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Details of WTO subsidies case show USA believes Airbus drove rivals Lockheed and McDonnell Douglas from commercial airliner market

By **Aimée Turner**

Details of WTO case over subsidiaries emerge, revealing allegations of sharp pricing practices and unfair competition

Airbus has been accused of driving US rivals Lockheed and McDonnell Douglas out of commercial aviation, as the first details emerge on the USA's case over unlawful aircraft subsidies.

In its submission to the World Trade Organisation, the US Trade Representative (USTR) charges Airbus with conducting a campaign of targeting market share at the expense of profitability, principally through sharp pricing practices. Part of the WTO's role is to arbitrate on and resolve transatlantic disputes between Europe and the USA.

In documents now publicly disclosed, the USA gives detailed examples of subsidies it claims Airbus received for infrastructure developments, research and development in addition to highly preferential financial support at state level. The USA says that the combined effect of this support has allowed Airbus an unfair competitive advantage on pricing.

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Lockheed was a casualty of Airbus's subsidised growth, says the USTR

"Airbus governments thus enable Airbus to launch aircraft at an otherwise unsustainable scale and pace, if it could have launched them at all. Thus they expand the range of the Airbus product family against which US producers must compete, and lower the price at which Airbus is able to offer those products." This, it says, has had a serious effect on Boeing: "The sole remaining US producer has seen its market share fall below 50%. In the past five years alone, the US share of worldwide deliveries has fallen by nearly 20 points, industry revenues have decreased by 35% and industry earnings have decreased by 25%."

The USA adds that this will continue to happen - risking tens of thousands of US jobs - despite Airbus last week having conceded defeat to its US rival on total civil airliner orders for 2006. "The subsidisation of Airbus jeopardises the durability of any recent improvement in Boeing's competitive situation," says the USA.

Citing evidence of aggressive Airbus pricing in US sales campaigns between 2001 and 2005, the USA says it believes the European airframer's price undercutting has, over the past five years, led to a steep decline in Boeing's civil business despite major cost-cutting and steady productivity gains. "Both companies compete head-to-head for virtually every [100-plus seater] sale in the world in a largely 'zero sum' competition - a win for one producer is almost always a loss for the other," says the USA.

US aviation analyst Scott Hamilton points out that it was their own industrial strategy and the failure of Rolls-Royce that largely led to the exit of the US airframers from commercial aviation. "The USTR right off the bat notes that Lockheed and McDonnell Douglas were 'forced' from commercial aviation, but there are so many things wrong with this statement that it's hard to know where to begin," he says.

"Boeing's decline in the marketplace is the centrepiece of the USA's case, and the underlying thesis is that Airbus has hurt Boeing, but perhaps it will really depend on legal technicalities as the issue of subsidies - both direct for Airbus and indirect for Boeing - were agreed to in the 1992 GATT agreement."

Dr David Pritchard of the University of Buffalo points out that the current EU/USA dispute risks challenging the way all aircraft manufacturers finance new programmes - pioneered by Boeing's 787 system integration business model, where 90% of key components and subassemblies will be designed and manufactured by external suppliers.

"The complex web of global subsidies which transcends national borders achieves risk reduction, market penetration, containment of launch costs and the use of foreign risk-sharing partners as a conduit to foreign government funding," says Pritchard.

"My view is that both sides in this dispute have sinned. They would be much better to fight it out between themselves, because the ramifications of this dispute run throughout the whole global aerospace supply chain.

"Many elements within the industry benefit from some form of subsidy and this could open a can of worms. It is one of those down alley whispering things, but the industry would not be happy with either a US WTO win or a counter-case led by Europe," he adds.

Europe meanwhile is promising to deliver its response to the USA's case with a scheduled date of 9 February for submission. "We will have a robust response as regards all the claims included in the US submission," says a senior EC source.

Why Boeing lost campaigns in 2001-2005: Washington

- Lost campaigns in Europe: Driven by significant EasyJet and Air Berlin wins - both previously Boeing customers - the USA says Airbus increases its share of the European market by 9 percentage points measured by volume, and 12 percentage points by value.
- Lost campaigns in third-country markets: Airbus increases its share in markets other than the USA and the EC by 20 percentage points by volume, 19 percentage points by value. In the two largest third-country markets, Airbus gains 24 percentage points at Boeing's expense in China and 18 percentage points in Australia. "Large new orders in third-country markets, most evidently India, threaten further displacement of Boeing exports...for years to come," says the USA.
- Lost campaigns through undercutting: Airbus's undercutting is "well recognised in the industry", with Boeing citing the European airframer as admitting that profitability is sacrificed providing that market share remains at an average 50%. Regarding the EasyJet deal, Boeing cites the airline as having expressed surprise at "just how aggressive Airbus was in the final round of sealed bids". Boeing understands that the A319s were bought for $19.36 million at 2001 prices - a 56% discount off the $44 million list price.

737, 747, 767 and 777, Boeing figures show negative price trends for each aircraft type, with post-order price adjustments further demonstrating the "price-depressing effects" of Airbus practices.