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Take the cover off KL-S'pore route

By Cassey Lee and Ivan Png

THE Malaysian government began a new chapter in the liberalisation of its domestic passenger air travel market when it allowed the budget airline AirAsia to operate in 2002.

There is little doubt that consumers in Malaysia have benefited significantly from this. The relatively low fares offered by AirAsia meant that more consumers can afford to fly both on domestic as well as on a few international routes.

Today, AirAsia's share in the Malaysian domestic market is estimated to be 25 per cent. While some of AirAsia's market share may have come at the expense of national carrier Malaysia Airlines (MAS), most of it is likely to come from the creation of 'new demand' in response to the low fares offered - consumers who would not otherwise have travelled by air.

To the Kuala Lumpur government's credit, both airlines have been allowed to compete. However, there is room for further improvement.

One issue that has been debated in the Singapore Parliament, which then prompted heated discussion in Malaysia's media, is further liberalisation of the Kuala Lumpur-Singapore shuttle route.

Several interesting facts have emerged from this debate.

First, the air fare for this route is relatively high - around RM713 (S\$310) for a round-trip between KL and Singapore.

Second, under the 1980 Air Services Agreement (ASA) signed by Malaysia and Singapore, all net revenues of MAS and Singapore Airlines are shared 50:50, with each airline bearing its own operating costs.

Third, both airlines have a dominant position in the KL-Singapore shuttle route. The combined market share of both airlines in this sector is estimated to be 85 per cent.

Singapore's Transport Ministry has stated that it is in favour of opening up the KL-Singapore route to more competition, but that this is only possible if Malaysia agrees to liberalise the ASA. However, in a recent Malaysian media report, KL's Transport Ministry was quoted as not being in favour of changing the present arrangements.

We do not know whether this is an official view of the ministry. We believe the Malaysian government should seriously consider liberalising the KL-Singapore shuttle route by adopting an open skies policy for the route.

The main issue that prevents this appears to be the perception that Singapore will gain more than Malaysia if such a policy is adopted, since MAS has only one destination - Singapore - whereas SIA/SilkAir has many destinations - the major cities in Malaysia. However, this reasoning is too narrow.

First, in estimating the 'national' welfare gains, Malaysia needs to expand its list of 'domestic carriers' to include AirAsia in the ASA negotiations. This implies including airlines that are substantially owned by Malaysians and not just those owned by the Malaysian government (69 per cent of MAS' equity is owned by Penerbangan Malaysia Berhad, which is a wholly owned subsidiary of Malaysia's Minister of Finance Inc).

Furthermore, liberalising the sector by allowing new entrants does not entail any subsidy on the part of the KL government. It merely expands business opportunities for Malaysian companies and makes the sector more competitive.

Second, liberalisation will enhance consumer welfare, in the form of benefits arising from more affordable air transport and shorter travel time. Greater competition within this sector would significantly lower fares.

Aside from benefiting local consumers in Malaysia and Singapore, it would also boost tourism in both countries.

The KL-Singapore route is perhaps the busiest of all air passenger routes between Malaysia and other countries. Singapore is also the most important source of Malaysia's tourist arrivals: Some 9.5 million people from Singapore visited Malaysia in 2004.

Furthermore, business will also benefit from lower air transportation costs. Cost-effective transport is key to Kuala Lumpur's role as a regional business hub. More choice and lower fares on the KL-Singapore route will benefit Malaysian business.

Third, there is a commitment among Asean member countries to fully liberalise direct passenger services among member nations by 2008. In December 2004, Brunei, Thailand and Singapore signed an open skies pact to liberalise their air transport sectors ahead of the 2008 deadline. Malaysia will benefit from 'first mover advantages' that would arise from joining such a network of low fare airlines.

In sum, the Malaysian government should seriously consider liberalising the KL-Singapore shuttle route by adopting an open skies policy for this sector. Holding back competition will only forestall the development of Malaysia's airline industry. Sure, there will be adjustment costs in the short run, but these should not prevent Malaysia from adopting policies that will make its economy more competitive in the long run.

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