



The U.S.-China Business Council
Aviation Forum
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The Importance of Aviation Liberalization

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**REMARKS OF ANDREW B. STEINBERG
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THANK YOU, BOB, FOR THE KIND INTRODUCTION. I ALSO WANT TO THANK THE U.S. CHINA BUSINESS COUNCIL AND ITS SPONSORS FOR HOSTING THIS TIMELY AND IMPORTANT FORUM, PRECEDING AS IT DOES THE RESUMPTION OF AVIATION NEGOTIATIONS BETWEEN THE GOVERNMENTS OF THE PEOPLE'S REPUBLIC OF CHINA AND THE UNITED STATES FOLLOWING OUR HISTORIC AGREEMENT IN 2004. IF I LEAVE YOU WITH ONE MESSAGE TODAY IT'S THIS: WE THINK THERE IS A CHANCE TO MAKE HISTORY AGAIN -- BY BRINGING THESE TWO GREAT NATIONS CLOSER TOGETHER THROUGH AN AVIATION ACCORD THAT WILL TRULY RECOGNIZE THE INCREASING BREADTH AND SIGNIFICANCE OF OUR ECONOMIC TIES. THIS MORNING I'D LIKE TO EXPLAIN WHY THAT MAKES SENSE.

Aviation is essential to expansion of the U.S.-China economic relationship

Liberalization will benefit both countries

- Because aviation is truly an **enabler** of future U.S.-China commerce, artificial restrictions serve neither side
- Experience shows us that “open skies” creates growth in the trade of services, new businesses, and jobs in **both** economies
- With 30 years of expertise in airline deregulation, U.S. firms can assist China in building a safe and prosperous aviation industry



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LET ME BEGIN WITH SOMETHING THAT IS SO OBVIOUS IT SOMETIMES ESCAPES US AVIATION TYPES, AND THAT IS THE OBSERVATION THAT AVIATION IS AN ENABLING INDUSTRY. MUCH LIKE TELECOMMUNICATIONS, COMMERCIAL AIR TRANSPORT OF PASSENGERS AND CARGO EXISTS PRIMARILY TO FACILITATE OTHER FORMS OF COMMERCE. NO ONE BUYS AN AIRPLANE TICKET JUST FOR THE SAKE OF DOING SO, THAT IS, WITHOUT A PURPOSE AT HIS OR HER DESTINATION; AND NO PACKAGE MOVES BY AIR WITHOUT SOME ULTIMATE COMMERCIAL USE. RESTRICTIONS ON AVIATION THEREFORE HAVE THE EFFECT OF SIGNIFICANTLY RESTRAINING OTHER FORMS OF COMMERCE. AND IT MAKES NO MORE SENSE TO CURTAIL THE NUMBER OF FLIGHTS BETWEEN TWO TRADING PARTNERS WHO ARE TRYING TO INCREASE AND IMPROVE THEIR ECONOMIC TIES THAN IT WOULD TO LIMIT THE NUMBER OF PHONE LINES BETWEEN THEM.

TODAY, IN MOST MAJOR INDUSTRIES, GOODS AND SERVICES ARE ALLOWED TO FLOW FREELY ACROSS NATIONAL BORDERS SO THAT COMPETITORS CAN ESTABLISH

A TRULY GLOBAL BRAND PRESENCE, EXPLOIT ECONOMIES OF SCOPE AND SCALE, RESPOND EFFECTIVELY TO CUSTOMER DEMAND AND TAP MARKET OPPORTUNITIES WHEREVER THEY ARISE. FREE TRADE IS BECOMING THE DEFAULT EVEN IN INDUSTRIES LONG THOUGHT ESSENTIAL TO OUR NATIONAL AND ECONOMIC SECURITY, SUCH AS AUTOMOBILES, FINANCIAL SERVICES, INFORMATION TECHNOLOGY, STEEL, AND PHARMACEUTICALS. IRONICALLY ENOUGH, HOWEVER, THE ONE INDUSTRY FOR WHICH FREE TRADE IS NOT YET THE STANDARD IS THE VERY INDUSTRY THAT HAS FACILITATED THE GLOBALIZATION OF ALL THE OTHERS – COMMERCIAL AVIATION. THAT’S BECAUSE MANY COUNTRIES STILL RESTRICT CARGO AND PASSENGER FLIGHTS ACROSS THEIR BORDERS THROUGH BILATERAL AVIATION AGREEMENTS THAT DOLE OUT AIRLINE RIGHTS SPARINGLY.

THIS NEEDS TO CHANGE IF AVIATION IS TO SERVE ITS RIGHTFUL PLACE AS A FACILITATOR OF ECONOMIC DEVELOPMENT. WORKING TOGETHER, THE U.S. AND CHINA HAVE THE OPPORTUNITY TO BRING ABOUT SUCH CHANGE. THE POSITION OF THE U.S. GOVERNMENT IS CLEAR: WE REMAIN COMMITTED TO PURSUING COMPLETE AIR SERVICES LIBERALIZATION WITH CHINA AND THE REST OF THE WORLD. OVER MORE THAN A DECADE, THE U.S. GOVERNMENT HAS SUCCESSFULLY NEGOTIATED “OPEN SKIES” AGREEMENTS WITH MORE THAN 70 COUNTRIES, INCLUDING MAJOR AVIATION MARKETS IN ASIA, EUROPE, AND ELSEWHERE. OPEN SKIES AGREEMENTS ARE AVIATION’S APPROXIMATION OF FREE TRADE AGREEMENTS AND ALLOW AIR CARRIERS OF EITHER SIGNATORY TO OFFER ANY TYPE OF AIR SERVICE (ROUTE, NUMBER OF SEATS, CODE SHARE SERVICE ETC) THAT THE MARKET DEMANDS AND AT ANY PRICE. THE CASE FOR OPEN SKIES IS MORE COMPELLING THAN IT WAS WHEN WE EMBARKED ON THIS ROAD NEARLY 18 YEARS AGO: EACH TIME THE UNITED STATES AND ANOTHER COUNTRY ARE ABLE TO ELIMINATE A LAYER OF

RESTRICTIONS AND ALLOW MARKET FORCES TO OPERATE, WE HAVE SEEN TANGIBLE EVIDENCE THAT STAKEHOLDERS ON BOTH SIDES ENJOY THE DIVIDENDS.

NOW, SOME OF OUR CHINESE BUSINESS COLLEAGUES MAY BE CONCERNED THAT A LIBERALIZED AVIATION AGREEMENT WITH THE UNITED STATES WILL SIMPLY PERPETUATE THE LEAD THAT U.S. CARRIERS CURRENTLY ENJOY IN PASSENGER TRAFFIC. U.S. CARRIERS DO TODAY ENJOY A COMPETITIVE ADVANTAGE IN CHINA DUE TO THEIR CUSTOMER AMENITIES, CARRIER ALLIANCES, FREQUENT FLYER PROGRAMS, AND WELL-ESTABLISHED DOMESTIC HUBS. THEREFORE, THE ARGUMENT GOES, LET'S KEEP PROTECTIONS IN PLACE INDEFINITELY, VERY GRADUALLY INCREASE THE NUMBER OF FLIGHTS AND THUS SHIELD CHINA'S THREE LARGEST CARRIERS FROM THE BRUNT OF COMPETITION.

BUT FOR TWO REASONS, PROTECTIONISM WILL NOT SERVE THE ECONOMIC INTEREST OF **EITHER** SIDE. FIRST, HISTORY HAS SHOWN THAT IT IS THE PRESENCE OF MORE COMPETITION, AND NOT BARRIERS TO COMPETITION, THAT WILL ACTUALLY STRENGTHEN THE QUALITY OF AIRLINE SERVICE AND MAKE AIRLINES MORE COMPETITIVE. YOU NEED ONLY LOOK AT THE U.S. ITSELF TO SEE THE PROFOUND BENEFITS TO CONSUMERS AND OUR ECONOMY CREATED BY A COMPETITIVE AIRLINE MARKET. AND EVERY TIME WE OPEN UP A NEW INTERNATIONAL MARKET, THE QUALITY OF SERVICE IN THAT MARKET IMPROVES.

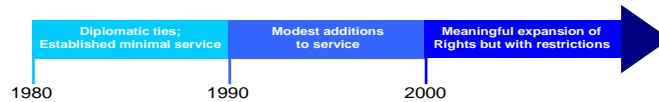
SECOND, AVIATION IS A HIGHLY COMPETITIVE AND DYNAMIC BUSINESS AND THERE IS ABSOLUTELY NO REASON TO BELIEVE THAT ANY ADVANTAGE BY U.S. CARRIERS WILL ENDURE. THIRTY YEARS OF DEREGULATION IN THE UNITED STATES HAVE TAUGHT US THAT COMPETITIVE ADVANTAGE IN THE AIRLINE BUSINESS IS NOT

PERMANENT. WHEN WE FIRST BEGAN DISCUSSIONS WITH CHINA OVER AIR SERVICES LIBERALIZATION, MORE THAN 25 YEARS AGO, OUR DOMINANT INTERNATIONAL CARRIERS WERE PAN AM AND TWA. THEY TOOK ADVANTAGE FOR AS LONG AS THEY COULD OF RESTRICTED INTERNATIONAL MARKETS BUT IT ULTIMATELY MADE THEM LESS COMPETITIVE AND RESPONSIVE TO FUNDAMENTAL MARKETPLACE DEVELOPMENTS. AND IN THE END EACH FAILED. INDEED, THE AIRLINE INDUSTRY IS ALMOST UNIQUE IN OFFERING START-UPS ESSENTIALLY NO BARRIERS TO ENTRY, IMMEDIATE DISTRIBUTION OF THEIR SERVICES TO MILLIONS OF CONSUMERS (THROUGH GLOBAL DISTRIBUTION SYSTEMS AND WEBSITES), AND READY ACCESS TO CAPITAL.

IF ANYTHING, VIGOROUS COMPETITION CREATED THROUGH AVIATION LIBERALIZATION SHOULD **BENEFIT** CHINESE CARRIERS, AS MUCH AS U.S. CARRIERS, BY FACILITATING ADDITIONAL ALLIANCES AND PROVIDING THE ECONOMIC INCENTIVE AND THE COMMERCIAL FLEXIBILITY TO ADAPT TO CHANGES IN THE GLOBAL MARKETPLACE. MARKET DEVELOPMENTS IN THE REST OF ASIA DEMONSTRATE THAT ASIAN CARRIERS CAN COMPETE VERY EFFECTIVELY IN OPEN MARKETS WITH U.S. CARRIERS AND, INDEED, GENERATE CUSTOMER LOYALTY EVEN AMONG U.S. ORIGINATING PASSENGERS.

The slow pace of liberalization

U.S.-China Bilateral Aviation Agreements



- 1980: Two airlines, four U.S. cities
- 1990s: One additional cargo route & one new airline for each side
- 2004: Few new entrants allowed with capacity limits in place to the major Chinese cities. Cooperative airline alliances restricted

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I MENTIONED EARLIER THAT CHINA AND THE U.S. FIRST BEGAN TALKING ABOUT AVIATION MORE THAN A QUARTER OF A CENTURY AGO. AS THIS CHART ILLUSTRATES WE HAVE MADE PROGRESS, BUT IT HAS NOT KEPT UP WITH THE DEMANDS OF THE GLOBAL MARKETPLACE. IN 1980 WE AGREED THAT TWO CARRIERS COULD ENTER THE MARKET SERVING JUST FOUR U.S. CITIES WITH TWO FREQUENCIES A WEEK. IT'S WORTH NOTING THAT ONE OF THOSE CARRIERS WAS PAN AM, WHICH AS I NOTED EARLIER, ULTIMATELY FAILED. THE NEXT DECADE SAW IMPROVEMENTS BUT ONLY IN VERY SMALL INCREMENTS; IT WASN'T UNTIL 1993 THAT THE U.S. DESIGNATED ITS FIRST CARGO CARRIER TO CHINA AND UNTIL 1999 THAT WE HAD ANY SUBSTANTIAL INCREASE IN FREQUENCIES. AND THEN OF COURSE FIVE YEARS LATER WAS THE 2004 PROTOCOL, WHICH PHASED IN ADDITIONAL RIGHTS OVER SIX YEARS, INCREASING FREQUENCIES FROM 54 TO 249 PER WEEK AND CARRIER DESIGNATIONS FROM FOUR (4) TO NINE (9) AND PERHAPS MOST SIGNIFICANTLY, AUTHORIZED THE ESTABLISHMENT OF CARGO HUBS IN CHINA BY U.S. CARRIERS. THIS WAS SIGNIFICANT PROGRESS, FOR WHICH WE THANK THE

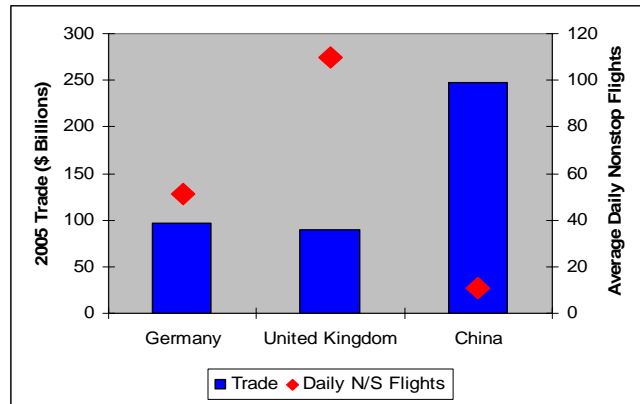
CHINESE, AND MY REMARKS TODAY ARE NOT MEANT TO DIMINISH THE IMPORTANCE OF THAT PROTOCOL. BUT WE DO BELIEVE MORE CAN AND SHOULD BE DONE.

Restrictions stifle commerce

U.S.-China capacity is plainly inadequate in light of the size of our trading relationship

Non Stop Daily Passenger Service:
Germany (open skies):
 55 flights
U.K. (restricted):
 116 daily flights
China (restricted):
 11 daily flights

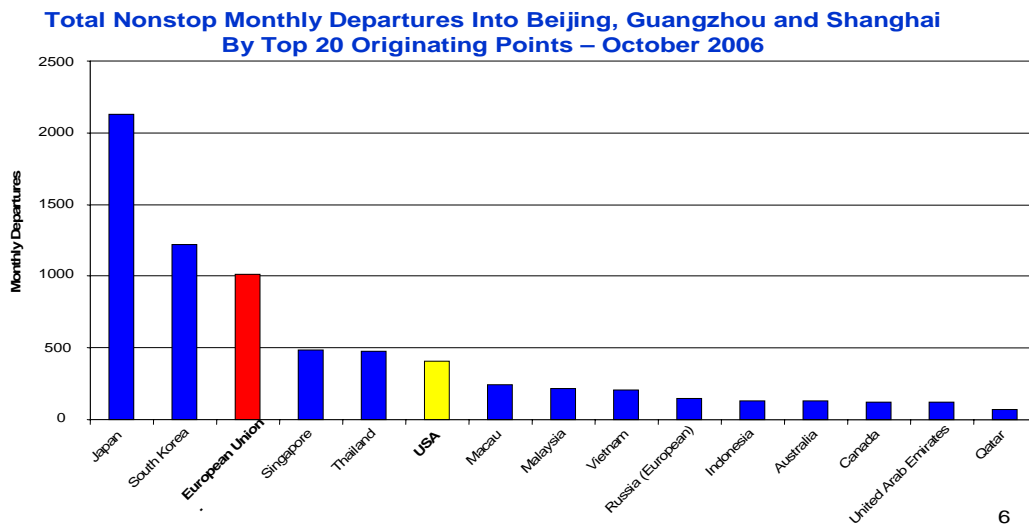
Source: Official Airline Guide, December 2006



HOW MUCH MORE DO WE NEED TO DO? WE THINK, A LOT. BETWEEN 2002 AND 2005 AVERAGE ANNUAL GROWTH IN PASSENGER DEMAND FOR NONSTOP U.S.-CHINA SERVICE WAS HIGH AT ALMOST 17 PERCENT, BUT THE BILATERAL RESTRICTIONS PREVENTED SUPPLY FROM MEETING THIS DEMAND. OVER THE SAME PERIOD THE NUMBER OF SEATS IN THE MARKET GREW AT A SLOWER RATE -- 13 PERCENT ANNUALLY. WITH ADDITIONAL RIGHTS FOR BOTH SIDES, OUR CARRIERS COULD ANSWER THIS GROWING DEMAND AND COMPETE ON A SERVICE BASIS BY OFFERING NONSTOP FLIGHTS CONNECTING ADDITIONAL U.S. CITIES TO AIRPORTS THROUGHOUT CHINA. CURRENTLY ONLY FOUR U.S. CITIES HAVE NONSTOP ACCESS TO CHINA AND, AS CARRIERS BUILD A TRAFFIC PRESENCE IN CHINA, FLIGHTS ARE HIGHLY CONCENTRATED IN THE KEY BEIJING AND SHANGHAI MARKETS.

BY ANY MEASURE, EVEN WITH THE PROGRESS MADE IN 2004, THE CURRENT BILATERAL AGREEMENT IS QUITE RESTRICTIVE. AS THIS CHART ILLUSTRATES, THE EXTREMELY LOW LEVEL OF DAILY PASSENGER FREQUENCIES FROM THE U.S. TO CHINA IS COMPLETELY OUT OF BALANCE WITH THE SIZE OF OUR OVERALL TRADING RELATIONSHIP. CURRENTLY THERE IS AN AVERAGE OF JUST 11 DAILY NONSTOP FLIGHTS BETWEEN THE UNITED STATES AND CHINA OFFERED BY ALL U.S. AND CHINESE AIRLINES COMBINED. BY CONTRAST, THERE ARE 55 DAILY FLIGHTS BETWEEN THE UNITED STATES AND GERMANY, AN OPEN SKIES COUNTRY WITH LESS THAN HALF THE U.S.- CHINA TWO-WAY TRADE. EVEN THE U.K., WHICH HAS A RESTRICTIVE AVIATION REGIME IN PLACE, ALLOWS TEN TIMES THE NUMBER OF FLIGHTS FROM THE UNITED STATES.

Fair Share?



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THE IMBALANCE OF TRADE AND AIR SERVICES IS ALSO REFLECTED WHEN YOU COMPARE THE U.S.-CHINA BILATERAL RELATIONSHIP TO WHAT CHINA NOW HAS IN PLACE WITH THE REST OF ITS TRADING PARTNERS. THIS CHART GRAPHICALLY ILLUSTRATES THE POINT AND FOCUSES ON TOTAL NONSTOP MONTHLY

DEPARTURES INTO THE THREE BIG CITIES – BEIJING, GUANGZHOU AND SHANGHAI FROM FOREIGN POINTS. THE DATA SPEAKS FOR ITSELF; THE U.S.-CHINA RELATIONSHIP LAGS FAR BEHIND THAT BETWEEN CHINA AND THE EUROPEAN UNION, SOUTH KOREA AND JAPAN AND IS EQUIVALENT ONLY WITH THE RELATIONSHIPS BETWEEN CHINA AND SIGNIFICANTLY SMALLER COUNTRIES. I HAVE TO TELL YOU – WHEN WE REVIEW THIS KIND OF DATA INSIDE THE U.S. GOVERNMENT AND WITH OUR CONGRESS – IT IS DIFFICULT TO EXPLAIN.

Restrictions lead to an imbalance that only benefits third countries

“U.S. carriers can’t expand their frequencies like this [near doubling of Korean Air flights] due to limited traffic rights. We have open skies with China and an enormous North American network. This gives us an edge and supports our goal of becoming the preferred airline to China.”

John Jackson, Marketing Director- North America, Korean Air, November 27, 2006



*Today 16% of U.S.-China passenger traffic
is being lost to third country airlines*

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WE NEED TO RECOGNIZE THAT BECAUSE AVIATION IS AT ITS CORE A **GLOBAL INDUSTRY**, LIBERALIZATION OF OUR INTERNATIONAL AVIATION REGULATORY SCHEMES IS NO LONGER A MATTER OF CHOICE. INDEED, AS LIBERAL AVIATION AGREEMENTS BECOME MORE COMMON, IT HAS BECOME IMPOSSIBLE FOR ANY COUNTRY TO PURSUE A PURELY DOMESTIC OR E VEN A BILATERAL AGENDA. GROWTH IN AIR TRAVEL IS DRIVEN BY GROWTH IN TRADE. NO COUNTRY CAN HALT

THE GROWTH OF INTERNATIONAL TRAFFIC —RESTRICTING TRAFFIC WITH ONE PARTNER SIMPLY BENEFITS ANOTHER.

AS WITH ANY MARKET, EVERY DAY WE LEAVE ARTIFICIAL RESTRICTIONS IN PLACE REPRESENTS ANOTHER DAY OF FOREGONE OPPORTUNITY AND LOST ECONOMIC VALUE. TRADING RESTRICTIONS IN AVIATION MARKETS HURT THE ABILITY OF RESTRICTED AIRLINES TO COMPETE MORE EFFECTIVELY IN WORLD MARKETS. WHILE IN EUROPE LAST YEAR I WAS IMPRESSED WITH THE AMOUNT OF ANIMATED DISCUSSION ABOUT THE ASTOUNDING GROWTH OF EMIRATES AIRLINES IN DUBAI. WHILE THERE ARE LOTS OF REASONS FOR ITS SUCCESS, THE FACT IS THAT ONE OF THEM IS THEIR ABILITY TO CREATE AND EXPAND A HUB IN A STRATEGIC LOCATION RELATIVELY FREE OF THE CUMBERSOME FREQUENCY AND DESTINATION RESTRICTIONS AFFECTING OTHER COUNTRIES. THUS, AN INDIRECT EFFECT OF THE ANACHRONISTIC TRADING RESTRICTIONS IN PLACE BETWEEN THE U.S. AND E.U. HAS BEEN THE FACILITATION OF A STRONG NETWORK COMPETITOR OUTSIDE THE BORDERS OF BOTH.

NOW THE SAME THING IS OCCURRING ON THIS SIDE OF THE PACIFIC AS THIS CHART INDICATES. CHINA HAS ENTERED INTO LIBERAL AVIATION AGREEMENTS -- WITH FEW OR NO RESTRICTIONS -- WITH KEY ASIAN PARTNERS OF THE UNITED STATES, SUCH AS SOUTH KOREA, SINGAPORE, AND JAPAN. THE U.S. FOR ITS PART ENJOYS OPEN SKIES WITH KOREA AND SINGAPORE AND MATERIALLY MORE SERVICE TO JAPAN THAN IT HAS WITH CHINA. THE RESULT?

AS YOU CAN SEE FROM THIS ILLUSTRATION, RESTRICTIONS ON U.S. AND CHINESE CARRIERS DON'T REDOUND TO EITHER COUNTRY'S BENEFIT. THEY SIMPLY SHIFT

THE TRAFFIC, AND WITH IT THE COMMERCIAL OPPORTUNITIES, TO THIRD COUNTRY CARRIERS. THAT'S WHY KOREAN AIR LINES, AS SUGGESTED BY THE QUOTATION IN THE ABOVE SLIDE, IS POSITIONED TO ACHIEVE ITS GOAL TO BECOME THE PREFERRED AIRLINE CONNECTING NORTH AMERICA TO CHINA. BY OUR ESTIMATE AT LEAST 16 PERCENT OF THIS O&D TRAFFIC MOVES OVER THIRD COUNTRIES. AND EVERY LIBERALIZED AGREEMENT THAT CHINA SIGNS WITH ANOTHER ASIAN PARTNER SIMPLY EXACERBATES THIS IMBALANCE. WE CAN'T SEE HOW ALLOWING THIS SITUATION TO CONTINUE IS GOOD FOR CHINESE OR U.S. CARRIERS – MUCH LESS THE CITIZENS AND BUSINESSES OF EITHER COUNTRY.

Aviation liberalization will reduce our trade imbalance



Export of U.S. professional services assists both Chinese businesses and those sectors where American firms excel

-- Examples: banking, consulting, communications, accounting

Expands travel and tourism – world's largest industry

- Drives more than 10% of global economic activity
- U.S. & China are the world's 3rd & 4th largest tourist destinations respectively



Each new wide-body flight from the United States generates a huge benefit for China:

- \$2,310 per passenger (estimated)
- \$585,000 per plane (estimated)
- **\$213,000,000 per year in economic activity**



Source: Booz Allen Hamilton Study, 1999 assuming a United Boeing 747-400 aircraft at a 73% load factor

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LAST YEAR, THE U.S. AND CHINA BEGAN A STRATEGIC ECONOMIC DIALOGUE, WHICH WILL COVER A WIDE RANGE OF ISSUES DESIGNED TO ENHANCE AND DEEPEN THE TRADE RELATIONSHIP. THE DIALOGUE WAS LAUNCHED BY PRESIDENTS BUSH AND HU AS AN OVERARCHING FORUM FOR DISCUSSING WAYS THE U.S. AND CHINA CAN WORK TOGETHER TO ENSURE THAT CITIZENS IN BOTH COUNTRIES BENEFIT FAIRLY

FROM OUR GROWING BILATERAL ECONOMIC RELATIONSHIP. THE FIRST MEETING OF THE S.E.D. AS IT IS KNOWN TOOK PLACE IN DECEMBER OF LAST YEAR, AND WAS LED BY SECRETARY OF THE TREASURY HANK PAULSON FOR THE U.S. SIDE AND VICE PREMIER MADAME WU YI FOR THE CHINESE SIDE. I WAS HONORED TO REPRESENT SECRETARY OF TRANSPORTATION MARY PETERS AT THIS EVENT.

THE TWO COUNTRIES ARE DISCUSSING A RANGE OF ISSUES INCLUDING HOW TO ASSURE SUSTAINABLE GROWTH, CHINA'S ECONOMIC DEVELOPMENT AND FURTHER INTEGRATION INTO THE WORLD TRADING SYSTEM, STABLE ENERGY MARKETS, AND COOPERATION ON BEST PRACTICES IN SOCIAL SERVICES AND THE ENVIRONMENT. RECOGNIZING THAT TRANSPORTATION IS A FUNDAMENTAL 'ENABLER' OF THE ECONOMIC RELATIONSHIP BETWEEN OUR TWO COUNTRIES, BOTH SIDES AGREED TO RESUME AVIATION TALKS, BRINGING US HERE THIS WEEK.

WE THINK A LIBERALIZED AVIATION RELATIONSHIP CAN HELP TO REDUCE THE TRADE DEFICIT BETWEEN THE UNITED STATES AND CHINA, WHICH THIS YEAR IS ON PACE TO SET A NEW RECORD OF MORE THAN \$225 BILLION AND IS FUELING DANGEROUS PROTECTIONIST SENTIMENTS IN THE UNITED STATES. HERE'S WHY: THE U.S. CURRENTLY ENJOYS A TRADE SURPLUS WITH CHINA IN PROFESSIONAL SERVICES; THAT'S NOT SURPRISING, AS THE UNITED STATES IS BECOMING OVERWHELMINGLY A SERVICES-BASED ECONOMY. IT'S PART OF NATURAL ECONOMIC EVOLUTION. BUT OBVIOUSLY PROFESSIONAL SERVICES CAN'T BE DELIVERED IN CARGO CONTAINERS; THEY ARE DELIVERED IN PERSON. MAKING IT MORE CONVENIENT AND LESS EXPENSIVE FOR U.S. PROFESSIONAL SERVICE FIRMS TO TRAVEL BACK AND FORTH TO CHINA WILL HELP SPUR ADDITIONAL GROWTH IN OUR SERVICES EXPORTS AND BROADEN OUR TRADE RELATIONSHIP.

MOREOVER, TRAVEL AND TOURISM IS THE WORLD'S LARGEST INDUSTRY – AND CHINA AND THE UNITED STATES ARE SIGNIFICANT DESTINATIONS -- AND OBVIOUSLY MORE AIRLINE FLIGHTS IN BOTH DIRECTIONS WILL CONTRIBUTE TO REVENUE GROWTH THERE AS WELL. FORTUNATELY, THIS IS A CLASSIC “WIN – WIN” FOR OUR ECONOMIES. WE MUST RECOGNIZE THAT TRAVELERS TO CHINA ARE GOING THERE TO DO BUSINESS OR ENJOY THE BEAUTIFUL TOURIST ATTRACTIONS CHINA HAS TO OFFER. CLEARLY, MORE FLIGHTS WILL NOT ONLY HELP REDUCE THE TRADE DEFICIT BUT ALSO BENEFIT CHINA. IN FACT, EACH NONSTOP DAILY FLIGHT FROM THE UNITED STATES TO CHINA IS ESTIMATED TO RESULT IN \$213 MILLION IN INCREMENTAL REVENUE AT THE DESTINATION.

Increased international service fuels regional development



- Produces large economic multipliers
 - Every \$1 spent in aviation results \$5 in US economic activity
 - One aviation job supports, directly and indirectly, ten jobs elsewhere

- Hub & spoke networks developed after U.S. deregulation often centered in secondary cities
- Serve as a catalyst to regional growth
 - Example: US Airways hub in **Charlotte, North Carolina** generates up to \$10 billion per year, supports 100,000 jobs
 - Charlotte was once largely reliant on agriculture and is now a booming regional financial center
- Aviation hubs are key to an environmentally friendly and fuel efficient mass transportation network



North Carolina- Agriculture



North Carolina- Financial Center

WE ALSO BELIEVE THAT MORE INTERNATIONAL SERVICE FROM THE UNITED STATES THROUGH A LIBERAL AVIATION RELATIONSHIP WILL ASSIST THE CHINESE IN THEIR OWN LAUDABLE EFFORTS TO PROMOTE REGIONAL DEVELOPMENT. WE

HAVE DIRECT EXPERIENCE WITH THIS: NOT ALL THAT LONG AGO AIRLINES IN THE UNITED STATES VOCALLY OPPOSED OPEN SKIES; THEY SAW FOREIGN CARRIERS AS A THREAT AND WANTED THE U.S. GOVERNMENT TO PROTECT THEM FROM COMPETITION. BUT SOMETHING ALTERED THE DYNAMIC: IT WAS THE COLLECTIVE EFFORTS OF AIRPORTS AND LOCALITIES THAT HELPED TO OVERCOME THE OPPOSITION. SOME OF YOU MAY RECALL THE 'CITIES' PROGRAM THAT WAS PROPOSED BY FORMER DOT SECRETARY SKINNER. THE IDEA WAS SIMPLE: IF AN AIRLINE FROM A LIBERAL TRADING PARTNER WANTED TO SERVE A CITY NOT LISTED IN THE GOVERNING BILATERAL AND NO U.S. CARRIER WANTED TO SERVE THE ROUTE, THEN THE DEPARTMENT WOULD PERMIT THE SERVICE WITHOUT NEED FOR FURTHER NEGOTIATION. I THINK THE CITIES PROGRAM LED THE DEPARTMENT TO RECOGNIZE CITIES AS ECONOMIC BENEFICIARIES OF AND IMPORTANT ALLIES IN OUR PURSUIT OF LIBERALIZED AVIATION MARKETS.

A LIBERALIZED U.S.-CHINA AVIATION AGREEMENT THAT COMES OUT OF THE STRATEGIC TRADE DIALOGUE AND THIS WEEK'S NEGOTIATIONS WOULD PERMIT AIRLINES TO RESPOND TO MARKET DEMAND AND INCREASE THEIR COMPETITIVENESS IN WORLD MARKETS. ADDITIONAL AIR RIGHTS TO CHINA WOULD ALLOW U.S. AIRLINES TO ADD NONSTOP SERVICE FROM SOME OF THE MANY U.S. CITIES THAT ARE EAGER FOR AIR LINKS TO CHINA. THIS SERVICE IN TURN WOULD SUPPORT THROUGH OR BEYOND TRAFFIC FROM CHINA'S MAJOR CITIES TO WESTERN PARTS OF THE COUNTRY, MAKING CHINESE HUB AND SPOKE NETWORKS MORE PROFITABLE AND ENCOURAGING U.S. BUSINESSES TO PARTICIPATE IN CHINESE ECONOMIC DEVELOPMENT IN THE INTERIOR.

AS THIS SLIDE INDICATES, THIS WAS OUR OWN EXPERIENCE IN THE UNITED STATES. FOLLOWING DEREGULATION AS FLIGHTS INCREASED FROM MAJOR CITIES TO OTHER DESTINATIONS, AIRLINES FOUND IT MADE SENSE TO OPERATE REGIONAL HUBS. THESE HUBS IN TURN REPRESENTED AN ECONOMIC BONANZA FOR THE CITIES WHERE THEY WERE LOCATED. AND WE SAW PLACES LIKE CHARLOTTE, NORTH CAROLINA SUBSTANTIALLY ADVANCE THEIR OWN ECONOMIC PROGRESS, MIGRATING FROM AN AGRICULTURALLY BASED ECONOMY TO A BOOMING FINANCIAL CENTER.



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OUR NEGOTIATIONS THIS WEEK TOWARD A POSSIBLE BREAKTHROUGH AVIATION AGREEMENT WITH CHINA COULD BRING AN ENTIRELY NEW LEVEL OF LIBERALIZATION TO TRANS-PACIFIC AIR SERVICES. WE WANT TO CONCLUDE THAT AGREEMENT – NOT ONLY FOR THE MARKET ACCESS THAT OUR CARRIERS WILL ACHIEVE, BUT BECAUSE IT CAN BE EXPECTED TO ENHANCE THE QUALITY OF COMPETITION ACROSS THE PACIFIC IN A DRAMATIC WAY. A BILATERAL AGREEMENT BETWEEN THE U.S. AND THE PEOPLE'S REPUBLIC OF CHINA WOULD BRING 1.7

BILLION PEOPLE UNDER A SINGLE LIBERALIZED REGIME. IT WOULD TAKE LIBERALIZATION TO THE NEXT LEVEL, LINKING TWO HUGE MARKETS AND ALLOWING AIRLINES FROM BOTH SIDES OF THE PACIFIC UNPRECEDENTED FLEXIBILITY IN HOW THEY BUILD, MANAGE, AND EXPAND THEIR OPERATIONS. AND IT WOULD DEMONSTRATE TO THE REST OF THE WORLD THAT THE U.S. AND CHINA ARE COMMITTED TO A HARMONIOUS AND PROSPEROUS FUTURE.

THANK YOU FOR LISTENING, AND I WOULD BE PLEASED TO TAKE ANY QUESTIONS.