home heating furnaces, would heat the states of Maine, New Hampshire, Vermont, and Rhode Island for a year.

Second, there is talk about lower fares. Senator Kennedy mentions reductions of 40 to 50 percent. We have already lowered some of them by that much. Our super-saver fare is 45 percent below the normal fare, and no new regulation was needed for us to do that.

Another point: the other day we asked our board to authorize a new lease in one of our major cities—a $46 million, twenty-year lease. The members of the board objected. They asked why we should sign that lease unless we knew we'd be in that city and knew what form deregulation would take. Yet, if the airlines do not sign such leases, there is no way the airports can finance improvements.

MR. ROBSON: Mr. Casey, I would like to know what happened to the Al Casey of April 1977 who said in his Senate testimony that he did not fear the effects of competition—that, quite the contrary, he was a firm believer in competition. The point that you make about waste in competition is one that is perpetually made by the people in your industry, and it is wrong. It is wrong because it assumes that everybody in the airline business is a damned fool.

Let me carry this further. There are thousands of street corners in America. And on those street corners there are gas stations, drug stores, groceries, and all kinds of other enterprises that nobody needs government permission to set up. Now, the fact that people can set up a drug store on a corner does not mean that they will. They'll do so only if they think it makes business sense. And in some cases they'll guess wrong, in others they'll guess right. Just because the opportunity exists does not mean that carriers will pursue suicidal paths.

MR. CASEY: John, I accept the criticism, but you didn't finish what I said after that line in my testimony that you referred to.

MR. ROBSON: You said you thought the airline business is competitive.

MR. CASEY: You bet your life, and I went on to explain competition.

MR. COLODNY: Let's be sure we understand two facts that have not been discussed.

First, while some U.S. markets undoubtedly would get lower air fares under any bill that Congress passes, a large number of them would get higher fares. That is because the thrust of this legislation is to eliminate a national pricing system and to go to what is essentially a system without cross-subsidization. That has been the heart of the debate.

The airlines system today is essentially cross-subsidized in many different forms. Because fares are distance-related rather than density-related, many markets in this country would have higher fares if the present system were abandoned. There would not be adequate profits from those markets to make up for the slicing off of the heavier profits from the larger markets.

Second, there is a need for more competition in the system. There have been many instances, over the last ten years, of monopoly routes where the CAB could—and should—have awarded competitive authority. The industry in general and the regional carriers in particular are not opposed to competition. The issue is whether the kind of competition being proposed will bring lower fares. It will not for a large part of the system—only a piece of it.

Competition is not putting another carrier in a monopoly route against a monopoly carrier. Competition has to do with P-R-I-C-E. —*Mr. Muse*

MR. MUSE: The first thing is to define *competition.* Competition is not putting another carrier in a monopoly route against a monopoly carrier. Competition has to do with *P-R-I-C-E.*

Mr. Casey mentioned the waste of a billion gallons of fuel during the first year of deregulation. That could only be true if, as Mr. Robson indicated, everybody in management in the airline industry were absolutely stupid. No airline would enter a market with the same prices as the two or three carriers already in it. If it did, the market would only be divided among four carriers, say, rather than three, and they would all lose money and burn lots more fuel for nothing. Common sense tells us that if a carrier were going to enter a market, it would have to provide a service that would vastly expand that market, as we have done in Texas.

Another point on fuel is this: competition can provide a greater saving of our fossil fuel resources than anything that the government has come up with yet, including the taxing of crude oil. To drive a car along any of the routes we serve in Texas—which average about 250 miles—would require twenty gallons of fuel. We fly a seat in any of those markets for six and one-half gallons of fuel. This means that thirteen and one-half gallons of fuel are saved for every passenger taken off the interstate highways and put into a Southwest airplane. And we have taken them off by the millions.

SENATOR KENNEDY: We have heard the argument for years that labor is cheaper for some of the intrastate carriers. The fact is that the low-fare intrastate airlines are organized by the same national unions that have organized the federally regulated airlines. The pilots and mechanics get the same wages.

We hear about competitive super-saver fares being offered now by American Airlines. That means a passenger has to leave on a Friday, the twenty-first of the month, wear a green tie, fly back three weeks from the following Sunday, and meet all kinds of other conditions.

We hear the questions about extra energy, about the big jets. In the two years of study by our Senate committee, we found that the intrastates are flying, in most instances, the same planes as the regulated carriers—and they are putting more people in them at lower cost.

Pacific Southwest Airlines, or PSA, a California intrastate line, flies the Boeing 727 at a configuration of 158 seats, and it carries at 60 percent of capacity. The same airframe used by American Airlines has 121 seats and travels at 55 percent. That is a basic difference. With more seats and more passengers in them, price can be lower and more people can fly.

Under our proposal, we would have more savings in oil and gas, as well as more people flying because flying would be cheaper. As we have seen in our hearings, competition now focuses on sirloin steaks, on how flight attendants are dressed, or on what movies are shown.

MR. DALY: Are you speaking about lifting price restrictions entirely, or within some range?

SENATOR KENNEDY: It would be within a range. I think the legislation will allow reductions of about 35 to 55 percent and increases of from 5 to 10 percent without federal regulation. Reductions of 10 to 15 percent will not accomplish anything. We have to permit the kind of dramatic price competition that Lamar Muse created—the kind that we see in California. The intrastate flight between San Diego and San Francisco, 456 miles, costs $32, but the interstate flight between Boston and Washington, 399 miles, costs $56. Dallas to San Antonio, under CAB-regulated fares, costs $41, but intrastate fares are anywhere from $25 to $15. Miami to Orlando, under the CAB fare, costs $36, but intrastate, it costs $18. That's the same distance as from Boston to New York, which costs $37. The intrastate is charging half the CAB price.

That much difference in price amounts to a subsidy. Why didn't the airlines say that to our congressional committees, so that the consumers of this country would understand who is subsidizing whom. During the course of two years of hearings, the airlines argued that these high fares are used to pay for money-losing flights to small communities—the cross-subsidy argument. When we asked the airlines to tell us which routes were subsidizing which others, we got no credible answers whatsoever. We sent economic analysts and investigators to go over the books of a number of the airlines, and they could not find any significant cross-subsidy.

If Allegheny is subsidizing a certain route, let's find out who is paying for it. Consumers are entitled to know whether they are paying extra to fund service to Pocatello, Idaho—and if so, is that the cheapest, most efficient, and most effective way of providing the service? Perhaps we should be using some other means. In the proposed legislation, we use *direct* subsidies, which have clearly been shown to be a more efficient and vastly less expensive way to subsidize transportation to isolated or small communities.

MR. CASEY: You give us no credit whatever for the fact that the planes confined to the intrastate markets carry no food services. Those planes only have to go 250–300 miles, whereas ours have to provide full transcontinental service. The food costs us about $4—about 2 percent of the cost of the ticket.

SENATOR KENNEDY: We rest our case not just with the studies; we rest it with Lamar Muse, with PSA, with Air Florida, with Air California, with the new applications that have been made at Midway, and with all who want to cut back prices. I am not talking just about academic testimony and other reports but also about the fact that millions of passengers get safe, convenient jet air service at half the regular price.

MR. ROBSON: The reason why I have come to believe—and why the Civil Aeronautics Board itself has recommended—that the law should be changed is that there is no incentive under the present system for price competition. It is very simple. There are two guys on the block, and nobody else can play in the sandlot without going through agonies at the CAB. Why should these two guys spoil a good thing by competing against each other on price? But each one is interested in getting a bigger share of the market, so he runs more airplanes—which, as both Mr. Colodny and Mr. Casey can tell us, is expensive—or he feeds his customers better, or does other things for them.

The game needs to be opened up so that the spur of competition can work. The fact that Lamar Muse and others have done it is evidence that it can be done.

MR. COLODNY: In most instances, public complaints are not about the price of air travel but about the lack of adequate schedules and service. And those who complain are willing to pay for better service—particularly the business community, which is the backbone of so much of the system and is essential to the dispersion of industry to smaller communities.

Only thirty-two markets in this country generate over 1,000 passengers a day. These are the markets that have the potential for a large increase in traffic with sharp price-cutting. The question is, how can this price-cutting be accomplished without jeopardizing adequate service to the medium-sized markets? The proponents of reform really propose to increase drastically the size of the government subsidies—by laying down standards that would make it impossible to deny service to practically any city that wanted it. And that would swamp the CAB with regulatory problems.

Nineteen cents of every revenue dollar pays for fuel and forty-five cents for wages and salaries. The fixed charges in airport facilities and the costs of noise regulation, which are starting to inhibit the system further, all increase the noncontrollable costs. The alternative is to pack more passengers into the airplane, in cases where the market responds to lower fares. We have shown this can be done in certain markets. But that is not the issue. The issue is how to realize substantial savings in cost without drastically reducing service to low-density points or increasing significantly the subsidy burden.

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MR. DALY: Mr. Robson, what about the argument that reform would mean higher unemployment, more job dislocations, and poorer working conditions for airline employees?

MR. ROBSON: I just don't think that is true. Those who have seriously studied the issue believe that regulatory reform will expand the market for air travel and increase the number of jobs. As for protection of employees, they have no protection now except in the case of a merger between two airlines. Such protections as they have are those they have bargained for with their own managements. Nobody is proposing to tamper with those protections or to interfere with bargaining rights.

MR. DALY: Why, then, is labor opposed?

MR. COLODNY: These people are concerned that overall wage levels would be debased, as they were in Texas by cut-rate labor. I am not saying that is bad, but that is what the working man is concerned about—that his job will go to somebody else, that there will be undercutting from new employees. We could go out on the street today and hire pilots at the same wages Mr. Muse pays, if we wanted to overlook our pilot agreements. But our agreements provide long-term stability for employees.

MR. MUSE: Concerning the cost components Mr. Colodny mentioned—fuel, salaries, and so forth—we pay 36.5 cents per gallon for fuel; Mr. Casey said, before the program began, that he pays only 28 cents. My pilots start out the first year, as first officers, at $800 a month. On Allegheny, they start at $750. My captains, as of July 1, 1977, earn $57,000 a year. If Mr. Colodny pays his more than that, he's a damn fool.

My facilities are just as expensive as his, but I get more productivity out of them. I get 28,000 passengers per month through a gate lounge. At the Dallas-Fort Worth Airport, American gets an average of 9,000. In San Antonio, last month, we handled 26,000 passengers through one gate, while Braniff handled 27,000 passengers through four gates. As to landing fees, we pay half as much at Love Field as Mr. Casey does at Dallas-Fort Worth, but at Hobby Airport in Houston we pay 150 percent more than he does at Houston's Intercontinental Airport.

MR. DALY: I assume the panel agrees that safety is the responsibility of the FAA, or Federal Aviation Administration, and is not—

MR. CASEY: I would not agree. Managements have imposed far tougher standards on retraining and on redundancy of equipment than the FAA ever has. There are many, many standards—on rest periods and other matters—that have been the decision of management. Safety is dependent upon management's ability to operate a strict maintenance program, to provide thorough training, and so forth. Safety is a matter of management commitment.

MR. DALY: Now that we have opened up every basic area that needs discussion, it is time to turn to the audience gathered here for questions.

WHITNEY DEBEVOISE, Harvard Law School: Mr. Casey, without getting into the details, I would like to know how it is that, in an industry you say is highly competitive, there is anything left over to subsidize the local routes?

MR. CASEY: I shall try to answer your question with an example. We subsidize the San Diego-Los Angeles passenger by carrying him for about $12, which is less than our fully allocated cost. The reason we do it is to feed our transcontinental and semi-transcontinental services out of Los Angeles to Chicago and New York—services that are currently profitable. If deregulation comes to pass, those transcontinental and semi-transcontinental services may no longer be profitable. In that case, it wouldn't make sense to subsidize a San Diego-Los Angeles passenger in order to put him on another unprofitable flight.

MARVIN GRISWOLD, Airline Division, International Brotherhood of Teamsters, Chauffeurs, Warehousemen & Helpers: Senator Kennedy, are you, in effect, asking the American taxpayer to subsidize the traveling public by paying the increased costs of the labor-protective provision of this bill and of service to the small communities?

SENATOR KENNEDY: First of all, there are no labor-protective provisions in the bill at the present time, and I think it is an open question whether there will be. The real issue, and a very tough one, is how to protect people's jobs against poor management decisions—no matter whether they are fishermen off the coast of Massachusetts or workers in machine tool companies, shoe companies, or other kinds of companies.

I am completely satisfied that our program would permit greater flexibility in fares and entry and would bring a dramatic expansion in air travel and, with that, an expansion in work and employment opportunities. A number of airlines understand that, and they and their workers are supporting the bill.

As for subsidies, during this past year the airlines received approximately $74 million. The initial projected subsidy under the Kennedy-Cannon bill is $15 million. That amount would vary depending upon the number of the communities to be protected. Basically, the legislation gives smaller communities a service guarantee that they do not have at present. I see no additional expense under the legislation—and rather dramatic savings. The estimated fare savings from more competition range from $1 billion to $3.5 billion annually, so even if direct federal subsidies were to increase to $100 million annually, the benefits would outweigh the costs.

MR. COLODNY: This legislation has something called market exit, as well as market entry. The provisions for exit would permit any carrier to leave any market on 90 days' notice if no one objects and a maximum of 180 days' notice if the carrier is losing money. If we have a provision for entry, we have to allow exit, because that is part of the philosophy of this movement. The point is that labor-protective provisions cannot be imposed to guarantee jobs for services that may have to be dropped. It could not be done without further compounding the economic problems of the industry.

MR. ROBSON: That comment suggests that there would be a great deal of exit, and I think that is very debatable. The fact is that, over the past twenty years, the CAB has already let the airlines drop virtually all the routes they wanted to drop. Lord knows, Ed Colodny's airline, Allegheny, has exited from more places than any other. In most cases, Allegheny has had a commuter airline provide the service that was previously subsidized. The commuter service is more frequent and better timed, and its traffic has grown over 100 percent, if my memory serves me correctly. And the taxpayers aren't paying a farthing for it.

MR. COLODNY: I agree that Allegheny has done a lot of pioneering in providing small-city service, but it has been done under the present statute. The statute permits the replacement of service under CAB oversight. This guarantees the community a level of service at least as good as, and most times far superior to, what larger equipment can provide.

Going back to something Al Casey said earlier, the future of the airline industry depends on the ability to finance new-technology aircraft in order to continue productivity gains. We cannot stay with the present generation of aircraft indefinitely. We can prolong the situation, but we are already paying a price for that—in fuel efficiency and in other technological advances.

The industry will have to husband its resources and do things differently, because there is now an unknown factor. I defy anybody here to predict what will happen under this bill.

MR. ROBSON: Most of the money in this country is loaned to, or invested in, businesses that are not regulated, and I don't know why that cannot be the case for the airline industry. Regulation is not like a respirator that supports the system as if it were a patient on the table. If the hand of the CAB were cut from the neck of the airlines, they would not expire.

Regulation is not like a respirator that supports the system as if it were a patient on the table. If the hand of the CAB were cut from the neck of the airlines, they would not expire. —*Mr. Robson*

MR. COLODNY: The heart of the problem is the stability of the route system, which is hard to deal with.

MR. ROBSON: Do we make people buy airplane tickets?

MR. COLODNY: The government does nothing to create sales, but it can inhibit sales. The government creates balances in many different fields. I have noticed a tremendous push in Congress to increase maritime subsidies in the movement of oil. That would cost the American consumers far more than any saving we are discussing here in connection with airline fares.

MR. ROBSON: Well, there are probably all sorts of policy disasters that are costing a lot of people a lot of money.

MR. COLODNY: One other point. The airlines could be moved to the unregulated sector of the economy—but that sector has had smaller productivity gains and larger price increases than the airlines have had under the present statute.

MR. ROBSON: What happened in the airline industry was that in 1959 or 1960 it was handed one of the greatest technological breakthroughs that ever happened in any industry—the jet airplane. But unlike the transistor, which dramatically reduced prices in electronics, the jet did not appreciably reduce normal air fares. The productivity gains were dissipated, fundamentally, through overscheduling. Neither the investors nor the consumers received the benefit that they should have had from those productivity gains. In the past few years, productivity in the airline industry has lagged behind general productivity in the country.

MR. COLODNY: That is absolutely right. However, it has been lagging, not because of CAB regulation, but because this economy, as a whole, has been in a serious situation.

REUBEN ROBERTSON, Public Citizens Litigation Group: I have two questions for Mr. Casey.

First, have you been able to raise new financing for expansion during the period of debate on this legislation? Second, if the Kennedy-Cannon bill were passed in substantially its present form, do you think that American Airlines could survive, or even expand?

MR. CASEY: On your first question, yes, we were able to raise money this spring. We did it by going to forty-three small insurance companies, rather than to the large ones. We showed a little more innovation and sold preferred stock with a warrant attached to it—which just happened to suit the marketplace.

American Airlines has been in the unique situation of having had a very favorable fuel contract and, partly for this reason, will make a lot of money this year. That benefit runs out on September 1, so our results for the rest of the year will reflect much higher fuel expenses.

Will American make out all right if it is deregulated? You can bet your life we will. American Airlines will whip Allegheny. They are the first ones we are going after. They are the most vulnerable.

MR. COLODNY: Unfortunately, Mr. Casey knows more about his plans than I do, but what he is saying in jest is part of the problem. Some carriers have very significant resources. American is one, along with United, Delta, and Northwest—all of whom have low debt, high equity, and strong cash positions. This is part of the key issue of concentration raised by the proposed legislation. I would write legislation that kept American, United, Northwest, and Delta from getting a single new route mile for at least five years—for the very reason that Mr. Casey has mentioned. Those carriers have the resources to redistribute traffic flow in this country; they have the resources to whomp an Allegheny, a TWA, or anybody they want. I know Mr. Casey is a reasonable man. But I don't want the legislation to be written so that I may find out otherwise in the real world.

TIM ENGLE, American Conservative Union: Mr. Muse, your situation in Texas has been described as unique and not applicable throughout the country. Do you disagree?

MR. MUSE: Yes, sir, I certainly do. That's the excuse people use to rationalize our phenomenal success. When we served only Dallas-Houston and Dallas-San Antonio, we were told these were large high-frequency markets and that we could not succeed in a smaller market. Since then, we have gone to the Rio Grande Valley and have increased the traffic there from 123,000 passengers in 1974 to 500,000 in 1976. It is no longer a small market; we have generated new traffic with low fares.

As of June 1977, we are serving three new cities: Corpus Christi, Midland-Odessa, and Lubbock in Texas. The boardings from those three airports in June 1977, as compared with June 1976, were up an average of 47 percent—with Corpus up 45.5 percent, Lubbock up 47.5 percent, and Midland-Odessa up 48.6 percent. In each of these cities there are at least three carriers—Southwest plus two CAB carriers.

As to other parts of the country, our confidence is very high. We have applied to the Civil Aeronautics Board for authority to serve fourteen commuter-type markets out of Midway Airport in Chicago, to such cities as Detroit, Buffalo, Cleveland, Columbus, Dayton, Cincinnati, Pittsburgh, St. Louis, Kansas City, Minneapolis, Omaha, and Des Moines—cities more than 200 miles and less than 500 miles from Chicago. The CAB has pretty well emasculated our application. Before even holding a hearing, it has limited its consideration to the six largest markets, which tells us something about current protection of the smaller markets.

MR. DALY: Mr. Muse, before we leave this area of intrastate carriers, tell us about the Texas

Aeronautic Commission which supervises the Texas carriers. How similar is it to the CAB?

MR. MUSE: In many respects, it is very similar. The difference is that the Texas commissioners are convinced that we know more about running an airline than they do, and they let us run our airline.

MR. ROBSON: I quite agree. I think that the problem with regulation is that we intrude into every major decision the airlines make. We tell them where they can sell their product and what they can charge for it. There isn't much left for Al and Ed to do during the day.

ALAN BOCK, *Libertarian Advocate:* What would you say to the contention that if the CAB was ever really necessary, it is necessary no longer, and that the time has come to abolish it? I would envision doing this gradually.

MR. ROBSON: Those of us who support airline regulatory reform would not argue the basic point that times have changed. The need for regulation, if there was that need back in 1938, is no longer with us, and the law ought to be changed to meet the new environment.

SENATOR KENNEDY: I start out with the fundamental view that in areas of economic regulation the federal government ought to have a substantially reduced presence. In the field of drugs or medical devices, there has to be some kind of unit to ensure adequate protection for the American consumer. But there should be a substantial reduction of the federal presence in the airlines. The proposal before the Senate is probably the strongest effort we could make that has a reasonable chance of success. It is also sensitive to the need for a period of transition.

As for the threat that American would chew up Allegheny, there is a point I should have made earlier. The economics of the industry show that small carriers are usually quite effective competitors. Nevertheless, we have included in our proposal a certain temporary advantage for the smaller airline companies by permitting and encouraging them to move in on the majors. Rather than Mr. Casey chewing up Mr. Colodny, Mr. Colodny might breathe down on Mr. Casey.

Also, we in the Congress have to be more sensitive—as we see a reduction of the federal presence in economic regulation—to enforcement of antitrust policy and protection against predatory practices.

MR. CASEY: Many committees, including yours and Senator Cannon's, have said there are no economies of scale in the airline business. So why do you pick on the big fellows?

MR. COLODNY: The issue rests on a social decision. What kind of a system do we want to gamble with? We know what we have today. Our present system is not perfect and needs procedural reforms. Maybe faster fare increases, in some instances, are justified. On the other hand, Mr. Muse, I doubt if you have raised any of your fares since you started up.

MR. MUSE: That's correct.

MR. COLODNY: And I assume you are willing to pledge yourself not to raise them, period.

MR. MUSE: Not at all.

MR. COLODNY: I didn't think so. But the other side of the coin is that the airlines have provided many different kinds of fare reductions, albeit not necessarily the same as Lamar Muse has provided. In any event, the issue before the country on this legislation is the degree of risk to take.

WILLIAM JORDAN, York University, Canada: Mr. Muse, with changes in regulation, productivity will be very important. Can you tell us how you achieve increased productivity?

MR. MUSE: Through volume, and we get volume through low prices. We create demand in all of our markets. Mr. Colodny says that the bulk of air travel is business travel. That's true on Allegheny—95 percent of it probably is. But business travel on Southwest only represents 46 percent of our volume. The other 54 percent is due to the very low fares. It is personal travel—emergencies, entertainment, or whatever.

MR. DALY: Would you explain, Mr. Muse, your two-tier fare system?

MR. MUSE: We have what we call executive-class flights Monday through Friday, 6:30 a.m. to 6:59 p.m. All other Monday through Friday flights and all Saturday and Sunday flights, when the working man or woman can travel, are what we call pleasure-class flights. They cost approximately 40 percent less than the executive-class flights, and the executive-class flights are priced approximately 40 percent below equivalent CAB fares.

FRANK WALDNER, International Association of Machinists and Aerospace Workers: I want to emphasize that the union I work for and all the other responsible unions in the industry are not opposed to responsible regulatory reform. But we are flatly opposed to the current proposal. It is an unnecessary step and will create havoc in the industry.

In regard to labor-protective provisions, we feel they must be incorporated if Congress really intends to proceed in the fashion now envisioned by Senator Kennedy. Do you, senator, share the views of former Chairman Robson that labor-protective provisions are unnecessary?

SENATOR KENNEDY: When this legislation was being fashioned, we tried to work with the Machinists, but they said they opposed it and would not make any recommendations. That has also been the position of some of the other groups affected by it. I would be more than glad to look at any recommendation or suggestion.

On the question of jobs, I believe there will be numerous opportunities for employment in expanded services. A number of workers were thrown out of work in New Bedford, Springfield, Fall River, and throughout New England when the major regulated airlines abandoned those communities. One third of those airports have been abandoned over the last fifteen years. I know those families, and there were no protections for them. They are not guaranteed protection under the present system. Moreover, I see that numbers of people in communities that had high unemployment are now working for the smaller commuters, and providing for their families.

DONALD FARMER, Antitrust Division, Department of Justice: Mr. Casey, why do you believe an unregulated airline system would be unduly concentrated when, as you said a moment ago, larger airlines do not have lower unit costs?

MR. CASEY: What I meant by that, sir, was that large carriers with financial muscle would have the ability to round out their route systems. For example, we could back up a Cleveland or an Indianapolis with many more support towns than we have right now. So, the big could get bigger. We would have the financial strength to stay in there and take a beating for two or three years, and it probably takes that long to develop a market. And we would have the superior management skills to identify the profitable markets.

MR. ROBSON: American has spent the last ten to fifteen years getting out of small markets, standardizing its equipment to fly in larger markets, and tailoring its marketing to that system. It strikes me as very unlikely that it would suddenly turn the clock back and go the other way. It is a lot more likely that Ed Colodny and some others would peck away at some of American's trees.

MR. CASEY: What we would do is cancel some of the marginal services that are unproductive and substitute services in areas where we have better opportunities to create traffic flows. We would not redirect the whole airline.

MR. ROBSON: It is interesting, too, that the greatest growth and the least concentration has occurred in the commuter industry, which is, essentially, unregulated.

MR. COLODNY: What is not generally recognized is that American and other large airlines sit on massive, dormant route authorities [certificates to fly specific routes], which can be reactivated without any change in the statute. Under deregulation, another large airline could gain access to a market and redirect the flow of traffic to a gateway to feed a DC-10, in competition with some other large airline, and the market would be reshaped.

MR. ROBSON: Is an air traveler hurt by that?

MR. COLODNY: Not necessarily, but how many airlines do we want in this country? Do we want a few large ones or do we want to have more?

MR. ROBSON: After forty years of regulation, we have fewer trunk carriers, fewer local-service carriers, and fewer supplemental carriers than we had when we started.

MR. MUSE: Mr. Colodny said that opening up the system so that carriers could begin utilizing the dormant authorities of other carriers would reshape the industry. If a carrier has dormant authorities, we have to assume it's because they aren't worth a damn. Why would a new carrier pick up and operate a worthless authority?

CHARLES WOOD, staff of Senator John C. Danforth (Republican, Missouri): Senator Kennedy, why do your bill's automatic entry provisions discriminate against the Big Five airlines, despite the relatively weak financial condition of some of them?

SENATOR KENNEDY: The entry provisions are tilted toward the smaller carriers to encourage them to expand, if that should be their desire. The purpose is to add to the forces of competition. The existing route system of the five majors is strong enough to withstand what moderate competition the new legislation would present.

MR. DALY: This concludes our discussion. On behalf of AEI, heartfelt thanks to our distinguished panelists and to our guests. ■

Based on an AEI Round Table held on July 12, 1977. For the full, edited transcript, see *Competition in the Airlines: What Is the Public Interest?* (AEI Forum 9), Washington, D.C.: American Enterprise Institute, 1977.

Lawn Mowers, Matchbooks, and Glass

(Continued from page 10)

located on the back cover of the matchbook; a requirement that matches self-extinguish within fifteen seconds of lighting; and finally, the most controversial requirement, a "latching device" to limit access by children.

After almost a year of deliberation, the CPSC decided to implement only the quality control and reverse-friction requirements. Since the quality control requirement is relatively easy for matchbook producers to meet, and since the industry has voluntarily switched to reverse friction, the costs of meeting the new standard will be minimal. Also, there is general agreement that these provisions will be helpful in reducing matchbook accidents. However, there was little hard evidence of significant benefits from the other two provisions of the initial standard. In fact, the Council on Wage and Price Stability suggested that the latching device—which alone would have increased the cost of producing matchbooks some 68 percent—might pose an interesting challenge to children, fostering further match-related injuries.

(3) In a somewhat less noticed—but extremely important—ruling of January 6, 1977, the CPSC promulgated a standard for architectual glazing materials. This standard requires that, in order to minimize the risk of injury, glass doors and similar fixtures posing potential hazards to occupants of buildings meet impact tests in which the glass either does not break or breaks into very small pieces.

This is the first nationwide building standard issued by the CPSC, and it preempts certain state and local regulations. The industry now is required to meet one uniform rule instead of numerous local laws, thereby permitting standardized production. For this reason the proposal garnered considerable industry support when it was under consideration.

In 1973 the products covered by this standard were responsible for an estimated 74,000 injuries. Most involved minor lacerations and only about 2 percent required hospitalization. Though this makes the monetary valuation of expected benefits very difficult, the Council on Wage and Price Stability tentatively estimates the present value of the future stream of benefits at around $5 million (roughly $500,000 per year discounted at 10 percent over the—average thirty-three year—life of the glass).

As for the costs of the standard, the CPSC relied upon an estimate from Batelle Columbus Laboratories that put additional construction costs (residential and nonresidential) at $45 million to $62 million—and implied a $30 to $50 increase per housing start. This sizable gap between calculated costs and benefits, if not narrowed by the advantages of standardized production, raises significant questions about the standard; if nothing else, it suggests the CPSC should have had more justification for its action than has yet been presented.