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GULF AIRLINES AND THE CHANGING MAP OF GLOBAL AVIATION

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Introduction

This report provides an empirical case study of one of the areas in which the Gulf States have been the most visible and dynamic generators of global change: the aviation sector.

- The startling rise of Emirates, Etihad, and Qatar Airways has reshaped global aviation markets around the three hubs of Dubai, Abu Dhabi, and Doha as the Gulf airlines have developed into what the *Economist* magazine has labelled "global super-connectors" capable of connecting any two points in the world with one stopover in the Gulf.[1]
- This culminated in the January 2015 announcement that Dubai International Airport had overtaken London's Heathrow Airport to become the world's busiest airport for international passengers. Significantly, the 6 percent annual rise in Dubai's international passengers (to almost 70 million in 2014) contrasted with the far smaller rate of increase caused by Heathrow operating at near-peak capacity owing to space and regulatory constraints.
- Moreover, Emirates, Etihad, and Qatar Airways have benefited further from the relative absence of political or legal constraints compared with European and North American "legacy carriers" in addition to "state capitalist" models of political and economic development.[2]

A brief overview of aviation in the Gulf constitutes the opening section in this report and illustrates how, for much of the 20th century, Kuwait, Bahrain, and (briefly) Sharjah led the Gulf in aviation, with Qatar and the United Arab Emirates (UAE) marginalized and peripheral:

- The development of Gulf Aviation (now Gulf Air) illustrated how the airline emerged as a symbol of pan-Gulf aspiration in the 1970s, with ownership divided among Bahrain, Abu Dhabi, Oman, and Qatar.
- Bahrain also made aviation headlines in 1976 when it was the destination for the inaugural British Airways Concorde flight from London's Heathrow Airport to Manama.
- Yet it was Gulf Air's relative neglect of Dubai that prompted the ruling circle in that emirate to form their own airline, Emirates, with two leased aircraft in 1985 and begin the process of transforming first regional and then global aviation patterns.

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[1] "Aviation in the Gulf: Rulers of the New Silk Road," *The Economist*, June 3-9, 2010.
[2] "Dubai Jumps Heathrow as 'World's Busiest International Airport,'" *USA Today*, January 28, 2015.

The rapid expansion of Emirates in the 1990s and the growth of regional rivals Qatar Airways (which began operating in 1994) and Etihad (2003) forms the centerpiece of the second section, which compares and contrasts the three airlines' development and operational models. The third and final section of this report examines how the Gulf airlines have contributed in practice to the deeper changes to the Gulf Cooperation Council (GCC) states' role in the world economy:

- This is evident in the announcement of new destinations that simultaneously reflect and reinforce the broader shifts in patterns of international trade and investment.
- Moreover, the announcement of lucrative aircraft orders has provided Boeing and Airbus with vital revenue flows at a time of contraction and consolidation elsewhere in the aviation industry.
- This has given the Gulf airlines further leverage over manufacturers and created significant sources of friction among their commercial rivals.

Yet the report ends by questioning whether the Gulf can sustain three aggressively expanding airlines within such a concentrated region (and market) and examines the fate of low-cost carriers as well as Kuwait Airways and Gulf Air as they struggle to compete and survive. Hence, the impact of the Gulf on global aviation is a microcosm of the GCC states' emergence as rising, yet potentially unsustainable, longer-term powers in the contemporary international system.

Gulf Aviation in Context

The geographical location of the Arabian Peninsula has made the region a strategic cog in the map of global aviation since the earliest period of intercontinental flight. This initially revolved around the British-protected sheikhdoms' positioning within the wider sphere of imperial communications that linked the United Kingdom with India, Hong Kong, and Australasia. When Imperial Airways (the forerunner of the British Overseas Airways Corporation and, still later, of British Airways) launched its eastern route from London's Croydon Airport to Brisbane in Australia in 1932, it established an overnight stop and constructed an airfield in the Trucial State of Sharjah. The resonance of this move echoed across the decades in a decision 80 years later when Emirates and Qantas established a code-sharing partnership that saw the Australian airline reroute its European traffic through Dubai, a mere few miles from Sharjah, rather than through

Singapore.[3] Imperial Airways paid the ruler of Sharjah, Sheikh Sultan bin Saqr Al Qasimi, a monthly fee of 800 rupees for landing rights and fees at the new airfield as well as a monthly subsidy of 500 rupees. For his part, the ruler constructed a rest house at the Al Mahatta Fort, which became one of the first "hotels" in the Gulf, while Britain's Royal Air Force (RAF) continued to use the Sharjah airfield as a regional base until Britain's military withdrawal from the Gulf in November 1971.[4]

Sharjah's pioneering role in regional aviation was superseded in the 1950s by the formation of Saudi Arabian Airlines in 1945, Gulf Aviation in Bahrain in 1950, and of Kuwait Airways in 1953 (Table 1).

Table 1. Founding of Airlines in the Gulf

Year	Airline	Current Status
1945	Saudi Arabian Airlines	Operating as Saudia
1950	Gulf Aviation	Gulf Air/national carrier of Bahrain since 2007
1953	Kuwait Airways	Operating
1985	Emirates	Operating
1993	Oman Air	Operating
1994	Qatar Airways	Operating
2003	Etihad	Operating
2003	Air Arabia	Low-cost carrier based in Sharjah
2004	Jazeera Airways	Low-cost carrier based in Kuwait
2005	Wataniya Airways	Kuwaiti carrier ceased operating in 2011
2006	RAK Airways	Ceased operating in 2014
2007	Flynas	Low-cost carrier operating in Saudi Arabia
2007	Bahrain Air	Low-cost carrier ceased operating in 2013

Source: Information compiled by Kristian Coates Ulrichsen

[3] "Qantas-Emirates Alliance Ends Singapore Stopover," *The Australian*, September 10, 2012.
[4] Frauke Heard-Bey, *From Trucial States to United Arab Emirates* (London: Longman, 1996), 298.

Gulf Aviation was established by a British former RAF pilot, Freddie Bosworth, as a private shareholding company and commenced regular scheduled services to Doha, Sharjah, and Dhahran in Saudi Arabia. Following Bosworth's death in 1951 while test flying a larger plane for the company, BOAC acquired a 22 percent stake in Gulf Aviation, only to be bought out by the governments of the newly-independent Abu Dhabi (UAE), Bahrain, Oman, and Qatar in 1973. Each of the governments took a quarter-share in the new holding company, Gulf Air, which became the carrier for the four states/emirates. In 1990, Gulf Air became the first Middle Eastern airline to fly to Australia and added direct flights to South Africa after the end of the country's apartheid-era isolation, but the evolving aviation market and the rise of Emirates as a regional competitor hit hard. In particular, the decision by Qatar and Abu Dhabi to follow Dubai and establish their own national airlines led them to withdraw from Gulf Air in 2003 and 2005. Oman followed suit in May 2007, whereupon Gulf Air became the national airline for Bahrain.[5]

Although an airport and regular air services had been established in Kuwait as early as 1927 and 1932, respectively, it was not until 1953 that two Kuwaiti businessmen launched the Kuwait Airways Corporation (KAC) with government participation in the form of a 25 percent stake (which became a 50 percent share in 1955 and full state ownership in 1962 after Kuwaiti independence). Flights to London and other European destinations began in 1964 (seven years before Gulf Air) and Kuwait Airways built up an extensive network of Middle Eastern and Asian routes during the 1960s and 1970s. However, Kuwait International Airport was among the first targets attacked in the opening phase of the Iraqi invasion of Kuwait on August 2, 1990 and the majority of the Kuwait Airways fleet either was destroyed or seized and taken to Iraq. This precipitated a long-running legal claim for compensation against Iraqi Airways that led in 2010 to the impounding of the first Iraqi Airways commercial flight to land in the United Kingdom since the Gulf War.[6] Kuwait Airways struggled to recover from the scale of the losses sustained during the occupation and developed a reputation as a bloated and inefficient state-run organization with a heavily-unionized labor force that lagged far behind its regional rivals in the 2000s. Long-running attempts to privatize Kuwait Airways started in the mid-1990s, but the

[5] "Oman's Gulf Air Pull Out to Benefit Bahrain in Long Run," *Khaleej Times*, May 7, 2007.
[6] David Roberts, "Kuwait's War of Words with Iraq," *Foreign Policy*, July 20, 2011.

stop-start negotiations failed repeatedly to find a suitable buyer willing or able to take on such a loss-making asset.[7]

While Gulf Air and Kuwait Airways have been far surpassed by the exponential growth of Emirates, Qatar Airways, and Etihad since the 1990s, it is instructive to bear in mind the sheer rapidity and scale of the growth in aviation in the UAE and Qatar. As late as 1962, an international official arriving in Abu Dhabi for the first time described his arrival thus:

> "Oh my God, we've crash landed!" I'm afraid this was my first thought as the small commuter plane of Gulf Aviation hit the ground. It took a while to realize that we had actually landed at Abu Dhabi. This was because looking out of the window upon landing just showed gravel on the ground and no tarmac, no runway as one was accustomed to seeing at airports … Stepping out, there was little semblance of an airport; no terminal building, just a shade by the wayside in what appeared to be total wilderness … A red and white Abu Dhabi flag hoisted upon a pole was the only indication that this was indeed Abu Dhabi. A lone date palm standing tall at a distance was the only welcome sign.[8]

A British official who also arrived in Abu Dhabi in 1962 to take up a post in the growing local bureaucracy described further how the airport manager would wave a flag to incoming pilots to indicate whether the dirt runway was firm enough to land on, and that, while there were no night flights, "in emergencies, as many vehicles as possible would be rounded up to line both sides of the runway and switch on their headlights to guide the pilot down."[9]

Rise of the Global Airlines

Emirates

As stated in the section above, the decline of the "early-movers" in Gulf aviation began in earnest with the creation of Emirates in 1985:

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[7] "Parliament Oks Amendments to Kuwait Airways Law," *Kuwait News Agency* (KUNA), January 9, 2014.
[8] Abdul Hafeez Yawar Khan Al Yousefi, "50 Years in Al Ain Oasis—Memoirs of Khabeer Khan," *Liwa: Journal of the National Center for Documentation and Research*, 5, no. 9 (2013): 58.
[9] John Woolfenden, "Memories of Abu Dhabi and Al Ain in the Early Nineteen-Sixties," *Liwa: Journal of the National Center for Documentation and Research*, 2, no. 4 (2010): 44.

- The standoff between Gulf Air and the ruler of Dubai began in 1984 after the company reduced the number of weekly flights from Dubai from 80 to 39.
- In response, Sheikh Mohamed bin Rashid Al Maktoum, the third son of the ruler, Sheikh Rashid bin Saeed Al Maktoum (and, from January 2006, the ruler of Dubai) resolved to create a new airline.
- With US$10 million in seed funding from the ruling family together with a US$88 million gift of two Boeing 727s from the royal fleet and an Airbus and a Boeing leased from Pakistan International Airways, Emirates' four-strong fleet commenced operations with a flight from Dubai to Karachi on October 25, 1985.

Throughout its history, Emirates has benefited from the close support of Dubai's ruling family through the chairmanship of Sheikh Ahmed bin Saeed Al Maktoum, an uncle of the present ruler, Sheikh Mohammed. Moreover, the airline was one of the few in the Gulf that maintained a full service throughout the Gulf War (January-February 1991) and picked up additional traffic during the conflict, especially from the temporarily grounded Kuwait Airways.[10]

Emirates based its early growth on the mass markets used by labor migrants to the Gulf with Mumbai, Delhi, Colombo, and Dhaka quickly joining the initial route from Dubai to Karachi. This was followed by expansion into regional markets (Cairo and Amman) and subsequently, in 1987, into Europe with flights to London's Gatwick, Frankfurt, and Istanbul. The London flight was noteworthy as Emirates offered alcoholic beverages to all passengers in a move that marked the airline as distinct from its regional competitors and able both to anticipate and cater to customer demand, which surged as a result. In response, Emirates subsequently made alcohol available in all classes of service on all routes save those to and from Saudi Arabia (and while over Saudi airspace). This was a highly innovative concept for a Middle Eastern airline to introduce at the time. Routes to East Asia (Bangkok, Singapore, and Hong Kong) followed in the late 1980s and early 1990s, and Manila; by the time of Emirates' 10th year of operation in 1995, it was already serving 30 different countries.[11]

A number of significant factors lay behind (and made possible) the great acceleration of Emirates' growth in the late-1990s:

[10] Jim Krane, *Dubai: The Story of the World's Largest City* (London: Atlantic Books, 2009),107-108.
[11] "Emirates Airline History," available online at http://www.airreview.com/Emirates/History.htm.

- The decision of Dubai's leadership to aggressively market the emirate as an international shopping and mass tourism destination and thereby create the demand for visitors that Emirates would tap.
- The launch of Emirates Holidays in 1992 marked an early attempt to raise brand awareness of Dubai as a destination and later events included the annual Dubai Shopping Festival (first held in 1996) in the winter months and the Dubai Summer Surprises Festival to overcome the traditional lull in summer visitors.[12]
- Integral components of this strategy encompassed the construction of the largest mall in the world (Dubai Mall), the launch of an artificial Ski Dubai slope in another signature mall (Mall of the Emirates), and such iconic hotels and buildings as the sail-shaped Burj Dubai and the 2,722-feet high Burj Khalifa, the tallest manmade structure in the world when it opened in a lavish ceremony in 2009.[13]

As the number of visitors to Dubai soared from just 400,000 in 1985 to over 3 million in the mid-2000s and 5.8 million in the first six months of 2014 alone,[14] a closely related element of Emirates' breakneck expansion was the series of massive new orders for long-range aircraft:

- The influx of state-of-the-art Boeing 777s in the 1990s and Airbus A340s and A380s in the 2000s gave the airline a transcontinental reach that offered passengers the option of bypassing traditional European hubs such as London, Frankfurt, Paris, and Amsterdam.
- The first Boeing 777s entered the fleet in 1996, but it was the arrival of the A340 in 2003 that enabled Emirates to launch direct services to the lucrative North American market.
- By 2014, Emirates linked Dubai with nine cities across the United States, the most of any Gulf airline, and flew as far afield as Houston, Los Angeles, San Francisco, and Seattle.
- Another successful approach saw the airline fly to hitherto "secondary" airports in key European countries, allowing travellers direct routings that would previously have required a stop in their capital's "hub" airport. Examples in the United Kingdom include Glasgow, Manchester, and Newcastle (bypassing London Heathrow), Hamburg and

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[12] Christopher Davidson, "The Impact of Economic Reform on Dubai," in *Reform in the Middle East Oil Monarchies*, eds. Anoushiravan Ehteshami and Steven Wright (Reading: Ithaca Press, 2008), 157-158.
[13] Christopher Davidson, *Dubai: The Vulnerability of Success* (London: Hurst & Co, 2008), 111.
[14] "Dubai Hotels Enjoy Busiest Half-Year Visitor Numbers," *Khaleej Times*, August 25, 2014.

Dusseldorf in Germany (bypassing Frankfurt), and Nice and Lyon in France (bypassing Paris Charles de Gaulle).[15]

Qatar Airways

The success of Emirates in branding Dubai as an internationally known city and destination resonated among the leadership in neighboring Qatar after the new Emir, Sheikh Hamad bin Khalifa Al Thani, took power in 1995. The generational shift that took place in Qatar in the mid-1990s brought to power the architects of Qatar's robust internationalization strategy spearheaded by the Emir and his ambitious foreign minister, Sheikh Hamad bin Jassim Al Thani:

- Qatar Airways was originally created in 1994, the year before Sheikh Hamad bin Khalifa became Emir, but the new leader re-launched the airline three years later having installed its (current) chief executive, Akbar al-Baker, in 1996.[16]
- Following its rebranding, Qatar Airways expanded quickly and mirrored Emirates in placing large new orders for next-generation aircraft.
- After being one of the earliest airlines to operate Boeing's 787 "Dreamliner," Qatar Airways took delivery of the very first Airbus A350 to enter commercial service in December 2014.
- Notably, Qatar Airways had been the first airline to place an order for the A350 in 2007, and its subsequent orders for 80 A350s were instrumental in driving the demand for the new wide-body aircraft.[17]

Qatar Airways gained a truly global reach as the size of its fleet rose from four aircraft in 1997 to 28 in 2003, 50 in 2006, and 146 by the end of 2014 with double-digit growth both in the number of destinations served each year and in percentage rises in passenger traffic. However, the airline followed a very different business strategy from Emirates that reflected, in part, the unwillingness of the Qatari authorities to follow the "Dubai model" and brand itself for the mass tourism market:

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[15] Author interviews, Dubai and London, April 2012 and January 2014.
[16] "The Qatar Airways Story," January 2015, available online at http://www.qatarairways.com/iwov-resources/temp-docs/press-kit/The%20Story%20of%20Qatar%20Airways%20-%20English.pdf.
[17] "Qatar Airlines Take Delivery of First Airbus A350," *Euronews*, December 22, 2014.

- Qatar has remained instead a relatively low-volume tourist destination, with an estimated 95 per cent of all visitors coming for business rather than pleasure, and Qatar Airways has marketed itself more as a hub and connector rather than as a destination in itself.[18]
- Statistics for March 2014 found that just over 40 percent of all incoming passengers to Doha's old (and about to be replaced) international airport were in transit rather than arrival (737,000 out of 1.817 million passengers).[19]
- Moreover, the Qatar Airways leadership was disinclined to purchase stakes in other airlines, with its chief executive, Akbar al-Baker, noting pointedly that "We will always go after goldsmiths, not scrap dealers."[20]
- Qatar Airways did nevertheless become the first Gulf airline to formally join a global alliance, Oneworld, in 2012, and in January 2015 purchased a 10 percent stake in the International Airlines Group, the parent company of British Airways and Iberia.[21]

The appeal to business (and transit) travellers reflected a decision of Qatari officials to target the lucrative MICE (Meetings, Incentives, Conferences, and Events) circuit as a key dimension of their effort to place Qatar firmly on the global map in the 2000s:

- Strategic emphasis was placed by Qatar, Dubai, and Abu Dhabi and their respective airlines on the hosting and sponsorship of major international sporting events. In the case of Qatar, the 2022 FIFA World Cup will give a major boost to Qatar Airways, particularly if the airline becomes one of FIFA's six Official Worldwide Partners after rival Emirates ended its sponsorship in November 2014.[22]
- Meanwhile, Emirates and Etihad each have attached their name to major soccer stadia in London and Manchester, respectively, and entered the global sporting lexicon in much the same way as Old Trafford and Wembley.

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[18] Q&A with Ahmed Al Nuaimi, chairman, Qatar Tourism Authority, "Boosting Visitor Numbers While Improving Quality and Offerings," *B'Here Annual Review*, Qatar 2012: The Vision Moves Forward: Towards a Knowledge-based Society (Doha: Arab Communications Consult, 2012), 260–2.
[19] "Overtaxed Doha Airport Sees 6mn Passengers in First Quarter 2014," *Doha News*, April 27, 2014.
[20] "Qatar Airways Interested in More Buyouts," *The Peninsula*, March 5, 2015.
[21] "Qatar Airways Buys 10% of British Airways Owner IAG," *The Guardian*, January 30, 2015.
[22] "Emirates Airline Pulls Out of Backing FIFA and Could be Followed by Sony," *The Guardian*, November 3, 2014.

- In 2010, Etihad increased by 60 percent the capacity of its flights to Manchester after its sponsorship of Manchester City's stadium (and the club's takeover by the ruling family) increased greatly the emirate's profile (and soft appeal) in the northwest of England.[23]

Etihad

As the youngest of the three major Gulf airlines, Etihad nevertheless has moved fast to develop a global profile and compete in a highly concentrated regional market:

- Established by an Emiri Decree in July 2003 and chaired by Sheikh Hamad bin Zayed Al Nahyan, a half-brother of the president of the UAE (and also the ruler of Abu Dhabi), Etihad commenced operations in November and almost immediately made a large, multi-billion dollar acquisition of new aircraft from Boeing and Airbus.
- Later, in 2008, the airline made international headlines when it announced the largest aircraft order in history with the planned purchase of up to 205 new planes worth more than US$20 billion. The arrivals facilitated the rapid expansion of the Etihad network, which like Qatar Airways added new destinations at often dizzying speed.
- Comments by Etihad's chief executive, former Gulf Air head James Hogan, captured the bullish mood among Gulf airlines: "The size of our order also mirrors the rising prominence of the Middle East and its increasing emergence as a new focal point for global aviation. The Gulf is a natural air bridge between East and West."[24]

Etihad has followed its own distinct growth model, which differs both from Emirates' organic expansion in tandem with Dubai's growth and the Qatar Airways emphasis on business and transit passengers:

- The most notable feature of this strategy has been the formation of "equity alliances" with struggling airlines, many in Europe, that enable Etihad to "add more spokes to its Abu Dhabi hub" and differ sharply from the Qatar Airways perspective on growth.[25]
- These equity alliances include 49 percent stakes in Alitalia and Air Serbia, 40 percent in Air Seychelles, a 34 percent stake in Darwin, a Swiss regional airline since rebranded as

[23] "Capacity Increase Confirmed on Etiihad's Flights to Manchester," *Skyscanner*, February 19, 2010.
[24] "Etihad Splits Massive Order Between Boeing, Airbus," *USA Today*, July 15, 2008.
[25] "Qatar Airways Stake in British Airways Parent IAG Creates Intriguing Alliance," *The National*, February 3, 2015.

Etihad Regional, 29.21 percent in Germany's Air Berlin, 24.2 percent in Virgin Australia, and 24 percent in India's Jet Airways.

- The stakes were intended to give Etihad a foothold in regional markets and provide feeder traffic for the long-haul flights operated by the parent airline but the Darwin acquisition, in particular, faced fierce local opposition by Swiss and its parent company, Lufthansa.
- Embattled European carriers also turned to the European Commission for support in their campaign to limit foreign ownership of European airlines with an (ongoing) investigation into the issue launched in 2014.[26]

Redrawing Global Maps

The emergence of the three Gulf airlines has shaken global aviation markets to their core:

- An example of the speed and scale of their rise was evident in a February 2015 report by the U.S. aviation industry that indicated that the Gulf carriers' share of bookings between the United States and the Indian subcontinent rose from 12 percent in 2008 to 40 percent by 2015.
- This surpassed the share of the international U.S. carriers (American Airlines, Delta Air Lines, and United Airlines) and their alliance partners such as British Airways and Air France, which fell from 39 percent to 34 percent over the same period.[27]

Such trends and shifts in market share have generated widespread concern among competitors who perceive the state-backed carriers benefit from unfair competitive advantages:

- Particular resentment focused around a "home market rule" preventing European and North American airlines originating from countries where Airbus and Boeing construct aircraft from using export credit agencies to assist their carriers buy aircraft.
- This regulation impacted all U.S. carriers due to Boeing and most of the larger airlines in Europe owing to the pan-European nature of Airbus, but left Gulf airlines unaffected.

[26] "EU Widens Etihad Probe to Include More European Carriers," *ArabianBusiness.com*, April 10, 2014.
[27] "U.S. Airlines Losing Asia Market Share," *Las Vegas Review-Journal*, February 10, 2015.

- Skepticism toward the Gulf airlines was strongest in Germany, where Lufthansa vociferously alleged that Gulf carriers utilize public subsidies to finance aircraft deals, and in Canada, where the government transport agency initially declined (in 2010) to make additional landing slots available to Emirates and Etihad.[28]

Ottawa's action triggered a damaging spat between Canada and the UAE:

- The Emirati government responded to the Canadian restriction on landing slots by closing a military base near Dubai that was being used to support Canadian troops in Afghanistan.
- An additional flexing of bilateral muscles occurred when the Emirati authorities suddenly introduced steep visa fees for Canadian citizens wishing to enter the UAE even as visas for most other European and North American visitors remained free at the port of entry.
- In a direct attempt to retaliate by gaining market share from Canadian airlines, Emirates and Etihad offered passengers significant discounts if they arranged their visas and their travel through the UAE carriers.[29]

The new regulations remained in place for nearly three years as officials struggled to rebuild the bilateral relationship with Canada's largest export market in the Middle East. In April 2013, the announcement of a codeshare agreement between Air Canada and Etihad that would open up the Canadian market signified the end of the Ottawa government's effort to protect the national airline that increasingly came at the cost of Canadian trade relations.[30]

European and North American carriers' concerns were not without foundation. The CEO of American Airlines, Doug Parker, acknowledged in September 2014 that "I worry about our ability to compete with other countries that are much more understanding and supportive of global aviation."[31] Indeed, the three Gulf airlines fall within the nebulous state-business landscape in the Gulf where the line between public and private enterprise (as well as state and ruling family wealth) can be opaque at best:

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[28] "Lufthansa Seeks to Clip Emirates' Wings in Europe, Berlin Mayor Says," *ArabianBusiness.com*, January 16, 2011.
[29] "UAE Embassy to Charge Canadians Steep Visa Fees," *The Globe and Mail*, December 28, 2010.
[30] "Etihad and Air Canada Strike Codeshare Deal," *The National*, April 25, 2013.
[31] Ted Reed, "Note to Abu Dhabi on Pre-Clearance: Be Careful What You Wish For," *Forbes.com*, October 14, 2014.

- As documented above, both Emirates and Etihad are chaired by the uncle and half-brother of the respective rulers.
- In May 2014, Qatar Airways chief executive Akbar al-Baker noted that "We became fully government owned in July last year" after the state bought out private investors who previously had a 50 percent shareholding in the airline.
- Significantly, it emerged that the largest private shareholder had been former Prime Minister Sheikh Hamad bin Jassim Al Thani, although it remained unclear how large his personal shareholding had been, how much the state had paid for the shares, and whether Sheikh Hamad had purchased the shares in his capacity as a member of the ruling family, a private businessman, Qatar's prime minister, foreign minister, or head of the Qatar Investment Authority.[32]

For their part, the three Gulf airlines responded robustly to the criticisms and allegations levelled against them, which include that they benefit from an un-unionized and lower-wage workforce in addition to access to cheaper fuel or financing options.

- Many of the international airlines' accusations against Gulf airlines revolved around subtle matters of interpretation of direct and indirect government support that, at times, resembled the splitting of hairs.
- Qatar Airways chief executive Al-Baker denied that his airline received government subsidies but added that "What the government has given us is equity into an airline which they own."[33]
- Al-Baker's counterpart at Etihad, James Hogan, was equally vague as he acknowledged—under pressure from negative publicity in the United States—that "Like any new airline, there was seed money and there was shareholder equity."
- Suspicion around such arrangements was magnified by the fact that neither Qatar Airways nor Etihad have allowed public scrutiny of their finances, in marked contrast to Emirates, which does disclose its financial accounts and use international auditors.[34]

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[32] "Qatar Airways CEO Says Company Fully Govt-Owned; Interested in IndiGo Stake," *Reuters*, May 5, 2014.
[33] "United States Escalates Arabian Gulf Airline Subsidies Row,'" *Bloomberg News*, March 5, 2015.
[34] "Etihad Airways' Rapid Growth Frustrates Rivals," *The New York Times*, March 2, 2015.

In February 2015, the three largest U.S. carriers—American, Delta, and United—revived the subsidy issue as their chief executives claimed that the Gulf airlines received an "unfair advantage" from state support and called on the Obama administration to review the U.S. government's air treaties with Gulf partners. This represented a major step away from the Open Skies policies that U.S. airlines had for years advocated:

- In meeting with Obama administration officials, the three U.S. airlines compiled a 55-page dossier detailing alleged irregularities in Gulf airlines' financing, which they did not make public.
- According to a report that appeared in *The New York Times*, the dossier alleged that the three Gulf airlines had received more than US$38 billion in government subsidies.
- The dossier suggested that Etihad alone had benefited from US$17 billion in government subsidies in its first decade of existence, including US$6 billion in interest-free loans from the Abu Dhabi government to fund new airplane acquisitions and a further US$6.5 billion to cover operating losses.

Belligerently, the dossier was believed to have claimed that:

> Etihad's argument fundamentally misunderstands the international consensus on the definition of subsidy. Given the company's dismal financial performance over the last 10 years, if not for the subsidies, Etihad would have gone out of business.[35]

- Qatar Airways, the dossier suggested, derived similar levels of state support in the form of an alleged US$7.7 billion in interest-free loans from the Qatari government and US$6.8 billion in reduced interest charges owing to sovereign debt guarantees.
- Moreover, the dossier indicated that Emirates had benefited from varying levels of support from the leadership in Dubai, which allegedly included their assumption of a US$2.4 billion loss from fuel hedging, a further US$2.3 billion in savings from artificially low airport charges, and, rather intangibly, US$1.9 billion in savings from the airline's non-unionized workforce.[36]

[35] Ibid.
[36] 'Airline Subsidies in the Gulf: Feeling the Heat,' The Economist, 6 March 2015.

However, Emirates chairman Sheikh Ahmed bin Saeed Al Maktoum responded bluntly to the allegations of uncompetitive advantage by calling on the U.S. carriers to "improve their service" and stating that "Offer the best to the passengers and people will fly with you."[37] Qatar Airways' chief executive Al-Baker was blunter still in response to a May 2015 decision by the Dutch government that it would temporarily suspend the granting of new landing slots at Amsterdam's Schiphol Airport to Gulf airlines. Addressing the Dutch government, al-Baker warned that

> "If you do not allow us to benefit in a small way by bringing flights, you should not expect commercial contracts from the [Qatari] government … My government will definitely not be happy … [Royal Dutch] Shell is one of the single biggest investors in the country and there are some US$150 billion in infrastructure projects coming up in the next years."[38]

Meanwhile, Etihad hit back at the U.S. airlines' allegations by making claims of its own that U.S. airlines had received more than US$70 billion in government benefits and concessions since 2000, "enabling the nation's three largest carriers to transition from the verge of bankruptcy to today's industry leaders."[39]

More substantively than the allegations contained in the dossier, which the U.S. airlines declined to publish, an investigation conducted by *Reuters* in February 2015 found that local cash-rich banks increasingly were playing a greater role in aircraft financing for the Gulf airlines in addition to the traditional reliance on the controversial use of export credit agencies and cash injections to fund acquisitions. Whereas only 17 percent of aircraft deals in the Middle East (as a whole) were funded by local banks in 2013, the figure rose substantially to 47 percent in 2014. *Reuters* suggested that this was in part due to the fact that "After years of piling lending into the region's volatile property sector, local bankers see aircraft financing as a way to diversify risk into an asset class where the likely pitfalls are smaller."[40]

The above notwithstanding, the Gulf airlines have taken advantage of a more benign set of domestic circumstances and have, on occasion, been robust in saying so. In a 2010 interview,

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[37] 'Emirates Executives Rebuff US Airlines' Claims of $40 Billion in Subsidies to Gulf Carriers.' The National, 11 February 2015.
[38] 'If You Want Qatar State Contracts, Give Us Flight Slots, Says Airline CEO,' The National, 27 May 2015.
[39] 'Etihad Says Top US Airlines Get USD71.5bn in Subsidies,' AFP, 15 May 2015.
[40] 'Gulf Banks Helping to Underwrite Region's Aviation Boom,' Reuters, 3 February 2015.

chief executive James Hogan explained the benefits Etihad derives from operating within the political economy of Abu Dhabi, and as a latecomer relative to established European "legacy" carriers:

> "I don't have to tackle the union issues of these other carriers and I don't have additional costs because we can outsource a lot of things. When it comes to other carriers, we are both similar service airlines, but they are bound by agreements, employment agreements, 15, 20, 30, or 40 years old that are very hard to renegotiate. They are bound by infrastructure—facilities and bases that were right for them 30 years ago or even 20 years ago, but aren't today. I am fortunate that I have a clean sheet of paper."[41]

Such comments encapsulate the commercial advantages to Gulf operators of working without the constraints imposed by organized labor on European and North American competitors, and by the less stringent social welfare requirements that impart a certain advantage over Western rivals.[42]

Gulf airlines have also been recipients of major levels of what might be construed as indirect or "soft" support by their parent emirates through the construction of some of the largest and most modern airports and associated infrastructure in the world:

- Both Dubai and Doha opened new airports in 2013 and 2014, respectively, while Abu Dhabi is engaged in a large-scale expansion of its own international airport with the construction of an enormous new Midfield Terminal Complex scheduled for completion by 2017.
- In addition to Dubai International Airport, officials in Dubai have started to open in phases what will eventually become the world's largest airport, Al Maktoum International, reinforcing the emirate's role as the preeminent logistical and infrastructural hub in the region. The centerpiece of the Dubai World Central economic, commercial, and residential zone, the airport is expected to have a capacity of 160 million passengers a year when it becomes fully operational.

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[41] Mark Summers, 'Etihad Airways: Staying the Course,' The Gulf Business News and Analysis, May 2010, available online at http://www.thegulfonline.com/Articles.aspx?ArtID=3001.
[42] David Held and Kristian Ulrichsen, 'Introduction,' in David Held and Kristian Ulrichsen (eds.), The Transformation of the Gulf: Politics, Economics and the Global Order (Abingdon: Routledge, 2011), p.11.

- Remarkably, the construction of the massive new airport will complement the existing Dubai International Airport, which already contains the largest terminal building in the world.

Dubai International handled almost 70 million international passengers in 2014 and work is underway to add a new concourse that would raise capacity to more than 90 million. This has induced a weary acceptance from long-established competitors such as Heathrow, evidenced in a statement following the news that Dubai had become the busiest international airport in the world: "Britain has benefited from being home to the world's largest port or airport for the last 350 years. But lack of capacity at Heathrow means we have inevitably lost our crown to Dubai."[43]

Table 2. World's Busiest Airports by International Passenger Traffic

Rank	2013	Traffic	Rank	2014	Traffic
1	London Heathrow	66,689,466	1	Dubai	69,954,392
2	Dubai	65,872,250	2	London Heathrow	68,091,095
3	Hong Kong	59,294,439	3	Hong Kong	62,929,420
4	Paris CDG	56,767,748	4	Paris CDG	58,623,111
5	Singapore	52,775,360	5	Amsterdam	54,940,534

Source: Airports Council International

A different form of leverage has been exercised by Abu Dhabi, which built up a close political, defense, and security relationship with the U.S. government, focused around (but not limited to) the emirate's plans to develop civilian nuclear energy:

- In the aviation sector, such ties were illustrated by the January 2014 launch of the first customs and border pre-clearance facility to open outside the United States since the 1980s.
- The pre-clearance facility encountered strong opposition from aviation leaders in the U.S., who worried it would give a further competitive advantage if passengers from Abu Dhabi could avoid potentially long lines on arrival at U.S. airports.

[43] 'Dubai Airport Claims Top Spot for Global Passenger Traffic in 2014,' Jakarta Globe, 27 January 2015.

- These concerns were offset by an agreement that Abu Dhabi would meet 80 percent of the cost of the facility, including the salaries of the Customs and Border Patrol officers needed to staff it. Fourteen members of Congress argued in a letter to the Department of Homeland Security in Washington, D.C., that the facility in Abu Dhabi represented a "dangerous precedent" of basing customs and border control on third-party financing rather than national security interests.[44]

Ironically, the pre-clearance facility was beset by chronic overcrowding in its first year of operation, leading to persistent delays on U.S.-bound flights and causing frustration among passengers and Etihad staff alike.[45]

The three Gulf airlines therefore have emerged as leading players in a global market that itself is undergoing major restructuring and consolidation. The importance of the Gulf airlines is reflected in numerous indicators such as the size of their order books for new aircraft—US$107.5 billion for Emirates, US$57.7 billion for Qatar Airways, and US$28.5 billion for Emirates as of 2015.

In addition to generating significant new demand at Airbus and Boeing, the scale of the orders are themselves reshaping patterns of international trade:

- By 2012, for example, the UAE was the fourth-largest export partner of Washington State after China, Canada, and Japan but far ahead of much larger industrialized economies such as South Korea, the United Kingdom, and Germany.[46] With nearly all of the bilateral trade between Washington and the UAE generated by Boeing, the launch of a daily Emirates flight from Dubai to Seattle in 2013 was symbolic.
- Elsewhere, the launch of new routes provided an illustration of the new intra-regional ties binding the Gulf into the global economy. These included heavy emphasis on new destinations throughout China as well as direct flights to Latin America, and made it

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[44] "U.S. Customs Passenger Facility Opens in Abu Dhabi," *USA Today*, January 27, 2014.
[45] Ted Reed, "Note to Abu Dhabi on Pre-Clearance: Be Careful What You Wish For," *Forbes.com*, October 14, 2014.
[46] "Total U.S. Exports (Origin of Movement) via Washington: Top 25 Countries Based on 2013 Dollar Value," United States Census Bureau: Foreign Trade, available online at https://www.census.gov/foreign-trade/statistics/state/data/wa.html.

possible for travellers to fly to any two points in the world with a single stop in the Gulf, with Johannesburg-Doha-Tokyo only one example of many.

Questions nevertheless remain over whether three such aggressive and expansionary airlines can coexist in such a concentrated region, no matter how global their activity:

- So long as Emirates, Etihad, and Qatar Airways are taking market share from international rivals they are likely to continue to grow.
- However, should the aviation market ever reach saturation point or the host emirates begin to experience long-term fiscal challenges, this will put to the test the Gulf carriers' ability to turn a profit and operate as genuine standalone entities independent of any state support.
- Moreover, their dominance also has resulted in a "two-tier" regional market that has made it far harder for operators such as Kuwait Airways and Gulf Air to be competitive with their powerful rivals while other airlines, such as Wataniya Airways (in Kuwait), Sama Airlines (a low-cost private carrier in Saudi Arabia), Bahrain Air, and RAK Airways in the UAE, ceased operating altogether between 2010 and 2014.

The case of Bahrain Air, in particular, was notable for the illustration of Gulf airlines' vulnerability to regional and political instability. The airline never fully recovered from the Bahraini government's decision to suspend direct flights to Lebanon, Iraq, and Iran following the 2011 Shia-led uprising in the country. The loss of some of Bahrain Air's highest-yield and most profitable routes was compounded by the denial of a request to the government for compensation; the airline cited the "unstable political and security situation" and "sustained considerable financial losses" as the reasons for its closure in February 2013.[47] Shortly thereafter, the chief executive officer of Bahrain Air, Richard Nuttall, spelled out the challenging operating conditions facing the "other" Gulf carriers:

> In a part of the world where almost every other airline is subsidized, and flying from a small kingdom which is currently going through its own issues, it was always going to be difficult to be truly profitable. There is not enough point-to-point traffic, and regional

[47] "Bahrain Air Plans to Liquidate as Unrest Disrupts Travel," *Bloomberg*, February 13, 2013.

> connecting traffic yields are too low to sustain an airline. So it was always going to struggle by traditional measures.[48]

In such a context, the discrepancy between the local aviation market in the Gulf and the global ambitions of its three largest carriers becomes readily apparent:

- Should state support, in all its soft forms, ever be withdrawn or scaled back, it is likely that Emirates, Etihad, and Qatar Airways would face similar restructuring and downsizing challenges as Kuwait Airways and Gulf Air, their predecessors as the aviation symbols of the Gulf.
- This may, however, be averted should the large Gulf carriers succeed in creating a critical mass of customers, destinations, and innovative products that take advantage of the region's central geographical location and upwardly mobile clientele.
- With more than 3 billion people living within an eight-hour flight from GCC capitals, including in the rapidly growing Chinese and Southeast Asian markets, such trends both reflect and reinforce the broader rebalancing of the global economy and the opportunities within this for Gulf airlines.

With the Gulf airlines a pivotal element of the rebalancing of global aviation power, U.S. and European airlines and government officials should work with their counterparts in Qatar and the UAE to avoid any breakdown in Open Skies policies and reversion to protectionism.

- The rise of large new growth areas and the appearance of "insurgent" market entrants inherently pose a challenge to the established markets and "status quo" airlines in North America and Europe.
- However, the current cycle of accusation and counter-accusation is unproductive and not conducive to a sustainable solution that satisfies all parties.
- Greater financial and operational transparency among all carries matched by a measured and open debate across the aviation sector could provide the basis for a more consensual approach to the deep structural changes underway in the industry.

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[48] "Bahrain Air CEO Richard Nuttall Discusses the Airline's Closure," *The Aviation Writer*, March 13, 2013.

The airline industry, comprising both the International Air Travel Association and member airlines, should work instead with national governments and international regulators to formulate an agreed set of guidelines to overcome the current sources of disagreement and tension. An example to follow might be the April 2008 creation of an International Working Group for sovereign wealth funds and the group's subsequent formulation of the "Santiago Principles," a voluntary set of 24 guidelines intended to establish "best practices" that October. To be sure, a voluntary code of conduct is far from perfect but can constitute a first step toward a broader discussion among all stakeholders on industry standards going forward. After all, the pace and direction of change in the aviation sector is tied fundamentally to broader shifts in the global economy and any attempt to resolve it through confrontation will almost certainly fail.