Chapter 3
The Marketing Environment

Abstract The tourism marketing environment consists of internal and external forces which could impact the organisations' performance. To be successful, companies must adapt to ongoing trends and developments in their macro and micro environments. When organisations scan their marketing environment they will be in a position to deal with any possible threats from the market and to capitalise on any available opportunities. Therefore, this chapter explains the external environmental factors, including; political, economic, social and technological influences. It also considers the internal environmental factors, including; capital structures, resources, capabilities and marketing intermediaries; as it identifies competitive forces from differentiated or low-cost service providers.

3.1 Introduction

A sound knowledge of the customer requirements is an essential ingredient for a successful business. For this reason, companies should consistently monitor their marketing environment. The marketing environment is continuously changing, as it consists of a number of unpredictable forces which surround the company.

As well as conducting a thorough analysis of the actual marketing environment, the businesses must investigate the conditions in which they operate. The regulatory and competitive conditions as well as other market forces, including; political, economic, social and technological forces, could affect the organisational performance of the tourism businesses. Hence, this chapter will look into some of these issues. The tourism industry is highly influenced by economic factors, including; strong exchange rate fluctuations, the price of oil and other commodities, among other matters. Moreover, social factors including global concerns about safety and security could influence tourist behaviours. Notwithstanding, the regulatory environments will also have an impact on tourism and airline businesses (Belobaba, Odoni & Barnhart, 2015). For instance, the airline industry's deregulation and liberalisation has created numerous opportunities for many airlines, including

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low-cost carriers. At the same time, it has threatened inefficient airlines who have been protected by regulation.

Undoubtedly, competition is a vitally important element in the marketing environment and it should not be under-estimated. The businesses competitors comprise suppliers of substitute products. They may be new entrants in the marketplace. Alternatively, they may include customers and suppliers who were stakeholders of the business. In this light, tourism marketers should be knowledgeable of different business models as competition can take different forms, like for example, differentiated, full-service companies or low-cost service providers. For these reasons, organisations should have effective mechanisms to monitor the latest developments in the marketing environment.

3.2 Environmental Scanning

Environmental scanning entails the collection of information relating to the various forces within the marketing environment. This involves the observation and examination of primary and secondary sources of information, including online content from business, trade, media and the government, among others. The environmental analysis is the process of assessing and interpreting the information gathered. An ongoing analysis of the gathered data may be carried out by marketing managers or by researchers who have been commissioned to conduct market research (as explained in the previous chapter). Through analysis, marketing managers can attempt to identify extant environmental patterns and could even predict future trends. By evaluating trends and tendencies, the marketing managers should be able to determine possible threats and opportunities that are associated with environmental fluctuations. When discussing the 'marketing environment' we must consider both the external environment (i.e. the macro-environment) as well as the internal environment (i.e. the micro-environment) (Kotler, Armstrong, Frank & Bunn, 1990).

3.3 The Macro Environment

The tourism businesses must constantly assess the marketing environment. It is crucial for their survival and achievement of their long-term economic goals. Therefore, marketing managers must engage in environmental scanning and analysis. Most firms are comfortable assessing the political climates in their home countries. However, the evaluation of political climates in foreign territories is far more problematic for them. Experienced international businesses engage in political risk assessment, as they need to carry out ongoing systematic analyses of the political risks they face in foreign countries. Political risks are any changes in the political environment that may adversely affect the value of any firm's business activities. Most political risks may result from governmental actions, such as; the passage of laws that expropriate private property, an increase in operating costs, the devaluation of the currency or constraints in the repatriation of funds, among others. Political risks may also arise from non-governmental actions when there is criminality (for example: kidnappings, extortion and acts of terrorism, et cetera). Political risks may equally affect all firms or may have an impact on particular sectors, as featured in Table 3.1. Non-governmental political risks should also be considered. For example, Disneyland Paris and McDonalds have been the target of numerous symbolic protests by French farmers, who view them as a convenient target for venting their unhappiness with US international agricultural policies. In some instances, protests could turn violent, and may even force firms to shut down their operations, in particular contexts.

International corporations who intend investing in different markets should consider asking these simple questions: Is the host country business-friendly? Is its government a democracy or a dictatorship? Is the authoritative power concentrated in the hands of one person or on one political party? Does the country rely on the free market or on governmental controls to allocate resources? How much of a contribution is the private sector expected to make in helping the government achieve its overall economic objectives? Does the government view foreign firms as a means of promoting or hindering its economic goals? When making changes in its policies, does the government act arbitrarily, or does it rely on the rule of law? How stable is the existing government? If it leaves office, are there going to be any drastic changes in the economic policies of the new government? Firms should always contemplate (research) these issues before entering into a new market. They should be knowledgeable about the host country's political and economic structures, in order to minimise uncertainty and unnecessary risks. Appendix 1. provides a good background on the aviation industry's regulatory environment.

Table 3.1 Typical examples of political risks

Type	Impact on firms
Expropriation	Loss of future profits
Confiscation	Loss of assets, loss of profits
Campaigns against businesses	Loss of sales; increased costs of public relation; efforts to improve public image
Mandatory labour benefits legislation	Increased operating costs
Kidnappings, terrorist threats and other forms of violence	Increased security costs; increased managerial costs; lower productivity
Civil wars	Destruction of property; lost sales; increased security costs
Inflation	Higher operating costs
Repatriation	Inability to transfer funds freely
Currency devaluations	Reduced value of repatriated earnings
Increased taxation	Lower after-tax profits

A PEST analysis (political, economic, social and technological) provides a useful framework to analyse macro-environmental factors. The businesses should carefully analyse these issues before considering their expansion in a different country through foreign direct investment.

3.3.1 Political, Legal and Regulatory Issues

The political analysis relates to how governments influence the companies' strategy and operations. The political environment encompasses laws, government agencies and pressure groups which could have an effect on tourism organisations and entrepreneurs. Such factors include; national politics on financial matters, including; foreign debt, and the rates of inflation (i.e. increase in prices), recession; policies and regulatory legislation on reciprocal trade and foreign investment; travel restrictions, the governments' tourism policies; as well as ecological considerations, among other issues.

Political, legal and regulatory issues can affect the viability of tourism firms. Therefore, any prospective changes in the governments' priorities (for example; public spending) or a change in government can lead to the opening-up or the closing of markets. The business activity tends to grow and thrive when a nation is politically stable. National governments and their legal systems could could facilitate or hinder businesses, in many areas. Therefore, any political changes are closely related with the legal and economic matters (for example: employment laws, minimum wage laws, health and safety laws, zoning regulations, environmental protection laws, consumer protection laws, tax laws, et cetera). For instance, new European Union regulations have led to greater levels of competition in European aviation. However, many stakeholders are concerned about the environmental impact from airlines.

Many nations are increasingly encouraging free trade by inviting firms to invest in their country, whilst allowing their domestic firms to engage in overseas business. These nations may decide not to impose conditions on imports, or they would not discriminate against foreign-based firms. On the other hand, there are other governments who may oppose free trade. The most common form of trade restrictions is the tariff, (i.e. a tax that is placed on imported goods). Tariffs or levies are usually established to protect domestic manufacturers against competitors by raising the prices of imported goods. Multinational firms may face the risk of expropriation. This happens when the government will take ownership of land, buildings and/or other fixed assets; sometimes, without compensating the rightful owners for their loss. When there is the risk of expropriation, multinational firms will be at the mercy of foreign administrations. Unstable governments may have the authority to change their laws and regulations at any point in time, to meet their needs.

Very often, the best sources of information are their own employees. Whether they are citizens of the business' home country or of their host country, employees possess first-hand knowledge of the local issues, and are a valuable source of risk information. The views of local staff should be supplemented with the views from outsiders. The government, embassy officials and the international chamber of commerces are often rich sources of information. Many governments will usually signal their economic and political agendas during their political campaigns before being elected in parliament. Once in office, several governments continue to provide useful information about their current and future plans. Moreover, numerous consulting firms specialise in political risk assessment. Their role is to assist those firms who are considering foreign direct investment, those who would like to penetrate into a particular market. To reduce the risk of foreign operations, many developed countries have created government-owned or government-sponsored organisations which insure firms against political risks. For instance, the Overseas Private Investment Corporation (OPIC) insures US overseas investments against nationalisation. The Multilateral Investment Guarantee Agency (MIGA), a subsidiary of the World Bank provides similar insurance against political risks. Private insurance firms such as Lloyds' of London also underwrite political risk insurance.

3.3.2 The Economic Issues

The economic analysis will involve an examination of the foreign countries' monetary, fiscal and economic policies. The factors affecting consumer purchasing and spending patterns, include; wealth per capita; discretionary income; industrial development; currency restrictions; balance of payments; leave of imports/exports; fluctuations in interest and foreign exchange rates, among other issues. The exchange rate of a country's currency represents its value in relation to that of another country's currency. Currency rates fluctuate on a daily basis, thus creating high risks for many industries, including the travel and hospitality sectors. Tourism businesses will be more encouraged to expand and to take calculated risks when economic conditions are right. For example, when there are low interest rates, and when they are experiencing rising demand. Rising incomes and higher standards of living have often translated to more disposable money on luxuries like; long-haul travel and other hedonic behaviours.

3.3.3 Social Issues

A social analysis delves into societal behaviours, customs, values, norms, lifestyles and preferences. Demographic factors, including the age structure of the population may also change, over time (for example, there are many developed countries that are already having an ageing population). Moreover, social issues could also comprise the cultural environment, which is influenced by the individual populations' size, race, religious beliefs, gender, family, education, occupation, and the individuals' position in the social stata, among other variables. Institutions could influence society's basic values, perceptions and preferences. For instance, there may be changes in consumer behaviours which could be attributed to trending fashions and styles. Climate and seasonal variations could also affect consumer behaviours, and their travelling propensity. Of course, there may be other factors that could affect the consumers' inclination to travel, including; credit facilities and attitudes, competition from other spending behaviours, et cetera. In addition, social issues may also relate to distances to be travelled; urban versus rural lifestyles and attitudes to travel; emigration, school vacation periods, perceptions on international commuting, et cetera.

Tourism marketers ought to be sensitive to different social issues. A good understanding of societal changes could help them position their business, and to anticipate market demands. For the time being, many countries are experiencing a surge in popularity, particularly in short-break itineraries. This has inevitably led to a boom in demand for tourism products in the off-peak and low seasons. At the same time, **a**irports and airlines are striving in their endeavours to improve their levels of security, in the wake of the latest terrorist attacks. Currently, there is also the possibility that the U.S. government could ban laptops from aircraft. Other social factors that must be taken into consideration, include; civil wars, assassinations or kidnappings of foreign people. These contingent matters are equally dangerous for the viability of the tourism firms' operations.

3.3.4 Technological Issues

A technological analysis is required as marketers need to keep themselves up-to-date with the latest innovations in the tourism industry. Like any other business, the tourism firms, including airlines are effected by new technologies, which could create new products and market opportunities (Tussyadiah, & Inversini, 2015). For example, larger and faster aircraft which are more pleasing to the customer, as well as airport+ developments and their facilities, including; efficient check-in desks; lounges, shuttles and online travel booking sites, among other things, have surely improved the customer experience. Moreover, recently there have been a number of interesting developments in the field of airport security. The need for quicker, seamless processing and baggage checks has led the Transportation Security Administration (TSA) to explore the possibility of new security lanes. There have also been significant efforts to improve the accuracy of threat detection. New emerging technologies are providing better security, but can also help to enhance the passenger experience. Recently, many airlines are also considering the introduction of facial recognition devices that may be used for the boarding of passengers.

The rapid pace of technological change has been forcing travel and tourism businesses to spend heavily to remain on the cutting edge. This way they could better serve their customers. In the 90 s, many full-service, legacy airlines have introduced elaborate reservation systems which enabled them to improve their services to passengers. Subsequently, they introduced big data, analytics and customer relationship management systems that have improved their customer-centric approaches. In addition, many airlines, particularly, the full-service carriers have established sophisticated frequent flyer programmes, as they forged industry partnerships and/or code-sharing agreements with other carriers.

Recently, the uses of digital media, electronic databases and interactive communications have enabled vast quantities of information to be shared and distributed online, in an efficient manner. Tourism marketers are increasingly using technology to improve the standards of service. Several innovative destination management organisations (DMOs) are utilising a range of smart technologies to improve their customer service levels. For instance, KTO Tourist Information Centre (TIC) of Seoul, in South Korea, has adopted a mix of information, communication technologies (ICTs), including a visitor website with an interactive map featuring pre-arrival information. Facebook, Twitter, Instagram and Snapchat are being used by marketing and public relations executives for customer engagement and wide array of mobile application are being used by many travellers. For instance, the city of Montreal Tourist Office promotes its attractions through an interactive video that provides virtual experiences to tourists; while, Las Vegas Tourism Office provides personalised itineraries and Tourism New Zealand have come up with an interactive trip planner with customisable maps, price ranges and activities. Tourism businesses are increasingly expected to be knowledgeable and proficient in the use of internet (Buhalis & Law, 2008). The ongoing developments in technology and the proliferation of ubiquitous media and mobile communications have affected tourism businesses, in many ways. Many customers and prospects are using interactive media to engage with the business in two-way communications. They may also get involved in electronic word-of-mouth publicity (which can be either positive or negative) in social media, and by using review and rating sites like TripAdvisor or Yelp.

3.4 Micro Environment

Many travel and tourism businesses are continuously monitoring the countries' political, economic, social and technological changes to reduce their risks. However, the external environmental forces will also affect the organisations' micro environment. The micro environment consists of forces which are close to the companies themselves, forces which will affect their ability to serve customers. These forces include the organisations' capital structure, resources, capabilities of management and staff, companies' aims and objectives, the companies' marketing intermediaries, customer markets, competitors and all other stakeholders that may have an interest or an impact on the organisations' ability to achieve their objectives (for example, financial, media and government stakeholders, among others).

3.4.1 Capital Structure

The organisations' capital structure and how finance is allocated across departments and units will have an effect on the companies' marketing programmes.

3.4.2 Resources

The firms' specific assets are useful for creating a cost or differentiation advantage over other competitors. The organisations' resources may include; patents and trademarks, intellectual capital, installed customer bases, reputation and brand equity, among others. For example, the size and type of fleet of aircraft that are owned and controlled by airlines will determine the type of service which they can offer to the market.

3.4.3 Capabilities

The firms' ability to utilise resources is one of their capabilities. When organisations introduce a product to the market before their rivals, they will achieve a competitive advantage. Such capabilities may be embedded in organisational routines and may not be documented as strategic procedures. Moreover, the organisations' structures and the leadership of their various departments, and the relationship between management and staff may not be easily replicated by other businesses. The competitors may not always be in a position to mimic the capabilities of successful businesses.

The firms' resources and capabilities together form their distinctive competences. These competences enable innovation, efficiency, quality and customer responsiveness; all of which can be leveraged to create cost or differentiation advantages.

3.4.4 Company Aims and Objectives

When companies decide which market segments to target, they must carefully evaluate their internal strengths and weaknesses, and communicate their value propositions to their chosen markets.

3.4.5 Marketing Intermediaries

Marketing intermediaries are firms which help companies to promote, sell and distribute their goods or services to customers. When discussing about the tourism industry, tour operators and travel agents will usually act as intermediaries. Therefore, travel and hospitality businesses, including airlines and hotels, need to develop a sound relationship, loyalty and a strong bargaining power with tour operators, travel agents to sell their products. Moreover, the tourism industry and its distribution network are exposed to a number of changing internal and external environmental forces (these have been mentioned in the previous sections). With technological developments, there may be variations in economies and consumers could become more sophisticated and demanding. For example, today's customers have access to price comparison web sites, like; Google Flights, Kayak, Momondo, TravelSupermarket.com, Expedia, et cetera.

3.5 Identifying Competition

An adequate knowledge and understanding of competitive trends in the market place is necessary, as competition is a vitally important element in the marketing environment (Kotler et al. 1990). The competitive forces determine whether there is profit potential for a specific industry. The starting point of the competitive analysis is the identification of competitors. Porter (1979) identified five forces that govern industry competition: the threat of new entrants; the bargaining power of suppliers; current competitors; the bargaining power of customers; and the threat of substitute products or services. According to Porter (1979), the key to growth and survival, is to use one's knowledge of these five forces to "stake out a position that is less vulnerable to attack from head-to-head opponents, whether established or new, and less vulnerable to erosion from the direction of buyers, suppliers, and substitute goods." Such a position, he argues, can be gained by solidifying relationships with profitable customers, by integrating operations, or by gaining technical leadership.

In the tourism industry, the suppliers of tourism amenities can exert pressures over other businesses. For instance, these suppliers may refuse to work with the firm or they may charge excessively, high prices for their services. In this day and age, digital media has facilitated offline and online sales as it has provided a platform for interactive communications between businesses and their customers. Moreover, the competition from new entrants has also posed significant threats to businesses (Schegg & Stangl, 2017). The profitable markets that yield high returns will obviously attract new firms. The arrival of new competitors could eventually decrease the profitability for all other incumbent firms within the industry.

For example, the airline industry is a growing one, and extant carriers who fail to enhance their route network may be bypassed by competing airlines (Belobaba et al., 2015). There may be a number of national or low-cost carriers who may be competing for the same customers, on the same route. Furthermore, the bargaining power of customers could also exert pressure on businesses. If a large number of customers ask for lower prices from companies, they will have no other choice but to succumb to their requests. On the other hand, the buyer power is low when the customers act independently. The buyer power is high if the customers have a wide selection of service providers to choose from. When customers are buying in large quantities from a supplier; a temptation exits for the customers to move back along the chain, to become direct competitors with the supplier, rather than to remain their customers. This may be the case for those established tour operators who frequently block pre-negotiated carrier seats or hotel rooms. These travel organisations have grown to a point where it would be more viable and secure for them to set up their own airline or hotel properties. Consequently, they will find themselves competing with the travel and tourism business that originally supplied them.

3.5.1 Analysing Competition

A competitor analysis involves an assessment of the strengths and weaknesses of current and potential competitors. This analysis provides an offensive and defensive strategic context to identify opportunities and threats in the marketplace. Travel and tourism business could profile their competitors into one framework. They need to identify who their competitors are and to determine their strengths and key success factors (for example, the provision of high quality services, low-cost operations, route networks, convenient timings, good onward connections, et cetera). They should also acquire knowledge on their customers' needs and wants (for example, business or leisure passengers), including the value propositions that they may offer them (as discussed in Chap. 2).

The generic competitive strategies of cost leadership, differentiation and focus are conspicuous in the airline industry. The legacy carriers usually provide higher quality services as they typically offer first class and business class seating, frequent-flyer programmes, and are usually characterised by their exclusive airport lounges. Also, legacy carriers generally have better cabin services, including; meal services and inflight entertainment. Whereas, the low-cost carriers (LCCs), which are also known as no-frills, discount or budget carriers may usually offer lower fares and fewer comforts. To make up for the revenue lost in decreased ticket prices, the LCCs will probably charge for extras such as food, priority boarding, seat allocating, and baggage.

Several legacy carriers are also members of established airline networks and alliances that include; Star, Oneworld or SkyTeam alliances. During the last twenty years, there were some major mergers and acquisitions among traditional airlines. For instance, in 2015, American Airlines' has merged with US Airways; AirTran merged with Southwest a year before, United joined Continental in 2010; and Northwest become part of Delta, back in 2008. These airline mergers have resulted in the consolidation of resources, improved efficiencies, in terms of economies of scale and scope, thereby reducing costs for the new conglomerates. For instance, American Airlines' merger with US Airways has yielded an annual savings of up to $1.5 billion. Yet, these mergers have often led to reduced competition, higher fares, crowded planes and added baggage fees, at the detriment of customers.

3.5.1.1 Legacy Versus Low-Cost Carriers

Even with their rich history, the legacy airlines had to evolve over time to adapt to the changing regulatory, economic and technological forces that have shaped the aviation industry. The legacy carriers had to compete in turbulent marketplaces, as LCCs have shaken up many markets. The arrival of the low-cost airlines has resulted in a reduction in air fares as these 'no-frills' airlines have cut on-board perks and introduced inclusive extras for their passengers. For example, their passengers are charged for check-in baggage, limited weight allowance for checked luggage, early boarding, seat allocation and the like.

Very often these developments have affected the quality of airline services. In fact, many national airlines are increasingly mimicking low-cost models. For example, KLM and British Airways have introduced checked-baggage fees on their European routes. Such fees were associated with budget airlines like EasyJet and AirAsia. Moreover, several traditional airlines have discontinued the provision of complimentary, inflight meals on short-haul flights. Several European flag carriers, including Aer Lingus and Iberia, sell food and beverage on board. Some of the legacy airlines are even charging their passengers for seat reservations and seat allocations. According to KPMG, these initiatives have reduced the legacy carriers' cost disadvantages against low-cost airlines by more than a third. Apparently, legacy airlines are abandoning old differentiators like free baggage and inflight catering, particularly in their short-haul flights. The service that is being offered by both low-cost and legacy carriers is becoming more or less the same.

Legacy carriers are frequently outsourcing short-haul traffic to specialised regional airlines. They may only offer multiple classes of service including business and first class in medium and long-haul flights. However, there are more travellers using airline services, year after year. This may be due to the fact that the travellers are increasingly availing themselves of the low fares that are being provided by different airlines (including legacy carriers). At the same time, the business travellers are increasingly becoming price-sensitive. In fact, many of them are also travelling on LCCs. Yet, the airlines' low prices are negatively affecting their bottom lines.

3.6 Questions

- *An airline marketing manager must have a sound knowledge of the airline marketing environment. Why?*

- *Explain environmental scanning. Outline its importance to travel and tourism marketers?*
- *Identify the forms of competition faced by the airlines industry today, as outlined in this chapter?*

3.7 Summary

The tourism marketing environment is made up of a number of unpredictable forces which surround the company. Examples of such forces include; political and regulatory issues, economic factors, social and technological developments. By closely monitoring the changing environment, the businesses could be in a position to anticipate certain threats and may possibly capitalise on any available opportunities in the market. They may only do this if they are consistently scanning and analysing their marketing environment. Briefly, environmental scanning involves the collection, observation and examination of information relating to the various forces in the macro (external) and micro (internal) environments. Environmental analysis is the process of assessing and interpreting the gathered information. The marketing managers must be aware of the latest trends and developments. They should continuously monitor their competitors, as they may take different forms. They may be suppliers of substitute products. They can be new entrants. Alternatively, competition may even come from customers and suppliers. Equally, marketers should be knowledgeable of different business models, as competition is coming from differentiated and low-cost service providers, among others.

Appendix 1

The Aviation Industry's Regulatory Environment

In the past, many governments have adopted a very high degree of regulation in all areas of the tourism industry's activities, particularly in the aviation sector. Such regulations imposed severe constraints on how airlines marketed their services. To gain a better understanding of the marketing environment, it is important to understand the regulatory environment and the changes which take place in this area (Kotler et al., 1990).

1. **Safety**

Safety is an important issue when discussing aviation regulation. As a means of ensuring that safety standards are maintained in airline operations, governments have imposed regulations into the industry. Only airlines which can demonstrate their ability to operate safely will gain admittance in their air space. This form of regulation has always been, and still is agreed upon by many countries.

2. **Protection of Scheduled Service**

A scheduled service may be defined as a regular, reliable service which is provided all year round, in accordance with a published timetable. For such a service to be maintained during the quieter off-peak periods, airlines must make substantial profits during the peak season. Without regulation, a heavy entry of airlines will only be attracted to the market during the peak season, which would greatly reduce the profits during off-peak periods. Consequently, regulation has often protected scheduled services. This argumentation has been used by incumbent airlines to discourage the arrival of new competing operators.

3. **Maintenance of Services for Societal Interests**

Although it may be declining in importance; in the past governments wanted to ensure that airline services were provided in thinner markets (even though it would have been unprofitable to the respective airlines) in order to encourage regional economic development in their respective country.

4. **Prevention of Excessive Competition**

Without regulatory controls, fierce competition would work against the consumers' interest (Porter, 1986). In normal conditions, competition should be seen as productive and healthy. It could be perceived as a positive market force, particularly for customers. However, a massive influx of competitors into the market can have a negative effect, if not controlled in an adequate manner. It could result in a substantial drop in air fares and price wars among airlines. Consequently, the weaker airlines will be unable to maintain their service at low fares levels, and will eventually file for bankruptcy; leaving stronger airlines to monopolise the market. This will lead to higher fares and the quality of service could be reduced, in the long run.

5. **To protect national interests**

The Paris agreement of 1919 accepted the principles that nations have absolute authority over the airspace above their territories. Since then, governments have regulated air transport to ensure that their national interests prevail. Regulation has often been reinforced by the governments' ownership of airlines. The governments often considered their flag carriers as a symbol of nationhood. National airlines were maintained to improve relationships with stakeholders, including bilateral relationships with other governments. Very often, national governments imposed strict regulations to promote their objectives. The state ownership of the national airline was prevalent for a number of reasons: Most airlines developed at a time when heavy government involvement in the industry was commonplace. Defence considerations were also of paramount importance, and the ownership of an airline was considered a matter of national security. Owning an airline was also seen as a way of protecting the balance of payments and promoting regional economic development. However, such ownership gave rise to the following problems: Unprofitable routes that were kept open for political reasons; Staff levels that were maintained at a high level as a means of keeping unemployment figures down. Fares were kept low as a means of reducing domestic inflation. As a result, money was coming out of public funds to keep an undercapitalised industry afloat, and so the tax payers had to fork out more money from their pockets to subsidise unprofitable airline operations.

Forms of Regulation

In the past, the governments' regulation has been prevalent in the aviation market. Governments often controlled the industry by granting or refusing entry into their market, as well as controlling capacities and frequencies, types of services and fares.

Both domestic and cabotage[1] services were under single government control. This avoided excessive competition among the national carriers. However, depending on the governments' policies, the regulatory regimes varied from country to country. For example, in the past a few governments allowed single, state-owned airlines in the market, where tight control cut out any direct competition between domestic airlines. The United States of America (USA) and the European Union (EU) countries have swept away from these regulatory systems as they liberalised their internal market (Wensveen, 2016; Shaw, 2016).

[1]Cabotage is the transport of goods or passengers between two places in the same country by a transport operator from another country.

Deregulation and Liberalisation

Since October 1978, the American domestic services were deregulated. Other countries, like; Canada, Australia and the UK have followed, with varying degrees of deregulation within their domestic markets. In international markets, significant developments have also taken place, with very liberal air agreements being conducted between European countries. USA has also signed a number of agreements which allowed competition on some of the international routes to and from America. In June 1990, the EU adopted the second phase of Air Transport Liberalisation in anticipation of the full common market (i.e. 31th December 1992). This package covered market access, fares, capacity, competition policy and external relations. From a multinational point of view, the main developments in deregulation have affected those EU carriers operating intra-European services.

The overall picture in relation to the regulation of the airline industry is one of substantial changes—changes which are still evolving (Belobaba et al., 2015). Some markets are still unaffected by liberalisation, and will probably continue to be so in the foreseeable future. However, many airlines hailing from regulated markets, will be affected if they compete with deregulated carriers in major international routes. In marketing terms, deregulation and liberalisation offer a considerable opportunity for efficient airlines to compete effectively. Nevertheless, incumbent airlines which could have been protected by regulation may be subject to considerable threats, unless they change and adapt to the competitive environment. It is important for their marketing managers to be aware of the differences between competition in regulated markets and competition in liberal or deregulated ones, so that they can make the necessary adaptations to their marketing policies.

Competition in the Deregulated Airline Market

Opportunities created by deregulation allow airlines to optimise their route networks. New and promising markets can be entered rapidly. Similarly, services can be quickly withdrawn from unprofitable routes, and the resources devoted to these markets may be transferred to other developing markets. Deregulation also means that airlines can increase their capacity levels, as soon as an increase in demand justifies it. The airlines who incur lower costs than their rivals, can afford providing reduced fares. This will enable them to exploit their cost advantages to the full.

It has been argued that deregulation has threatened inefficient airlines. The airlines who operate their services in liberalised markets had to learn to compete with other carriers (Button, 2017). To do this, they had to take quick decisions quickly, and they also needed access to up-to-date information about the changing marketing environments. This way, they would minimise their rivals' chances to compete against them. For instance, they may use smaller aircraft, improve their service and enhance their route network. If an airline garners control over particular routes, over slots and gate space, they will be in a dominant position in the market, relative to their competitors. The airlines' capability to control its market loyalty, feed traffic and operating costs (including labour costs) are also extremely important factors. The airlines should also defend their brand status, at all times.

Today, the airline industry is considered as a service business and must be prepared to operate in a highly competitive environment. No longer will public funds and regulation protect inefficient airlines. In the last few decades, many governments have reduced their direct involvement in the aviation industry. Many European airlines which were previously state-owned have sold their equity stake to private investors. Recently, the European Commission has put forward a comprehensive strategy to strengthen the competitiveness and sustainability of the entire EU air transport network. It has therefore identified three key priorities:

- "Tapping into growth markets, by improving services, market access and investment opportunities with third countries, whilst guaranteeing a level playing field;
- Tackling limits to growth in the air and on the ground, by reducing capacity constraints and improving efficiency and connectivity;
- Maintaining high EU safety and security standards, by shifting to a risk and performance based mind-set" (EU, 2015).

In the main, the EU airlines have an unprecedented choice of European destinations, and they could offer competitive prices to their passengers. The liberalisation of the European aviation industry has led to increased frequencies of domestic and international flights. As a result, the number of passengers carried have increased substantially, following the deregulation of markets. Moreover, low-fare carriers are now amongst the top airlines, both in terms of passengers and in terms of market capitalisation. For example, there is no limitation on traffic rights within Europe for EU airlines, as long as they have been granted an EU operating licence. However, restrictions and obstacles are still very common outside of Europe and in the context of international services and third country markets. The international routes (beyond the EU zone) will usually involve at least two governments. This means that international aviation is negotiated by way of bilateral bargaining.

Air Services Agreements

Agreements between governments relating to scheduled air services are known as air service agreements (ASAs) and they cover many aspects of air services between the countries. One of their primary functions is to regulate traffic rights, in terms of what traffic can be carried and what cannot. Traffic rights are defined under the so-called 'Freedoms of the Air'.

- The First Freedom permits overflying of one country's airspace by airlines from another country. For example, when flying from London to Geneva, the aircraft flies through French air space.
- The Second Freedom allows airlines from the first country to land in a second for non-traffic purposes (for example for refuelling). Between friendly nations, the exchange of these non-controversial freedoms is virtually automatic.
- The Third Freedom allows traffic to be carried by the home airline to a foreign country, for example, a flight from London to Paris.
- The Fourth Freedom permits this airline to pick up commercial traffic in the foreign country and to bring it back to its home base.
- The Fifth Freedom is the right to carry traffic between two foreign points. Under the terms of the Air Services Agreement between the United Kingdom and India, the Indian carrier is granted the right to pick up traffic originating in the UK and to fly between London and New York. Therefore, the granting of the Fifth Freedom rights is often contentious. Again, where such rights are granted, it is nearly always on a reciprocal basis. In the case of flights offered to Air India, under the terms of the UK/India Air Service Agreement, these rights are only given by the UK government because, in return, the Indian government allows Fifth Freedom opportunities for a British carrier to pick up Indian traffic originating in Mumbai, and to fly beyond.
- The Sixth Freedom occurs when airlines fly passengers from outside destinations to their home base, and then from their home base to a point beyond; thus combining Third and Fourth Freedoms. For example: Singapore Airlines (SIA) is an active competitor in the markets between the UK and Singapore. It also has an agreement with Australia covering the same rights between Singapore and Australia. By combining these sets of rights, and using its home base as a refuelling and stopover point, SIA has been able to expand significantly.

Following the granting of traffic rights, air service agreements can dictate which gateways can be served by an airline or airlines, from each country. ASAs may also cover frequency and capacity of services. Arguably, the development of the Fifth and Sixth Freedoms has made many of the traditional forms of regulation less significant, in marketing terms. Even in nominally regulated markets, price competition became prevalent with consumers availing of discounts in many ways. For example, all routes within the European Union were open to Third, Fourth and Fifth Freedom services. The capacity restrictions have been eased and were completely abolished by 1993. Eventually, greater pricing freedoms became available. The EU commission has been empowered to go ahead with negotiations, initially with the European Free Trade Association (EFTA) and later with others, to extend the benefits of LUX II package. Other initiatives are currently being dealt with in possible multi-lateral ASAs.

Open Skies Agreement

Since 1992, the USA's Department of State has pursued an "open-skies" policy that is designed to eliminate government involvement in airline decision-making about routes, capacity, and pricing in international markets. Open-Skies agreements also contain provisions governing commercial opportunities, safety, and security issues. The United States has negotiated open-skies agreements with more than 100 aviation partners.

The EU-USA Open Skies Agreement

The EU–USA Open Skies Agreement is an open skies air transport agreement between the European Union and the United States of America. The agreement allows any EU or American airline to fly between any point within their territories. Airlines of the European Union are also allowed to fly between the United States and non-EU countries like Switzerland. The initial agreement was signed in Washington, DC., on the 30th April 2007. The agreement became effective on the 30th March 2008. Phase two was signed in June 2010. For example, under this agreement, London Heathrow Airport was opened to full competition. This ended the exclusive right that was primarily granted for only two American airlines and two British airlines (Bermuda II) to fly transatlantic services out of Heathrow. Nevertheless, the expansion of transatlantic flights to or from Heathrow continue to be limited by lack of runway capacity (currently its two runways operate at over 98% of their capacity), government restrictions (especially when expansion plans to build a third runway and a sixth terminal was cancelled on the 12th May 2010, and the fact that many take-off slots are owned by incumbent airlines).