

# Political Dynamics and Liberalization in the Brazilian Air Transport Industry: 1990-2002

**Cristiano Fonseca Monteiro**

Fluminense Federal University (UFF), Brazil

A first wave of theories on globalization suggested that because of new competitive pressures, national economies would converge into a single market economy model. Economic rationale would overcome politics, and political choices would be restricted to the implementation of a set of policy prescriptions aimed at favoring private investment, so-called “market-oriented reforms”. More recently, research based on economic sociology and historical institutionalism has shown that the implementation of market-oriented reforms at national, regional and industry-level has been characterized by a variety of outcomes, and politics has played a major role in producing such variety. The analysis of official documents, newspaper articles, interviews and other sources related to the main actors in the Brazilian air transport industry shows that the implementation of market-oriented reforms in this industry has also been marked by a complex political dynamics, comprising conflict, dispute, negotiation and compromise. This political dynamics has forged a trajectory that is unique in relation to other economic sectors in Brazil, and to the same industry in other countries. This paper concludes that politics has to be seriously taken into account in the debate on the search for efficiency and competitiveness in the Brazilian air transport industry.

Keywords: Deregulation; Market reforms; Economy and politics; Economic sociology; Historical institutionalism.

---

## Introduction

This article analyses the political dynamics of market-oriented reforms in the Brazilian air transport market between 1990 and 2002. During these years, regulation and market structure have been radically transformed, as economic policy has shifted from a nationalist-developmental strategy towards one aimed at insertion in a new globalized capitalism. Reforms involved macroeconomic stabilization (controlled inflation, fiscal discipline) and liberalization of economic activity, via trade opening,

privatization, deregulation and, finally, re-regulation under a new set of international competitiveness parameters.

The new model has drawn its legitimacy from a first wave of interpretations of globalization according to which the national domain – in the realms of politics, economy and also culture – would give way to a borderless world, materially based on new information technologies and ideologically sustained by the end of the polarity between the capitalist and the socialist blocs. In this new world, we would witness the virtual end of ideologies, history, and politics, so that the twenty-first century globalized capitalism would force all the national, regional and sector-level trajectories to converge into an increasingly homogeneous market economy.<sup>1</sup>

Underlying these interpretations was the proposition that the economy would assume preeminence over politics in the new globalized capitalism (Cf. Diniz 2000). In the face of greater freedom given to the circulation of capital, reinforced by the conditionality policies imposed by international agencies upon developing countries, and competitive pressure coming from everywhere, there would be no other alternative for national States but to create adequate conditions for the reproduction of capital. Interferences of a political nature would be “punished” by capital, which would flee to best-fit locations. Finally, there would be no room left for active policies out of a pro-market agenda, as they became perceived as conducive to inefficiencies and distortions in the economic rationality.<sup>2</sup> A kind of “politics-free” policy process would be a necessary consequence of such tendency.

Most of the existing literature on the Brazilian air transport industry, even if it does not discuss the forces at work in the globalization process, is deeply marked by such a “politics-free” perspective. The core of this literature (Franco *et al.* 2002; Pêgo Filho 2002; Guimarães 2003; Salgado 2003; Oliveira 2005; 2006a; 2006b) can be said to ignore the role of politics, leaving a gap in terms of historical analysis, as the implementation of market reforms is interpreted as an inexorable, uncontroversial process in face of globalization.

Guimarães’s (2003) study, for example, speaks of a “long term equilibrium trajectory” which has been pursued by the air transport industry around the world in the last decades. Such trajectory has been characterized by the “search for more efficiency” by airlines as a response to the entrance of new competitors, while at the same time being “also simply the result of the very removal of regulation” (Guimarães 2003, 3, my italics). Salgado, for her part, speaks of a “careful process of liberalization of the domestic air transport market, with the gradual introduction of competition” (Salgado 2003, 13, my italics), while Oliveira (2005, 7-8; 2006a, 8) mentions a “European approach, followed by the Department of Civil Aviation (DAC), emphasizing gradualism in (liberalization) policies, in order to try to avoid its potential ‘harmful’ short-term effects”. In summary, all of them narrate the liberalization of the Brazilian air transport industry as the gradual, deliberate and uncontested removal

of regulatory restrictions by authorities, and airlines automatically responding to it with more competition.

In contrast with these analyses, this article approaches the implementation of market-oriented reforms in the Brazilian air transport industry from a perspective in which politics is central to the explanation. Historical backgrounds, institutional settings and the balance of power among key actors help define the initial conditions under which reforms take place, and influence the way they are carried out. In turn, changes cannot be reduced to a mere passive adaptation. On the contrary, they involve choices, negotiation, dispute and compromise, making the processes of pro-market reforms rather open and contested ones, as has been demonstrated, both at theoretical and empirical levels, by institutional analyses in Sociology and Political Science.<sup>5</sup>

This paper aims to shed new light on the policy and regulation debate about the Brazilian air transport industry as it questions the “politics-free” perspective which characterizes most of the existing literature on the issue. By demonstrating that the logic of politics played a major role in this process, making the changes possible in the first place and determining their course, this article sustains that policy prescriptions have to take this into consideration.<sup>4</sup> The next section presents a historical account of the political dynamics of the air transport market in Brazil in the decades that preceded market-oriented reforms. The following sections present the main events that comprise the political dynamics of the twelve years of market-oriented reforms in the Brazilian air transport industry (1990-2002). Each section corresponds to a period of time in which the main actors involved, their interests, and disputes will be identified. A concluding section discusses some contributions of this article to the policy debate on air transport.

## **State-Market Relations in the Brazilian Air Transport Industry between the 1960s and the 1980s**

A major characteristic of the political dynamics between the 1960s and 1980s, in the air transport sector, was the existence of close ties linking authorities in charge of commercial aviation, represented by the Ministry of Aeronautics and the Civil Aviation Department, and the airlines. The milestone for the consolidation of this pattern of relationship was the military coup of 1964, when a restrictive regulatory model started being adopted as a response to the crisis that had been affecting air transport since the end of the 1950s.<sup>5</sup>

Discussion on the regulatory model defined after 1964 started during the two first Civil Aviation National Conferences (Conferências Nacionais de Aviação Civil (CONACs)), which took place in 1961 and 1963, respectively, in the cities of Petrópolis and Rio de Janeiro. Representatives of the airlines, the Civil Aviation Department, and economic authorities

participated in these meetings, which had few practical results, considering the political instability of the period. However, they helped strengthen the ties between business leaders and aeronautical authorities, in a context in which the whole air transport system was under strong criticism from public opinion.

On the other hand, the two first CONACs opened up the debate for topics such as the tighter control of market access in order to reduce the costs of the existing airlines, and the maintenance of operations in small towns, which were being abandoned since the old DC-3s had started to be substituted by larger planes, unable to operate in such locations due to the lack of infra-structure and the higher costs involved. Among the consensual propositions was the support for a model based on privately-owned airlines<sup>6</sup> and, consequently, the repudiation of the labor unions' demand for the creation of a new state-owned company to operate international flights.

It was at the third CONAC, in 1968, when the sector had already undergone a long process of consolidation,<sup>7</sup> that the regulatory principles of “fare realism” and “controlled competition” were settled. The former meant that the users of the service were supposed to cover all the costs of the air transport service, putting an end to the state aid that airlines had been receiving since the 1950s. The latter was aimed at reducing what was considered an “excessive expenditure of resources”, due to the concentration of services on the main routes. Authorities mentioned frequent cases of two or more airplanes taking off from the same airport to the same destination, at the same time, with few passengers. The risk of a predatory competition (with the increase in the discounts offered on these major routes) and the fact that most of the airlines were abandoning flights to smaller towns were considered additional problems that the principle of “controlled competition” aimed to solve.

The new regulation also prohibited new agents from entering the domestic market, while foreign capital had to be limited to 20% of the total capital of the existing companies. The few existing airlines therefore became fully protected from any sort of direct competition in the domestic market. A remaining problem was the maintenance of flights to smaller towns. It was not until 1975 that a regional system was created, the “Integrated Regional Air Transport System” (in Portuguese, SITAR). This system comprised the creation of five new regional airlines, which would operate flights in five different regions of Brazil, in a monopoly regime.

Considering the various regulations, the whole air transport sector was under strict state control. Airlines, on the other hand, enjoyed privileged access to the DAC and other government authorities, by means of frequent formal meetings, and also more informal ones, such as dinners and ceremonies. The fact that the sector was controlled by the Air Force, in the context of a military dictatorship, provided additional stability for the airlines. Other social forces capable of contesting the status quo, such as labor unions, had been excluded

from the CONACs since the beginning of the 1960s, and with the coup of 1964, the most active union leaders had been banned, and some of them exiled.

This arrangement lasted for over a decade, a period in which most of the airlines' profit margins grew constantly. It was only with the end of the military dictatorship in 1985 that such arrangement started to be challenged, with the gradual abandonment of nationalist-developmental policies, and greater room given to stabilization and pro-market policies. Within the executive branch, taming inflation by means of strict control of prices became a top priority, and aeronautical authorities would find it harder to authorize readjustments in fares, in order to maintain the principle of "air fare reality".

Along with the loss of power vis-à-vis economic authorities, Air Force and the DAC's position was confronted by the reemergence of organized labor in the political arena. Among the numerous subjects discussed in the Constitutional Congress elected in 1986 was the proposition, by labor unions representing workers in air transport, to create a civil agency to substitute the DAC in the control of non-military aeronautical activity. The "Pássaro Civil" (Civil Bird) campaign, as it was called, mobilized workers and progressive political leaders, representing a real threat to the interests of the Air Force and airlines. The proposition, however, did not pass. Aeronautical authorities, with strong support from airlines, lobbied against it in Congress, demonstrating that, despite the end of the military governments, the Air Force was still politically strong. While the debate about the military control of air transport would have to wait for another decade to return to the political arena, the relative loss of power of the Air Force and the DAC to economic authorities on the issue of fares would be the first round of a long dispute about the liberalization of air transport.

### **The First Cycle of Reforms: 1990-1994**

In 1989, Fernando Collor was elected president, with the promise of a new economic era in Brazil, based on pro-market reforms aimed at the modernization of economic activity. Under the new government, the first wave of market-oriented reforms in the Brazilian air transport industry took place with the ratification of the new International Air Transport Agreement between Brazil and the United States (signed in 1989 and approved by Congress in 1991), and the privatization of Vasp, which was acquired in October of 1990 by entrepreneur Wagner Canhedo. With the new agreement between Brazil and the United States, Varig started sharing routes between these two countries with Vasp and Transbrasil<sup>8</sup> after years of exclusiveness as the only Brazilian airline designated for international routes.

At the same time, as the new owner of Vasp, Canhedo challenged the air transport market in Brazil.<sup>9</sup> In practice, the strategies adopted by Canhedo violated both the principles of "controlled competition" and "air fare reality". In the first semester of 1991, Vasp started

scheduling flights to some of the main destinations at hours that coincided with flights offered by other airlines, offering more flights, and greater discounts during the low season.<sup>10</sup> Varig and Transbrasil protested against such initiatives, presenting complaints to the DAC, arguing that Vasp was using unfair competition practices, which were not compatible with the traditional functioning of the market. Canhedo replied with a radical defense of the liberalization of air transport, by means of interviews and articles published in the press accusing the other airlines of not being prepared for competition (Canhedo 1991a; 1991b). The DAC demonstrated some sympathy for Vasp's strategies, suggesting that these events represented an "adjustment" process.<sup>11</sup>

If aeronautical authorities seemed to be supportive to Canhedo's more aggressive strategies within the domestic market, the same was not true for regional flights. Vasp presented a demand to start flying from São Paulo's central airport, Congonhas, to other important cities such as Brasília, Curitiba and Belo Horizonte. In Congonhas at that time, Vasp, Transbrasil and Varig were only authorized to operate the traditional "air shuttle" between São Paulo and Rio de Janeiro, the country's most important route. Other domestic flights were operated from Guarulhos International Airport, which was distant from downtown São Paulo. Except for the Rio-São Paulo air shuttle, the airport was dedicated to regional airlines, such as Tam and Rio-Sul. It was the Air Force minister himself who answered Canhedo's request: "Congonhas is for regional airlines, and Vasp and Transbrasil are considered national airlines".<sup>12</sup>

Canhedo's disposition to challenge the market was shortlived. After a few months after Vasp launched its most aggressive strategies, the press started publishing a sequence of articles about the airlines' debts with several suppliers, including Infraero, the Brazilian state-owned firm in charge of operating most of the country's commercial airports.<sup>13</sup> Eventually, Canhedo had to retreat from his most aggressive strategies and give up his challenger reputation, inviting other airlines to form some kind of operational agreement that would re-establish the previous market structure. At the same time, a congressional commission was created in 1992 in order to investigate the privatization of Vasp, motivated by evidence that the process had been fraudulent. Key members of the Federal Government, such as the minister of the Economy, Zélia Cardoso, were accused of having favored Canhedo (Cf. Salomão 1993).

Such evidence demonstrates that Canhedo's aggressive, competitive style, apparently in line with the new president's platform of economic modernization, was actually anchored in the same traditional clientelistic mechanisms that characterized state-market relations in Brazil. In this sense, this first round of liberalization in Brazilian air transport was a rather superficial one. One can say that it helped to publicize the neoliberal agenda, but it did not actually break away from the previous pattern of state-market relations. The fifth



Civil Aviation National Conference, which took place in Rio de Janeiro, in October of 1991, would ratify the liberalization agenda, as it sanctioned measures such as the increase in the margin for discounts, extinguished the SITAR (although maintaining the separation of domestic and regional markets), authorized regional airlines to operate jets from the central airports of São Paulo (Congonhas) and Rio de Janeiro (Santos Dumont) to Belo Horizonte, Curitiba and Brasília, aiming at business travelers, and, finally, opened the market up to new players. On the other hand, the meeting maintained the compromise with the principles of “controlled competition”.<sup>14</sup>

Despite maintaining this principle, the macro-economic scene was not favorable to airlines in the first years of the 1990s. Rising inflation, economic recession and the political crisis that led to the impeachment of Fernando Collor in 1992 were the main features of a period of severe losses for all national airlines.<sup>15</sup> It was in this context that the proposal for the creation of a Câmara Setorial (Sectoral Chamber) emerged, in which representatives of the airlines, government and workers would discuss and negotiate alternatives for the sector.

The Câmaras Setoriais represented an important institutional change in the relationship between state and society in the first half of the 1990s in Brazil. It aimed to expand the traditional corporatist model which state and business used to negotiate, away from other social forces. Inspired by European-style neocorporatist arrangements, labor was introduced as an active part in the negotiation process. In a way, such innovative practice represented the recognition of the labor unions’ struggle for political voice which was one of the main aspects of the redemocratization process in Brazil. By focusing on the production chain, instead of exclusively considering the major firms of the economic sectors in which these chambers were created, this institutional arrangement would also be more open to the plurality of interest within business community itself (Cf. Arbix 1997; Diniz 1996, chapter 4).

Notwithstanding the severity of the crisis, and the success of other Câmaras Setoriais (especially the one created for the automobile industry), aeronautical authorities and airline businessmen did not accept some of the main principles of such arrangement. They refused to provide information that would subsidize a diagnosis of the sector, and rejected negotiation of measures to overcome the crisis.<sup>16</sup> Thus, the Câmara was shut down after a few meetings, while the economic crisis worsened.<sup>17</sup>

In 1993, the crisis struck Vasp and Transbrasil more severely, as they had to start lay off programs, and renegotiate debts with suppliers and airplane lessors. It was not until the beginning of 1994 that Varig, still the leading Brazilian airline, openly recognized that lay-offs would be inevitable, while it failed to meet obligations with leasing companies. Because of Varig’s default, some airplanes did have to stop flying or were subject to judicial mandates.

The airlines' strategy to cope with the crisis was to demand some kind of aid from the state, reproducing the traditional pattern of public-private relations in Brazil. In fact, air transport businessmen started negotiating with National Development Bank (BNDES) and top government officials for a special loan that would help airlines to restructure and have enough cash to get through the period of crisis. Labor unions criticized such aid, arguing that it was not fair to use public funds to help companies adopt restructuring programs that would lead to more lay-offs. They also criticized the negotiation process for being "obscure" as it was not open to public scrutiny. They proposed that any program aimed at dealing with the crisis of the Brazilian airlines had to be discussed in an open forum. Thus, they proposed the creation of a new *Câmara Setorial*, which was eventually accepted by government officials.<sup>18</sup>

Despite the support from some important segments of the central government, and the fact that aeronautical authorities and airlines did agree to provide some of the necessary information to support the work of the second *Câmara*, once again, aeronautical authorities, airlines and labor unions were not able to carry out the process. Airlines eventually managed to obtain financial aid from BNDES, while the Plano Real – the economic reform program which would effectively tame inflation and open the way for the implementation of the most radical neoliberal reforms in Brazil – produced a substantial improvement in economic activity as a whole, directly benefiting air transport.<sup>19</sup> Crisis, then, gave way to a cycle of expansion of the Brazilian economy which would diminish the interest of airlines in carrying on the work of the *Câmara*.

Thus, the first wave of liberalization in the Brazilian air transport industry, between 1990 and 1994, had a limited impact. It helped to publicize the neoliberal agenda more than to effectively break away from regulatory restrictions or to introduce new competitive practices. The possibility of offering a greater margin of discounts was a modest change, as many restrictions were maintained on routes and the use of airports. While international flights were liberalized to a greater extent, separation between domestic and regional segments were maintained, favoring those airlines that could fly from central airports – the ones preferred by passengers flying for business purposes, who were more willing to pay higher fares.

In turn, state-market relations can be said to have changed little. It is true that labor unions became recognized as a new, legitimate component of this relationship, with their participation in such institutional settings as the fifth CONAC and the *Câmaras Setoriais*. These forums, however, had modest practical consequences for the development of air transport. The CONAC did actually ratify some of the practices that had already been undertaken with the privatization of Vasp, while the *Câmaras* were unable to continue, due to the resistance of aeronautical authorities and airlines to provide information and



to negotiate the content of policies. On the other hand, the traditional patterns of public-private relations in the Brazilian air transport industry did not change in substance, as the privatization of Vasp and the negotiation for the BNDES loan in 1994 demonstrated.

### The Radicalization of Neoliberal Reforms under Cardoso: 1995-1998

If the improvement in economic indicators after the Plano Real was reason enough to justify the lack of interest of airlines in maintaining links with the Câmara, new policy prescriptions also played a role in the failure of such arrangement. In fact, with the election of Fernando Henrique Cardoso, in 1994, a new technocratic elite, profoundly committed to the neoliberal agenda, ascended to power. This new technocracy advocated that state bureaucracy in charge of economic affairs had to be insularized from political forces, so that former state-market ties had to be broken. Thus, the kind of concertation strategies represented by the Câmaras were suspended, while the liberalization agenda was to be pushed further.

From the point of view of aeronautical authorities, a very restrictive perspective of liberalization was still predominant. The discourse of key representatives of the Air Force Ministry and the DAC in the bulletin DAC Notícias, published between 1994 and 1999, make this perspective evident. Brigadier Renato Pereira da Silva, for example, says about discounts and the increase in the number of flights offered by airlines right after the Plano Real:

Discounts exist only to increase the access of passengers when the market is weak. In principle, discount should exist only in such circumstances. However, with the implementation of Plano Real, airlines were not fast enough to eliminate such discounts. (...). Some people might not be able to fly during high season due to the unavailability of seats on airplanes; on the other hand, airlines should increase their fleets very carefully. There must be some sort of planning (...) right now, air transport users are being favored, but there must be an equilibrium.<sup>20</sup>

It is also worth quoting the DAC's General Director during this period, João Felipe S. de Lacerda Jr., who appeared to be generically in favor of liberalization, while making several references to the traditional, interventionist model, that had been typical of the action of the DAC.

My objective is to continue the program of flexibilization in the regulation (of air transport), aiming at a healthy, free and non-ruinous competition. Proceeding in such a manner, I hope to continue promoting the necessary expansion of the airlines that represent our flag abroad, based upon discerning studies of the demand. In the domestic field, I will encourage national and regional airlines to expand according to their interests, always taking into account the interest of the user.<sup>21</sup>

Airlines, for their part, would once more have to deal with the toughening of control over price readjustments by economic authorities. According to the legislation that created the Plano Real, public utilities and services, in which air transport is included in Brazil, would have their fares adjusted on a yearly basis, and the increases had to be authorized by economic authorities.<sup>22</sup> It was during this period that president Cardoso's Civil Cabinet and economic authorities started threatening aeronautical authorities and the airlines with the opening of the domestic market to foreign airlines, which would allow much more powerful companies from the U.S., Europe and Asia to transport passengers between Brazilian cities.

During the second semester of 1997, the prices of air fares became a top priority for government authorities, and the Civil Cabinet started a workgroup<sup>23</sup> responsible for implementing new liberalization measures within the Brazilian air transport market. Confirming the new public-private relationship pattern, airlines were not invited to participate or to discuss the measures to be implemented by the workgroup. It was during this period that the influential minister of the Economy, Pedro Malan, proposed the creation of a new civil agency that would substitute the DAC.<sup>24</sup>

Civil Cabinet officials and economic authorities struggled with the Air Force Ministry, the DAC and airlines to impose a new round of liberalization. Under the threat of opening the domestic market to foreign airlines and creating a civil agency that would put an end to the DAC's control over commercial aviation, aeronautical authorities progressively eliminated regulatory restrictions regarding the offer of discounts, control over routes and the use of central airports. An article by the general director of the DAC in 1998, Masao Kawanami, suggested that the former "controlled competition" principle was being substituted by "healthy competition". In turn, airlines responded with aggressive competition, in which fares dropped while the number of passengers grew by more than 20%.<sup>25</sup>

As the elections of October 1998 were getting closer, however, the liberalization agenda weakened.<sup>26</sup> Government officials seemed to be satisfied with the airlines' response to the liberalization measures, and propositions to take reform further, such as the increase in the percentage of foreign capital in Brazilian airlines, were suspended. After the reelection of Cardoso, the political dynamics of the air transport industry would change radically as a new economic crisis struck the Brazilian economy, with dramatic consequences for the sector. In such a setting, the liberalization agenda gave way to another period of demands for state aid by airlines. But this time, new strategies, new kinds of demands and a new relationship with other key social actors would characterize the political action of business leaders, signaling new trends in the political dynamics of the consolidation of neoliberal reforms. Such features will be analyzed in the next section.

## Crisis and Impasse towards the New Century: Cardoso's Second Term, 1999-2002

In January of 1999, after Cardoso was reelected for a second term as president of Brazil, and in the middle of a series of global financial crises, economic authorities decided to implement a radical move in the exchange-rate policies, by introducing a more flexible system in which the fixed rate system would be substituted by a flexible one. Real, which so far had been worth approximately one dollar, devaluated to next to half of a dollar. Firms and individuals that had signed contracts in dollars for local transactions, saw their costs double in less than a month. Brazilian airlines were especially affected by this change, as their revenues in the domestic market were in reals, while most of their costs (fuel, leasing, maintenance, insurance) were in dollars. Since fares could not be updated, airlines had to bear the losses of the sudden devaluation.

In the domain of economic agenda, another important change took place. Cardoso's first term had been characterized by a widespread consensus regarding stabilization policies, recognized as a top priority. After reelection, so-called developmentalists claimed that such policies could not be restricted to the control of inflation, introducing the question of economic growth (Cf. Diniz 2000, 96ss). While economic authorities tended to stick to the stabilization priorities (including the Ministry of Finance, Ministry of Planning, and the Central Bank), authorities related to industry and services, such as the Ministries of Development, Transport and Tourism, tended to question the exclusive focus on stabilization, demanding pro-growth measures.

In relation to air transport, the creation, in April of 1999, of a workgroup to elaborate a program to support airlines after the shock caused by the devaluation of the real, indicated that neoliberal orthodoxy might be losing its strength. The program, however, was not implemented. At that moment, the search for solutions to the crisis were limited to the creation of another workgroup, this time under the responsibility of the newly created Ministry of Defense.<sup>27</sup> In fact, members of the Air Force were inclined to support Brazilian airlines from what they interpreted as the "threats of globalization".<sup>28</sup>

In turn, airlines adopted new strategies to cope with such threats. As the traditional links to state bureaucracy, which allowed the negotiation of loans, tax reliefs and other forms of protection, were suspended by economic authorities, they had no alternative but to look for other forms of political action. From 1998 onwards, airlines invested in legitimizing their claims, publicizing their action, and extending their alliances to civil society entities (such as universities, associations and so on), labor unions and Congress. Their discourse changed: instead of "protection", airlines demanded measures that would assure equal competitive conditions with foreign companies.<sup>29</sup>

Despite such threats, the year 2000 represented a period of recovery for all airlines, as the Brazilian economy seemed to be entering an upward cycle. Such recovery, however, was interrupted by the energy “black-out” of 2001, followed by the terrorist attacks of September 11. Such events were deleterious for a sector that had already entered the new millennium with accumulated losses. Even Tam, despite having benefited from some crucial years of exclusivity in the operation of business routes linking São Paulo to other important capitals from its central airport, presenting increasing profits throughout most of the 1990s, joined Varig, Transbrasil and Vasp in negative results.

In December of 2001, Transbrasil had to quit the market, as suppliers stopped providing crucial services such as fuel, due to successive delays in the payment for their services. Vasp and Varig also depended on frequent renegotiations of debts with fuel and catering suppliers, and lessors. It was in this context that the Ministry of Development, along with the Ministry of Defense and other key government officials representing the developmentalist group, accepted the proposition by labor unions to create a “Competitiveness Forum” for air transport. The forum resembled the previous *Câmaras Setoriais*, serving as a concertation arrangement in which government authorities, airlines and workers would discuss the sector’s weaknesses (and strengths, if there were any) and possible measures to overcome the crisis.<sup>30</sup>

The creation of such a forum, after years of radical opposition to the existence of this kind of arrangement by neoliberal orthodoxy, was evidence that things were changing. The Forum, in fact, was successful in carrying out measures that were in line with the demands of airlines, with the support of labor unions and developmentalist sectors within the government.<sup>31</sup> Essentially, government offered temporary tax reliefs, exempted airlines from taxes on imported airplane parts, simplified procedures to import such parts and opened new credit lines. Even though these measures were announced in September 2002, a few months before the end of Cardoso’s term, they undoubtedly indicated that state-market relations were moving away from the orthodox, insularized model of neoliberals.

At the same time, pro-market reforms were not fully achieved during Cardoso’s two terms. Although former regulatory restrictions had been removed, the institutional infrastructure in charge of commercial aviation did not change. The Air Force, by means of the DAC, which resisted the liberalization of air transport as long as it could, was still the state bureaucracy responsible for the control of air transport. Cardoso’s cabinet did propose the creation of a new, non-military agency, that would substitute the DAC. A new legislation was also being analysed, as the existing one (*Código Brasileiro do Ar*) dated from 1986.

The project to create the new agency was designed by a restricted workgroup, with the participation of representatives of the economic authorities, the Air Force and Infraero. Once again, neither airlines nor labor unions were invited to discuss the project, under the

pretext that it was an administrative matter, not subject to open debate. When the project was sent to Congress for approval, however, airlines identified a series of items that had major implications for their competitive capacities.<sup>32</sup> While the project was under analysis in Congress, several public hearings were held in which representatives of the government, airlines, labor unions and other entities were invited to discuss it. After six months of public debate, congressmen decided to incorporate most of the airlines' and labor unions' demands. The government decided to withdraw the project, and the creation of a new agency was indefinitely postponed.<sup>33</sup>

It is interesting to note that, while the executive branch was unable to carry out the reforms and the whole sector suffered severe losses, a new relationship pattern was emerging with non-state actors involved in the process. The analysis of the business leaders' and labor unions' strategies during the period shows that there was a greater investment in the publicization of the air transport debate, and more dialogue between them. Business leaders were present in more institutionalized and public spaces, and established new links with civil society entities, including labor unions. These continued investing in the creation and strengthening of public spaces where stakeholders could discuss policies for the sector. Even if they suffered the consequences of the crisis of the 1990s, with job losses and the precarization of the jobs that remained, they were capable of advancing their institutional agenda, as the creation of the "Competitiveness Forum" demonstrates. As for the executive branch, it seems to have adhered too long to a neoliberal orthodoxy which kept it from engaging business leaders and labor unions in a renewal of the relationship between state and market towards a more open and democratic pattern.

## Conclusion

This article has aimed to show the role of political dynamics in the twelve years of pro-market reforms in the Brazilian air transport industry. Politics evolved, during Collor de Mello's and Cardoso's terms, in such a way that aeronautical authorities were increasingly pressured by the core agencies of the executive branch to deepen liberalization. Airlines eventually engaged in price wars, as a response to such political pressure, but these wars tended to be short-lived since airlines could not bear the increasing costs, worsened by the frequent internal and external economic crises that affected Brazil and the global economy during the period. While the proponents of the reforms were successful in deregulating the market, the project of a new regulatory apparatus did not materialize. The creation of the Civil Aviation National Agency (ANAC) which in theory should be part of the reform process to adapt air transport to a new competitive global environment, was postponed and would not be completed until 2006.

Understanding the political dynamics of the liberalization of the Brazilian air transport industry is a necessary exercise. If this important dimension is not taken into account, the policy debate will miss the specificities that characterize the way the sector has been trying to adapt to the new competitive environment of a globalized capitalism. Instead of an “uncontroversial” option for liberalization as a result of a “natural” tendency, this article shows that the trajectory of the reforms in the air transport sector has been characterized by the confrontation of interests, sometimes resulting in contradictory movements, as in the case of the privatization of Vasp. Because of its political nature, the liberalization of air transport in Brazil has assumed a very particular character.

Even if this article has not directly aimed to discuss policy prescriptions per se, a few words can be mentioned about the issue. The literature on air transport in Brazil strongly supports more liberalization in order to face the challenges of twenty-first century capitalism. Among common prescriptions are the removal of remaining regulations for market access, the extension of market reforms to airports, an increase in the limit of the participation of foreign capital in the industry, and, more recently, they have incorporated the emergent contradictions between the efficiency-enhancing, profit-oriented strategies of airlines operating in a competitive market and the well-being of consumers. This is an issue with important political implications; however, the prescriptions that have been offered are also reduced to technical matters, for example, the proposition of specific regulations to stimulate services to regions where air services are not economically viable. Because the authors do not take the dispute, negotiation and necessary compromise involved in policy implementation into consideration, prescriptions do not mention potential conflicts of interest between airlines, authorities in different spheres of government, workers, and other stakeholders, let alone a way to deal with them.

Every rule has its exceptions. An important one from the economic literature discussed in this article is the last paragraph of Salgado (2003, 24). After criticizing the measures taken by aeronautical authorities in the first months of the government of Lula da Silva, in a movement that she interpreted as a (undesirable) return to the principle of “controlled competition”, the author asserts:

The debate on the best regulation for the sector, which simultaneously promotes the development of industry and the well-being of users, will certainly benefit from its publicization and the inclusion of more participants who can carefully assess the effects of policy prescriptions on the market.

Publicization and inclusion of more participants in the debate means recognizing the existence of potentially divergent views about the policies to be adopted. The recognition of divergence and the proposition to incorporate it into the debate does mean acknowledging politics and incorporating it as an issue. The debate on the policies for the Brazilian air



transport industry will have much to gain in terms of historical consistency if the recognition of the importance of politics becomes less an exception and more the rule.

Revised by Hedd Megchild

Submitted in March, 2011.

Accepted in July, 2011.

## Notes

- 1 For critical assessments of convergence theory, see Berger and Dore (1996), Drache (1996) and Ferrer (1997).
- 2 For an example of this approach, see Bacha (1995), who discusses economic policy in Brazil and Latin America in the early 1990s.
- 3 Institutional approaches in Sociology (Fligstein 2001; Nee and Swedberg 2005), Political Sciences (Hall and Soskice 2001), and at the border of both (Evans 1995) have highlighted the role of historical and political elements in shaping contemporary capitalism. In Brazil, see Velasco e Cruz (1998) and Diniz (2000).
- 4 For an example of a policy analysis that takes politics into consideration, see BID (2007). The report explores several key political dimensions of policy implementation in Latin America, such as intragovernmental conflict; public x private formal and informal mechanisms of interaction; the role of civil society; and the potential impacts of such political processes in policy implementation. Contrary to the neoliberal approach, the report recognizes that political processes can have both negative and positive outcomes, therefore successful policies do not depend on removing, ignoring or lamenting politics but on trying to understand it in the first place.
- 5 See Fay (2001) for a narrative of this crisis, describing the work carried out in the commissions created in the Brazilian congress (Comissões Parlamentares de Inquérito or CPIs) to discuss the increase in the number of accidents, bankruptcies and the claims, by surviving firms, for greater state aid. See also Pereira (1987), for a narrative presenting the point of view of labor unions.
- 6 At that time, Brazil, along with the United States and a few other countries, adopted an air transport system in which private airlines were predominant. The only exception was Vasp Airlines, owned by the state of São Paulo.
- 7 At that time there were two companies exploring international routes: Cruzeiro do Sul, flying to South America and the Caribbean; and Varig, flying to Asia, North America and Europe (flights to Africa would start during the 1970s). These companies shared the domestic market with Transbrasil and Vasp. A fifth company, Paraense, was still operating, but it would stop in 1970. At least two of the Brazilian major airlines since the end of the Second World War, Real Aerovias and Panair do Brasil, had stopped flying during the 1960s. In both cases, Varig had been able to negotiate with the federal government and aeronautical authorities support to incorporate routes, equipment, airport areas, and human resources from these airlines. The

most dramatic episode was the one involving Panair do Brasil, which was ruled bankrupt by a government decree, in the middle of a series of discretionary acts aiming to attack the company's owners, who supported political leaders that opposed the military regime.

- 8 A principle of reciprocity had to be observed in all bilateral air transport agreements, according to the Chicago Convention of 1944. Therefore, the permission for Vasp and Transbrasil to fly these routes implied that two other North-American airlines would also be granted such permission, so that a total of six airlines started competing in the routes between Brazil and the United States in the beginning of the 1990s.
- 9 A few months before the fifth CONAC, which is formally recognized as the milestone of the liberalization process in Brazilian air transport, privatized Vasp launched an aggressive strategy of expansion, both within domestic and international services, which was partially tolerated, if not approved, by aeronautical authorities.
- 10 The decision to offer discounts in fares obeyed a different logic during the years of heavy regulation. In the first place, discounts were rare, being offered only during the "high season", i.e., vacations (especially during the summer, which in Brazil occurs in January and February). The whole system was structured in order to serve frequent users, usually people traveling for business purposes, who had their tickets paid by employers (in many cases, the Government). Since those who travel for business do not have the option of not traveling, and considering that the quality of roads and railroads is very poor in Brazil, firms and government agencies had no alternative but to pay for air transport services if they needed it. Thus, discounts were limited to those months when there was a drop in business activity, during the summer, when more people flew for leisure purposes.
- 11 See "DAC considera disputa aérea mero ajuste", *Jornal do Brasil*, 30/5/1991; "DAC considera em parecer que a Vasp não pratica dumping", *O Globo*, 7/6/1991.
- 12 See "Governo rejeita mesmos horários para vôos de linha aérea regional", *Folha de São Paulo*, 19/6/1991.
- 13 See "Infraero ameaça ir à Justiça contra Vasp", *O Estado de São Paulo*, 28/6/1991.
- 14 According to a document by the DAC: "A more flexible approach to regulation was adopted, with stimulus to the exploration of markets, routes and new schedules, always preserving the competitive equilibrium among airlines, under a less rigid price system. The policy prescribes the liberalization of fares as a goal to be pursued, but reminds the recent deregulation experience in other countries, recommending the necessary care in its adoption" (Ribeiro 2001,140, my italics).
- 15 In 1992, for example, the domestic market decreased by 17.6% in relation to the previous year, while the total profitability of the Brazilian airlines (including both national and international operations), was negative by approximately 11% in 1991 and 1992 (Cf. Departamento de Aviação Civil 1992).
- 16 Such resistance became evident, for example, when a representative of DAC said in one of the meetings, that the Câmara was not a forum to discuss policies for the sector, since there was already a policy which had been formulated by the Air Force Ministry, "with the experience of several years leading aviation" (Cf. *Dia a Dia*, 8/5/92, no. 68:2).
- 17 Inflation reached above 1.100% in 1992 and 2.500% in 1993. Gross Domestic Product (GDP) growth rates were even worse: after dropping to -4.35% in 1990, they raised to a modest 1% in 1991, going back down to -0.47% the next year.
- 18 See *Dia a Dia*, 27/5/1994, no. 173:3.

- 19 In 1994 and 1995, the industry's average profitability reached more than 6% (domestic and international). For domestic flights only, the rate reached more than 14% (Cf. Departamento de Aviação Civil 1995).
- 20 See *DAC Notícias*, 1994, no. 2:5, my italics.
- 21 *DAC*, 1995, my italics.
- 22 Between 1996 and 1997, government and airlines would struggle around the issue of ticket prices. Airlines were accused of cartelization and abusive fares, and entities such as the Brazilian Consumers Association started campaigns against the companies, while public authorities started investigating airlines and the Air Force ministry, accusing the former of anti-competitive practices, and the latter of allowing such practices – see “Ofensiva para derrubar o valor das passagens aéreas”, *O Globo*, 27/7/1996 and “Ponte aérea pode ser cartel”, *Jornal da Tarde*, 23/9/1996.
- 23 The minister of the Civil Cabinet, Clóvis Carvalho, was the head of the workgroup, which was composed of representatives of the main agencies involved with economic policies, including anti-trust, and the Brazilian tourism agency, Embratur.
- 24 “Malan propõe agência reguladora para transporte aéreo: meta é baixar tarifas”, *O Globo*, 8/8/1997.
- 25 *DAC Notícias*, n. 4, 1998:1. Another publication by the DAC narrated this period of changes as follows: “Airlines accepted the measures implemented by the DAC and reduced their fares. As a result, between February and August (of 1998) there was a 25% increase in the number of passengers in domestic flights, both in the national and regional segments. During the month of July only, 250,000 people traveled by air for the first time, people who had never boarded an airplane before” (Ribeiro 2001, 146).
- 26 See “Abertura depende das eleições”, *Gazeta Mercantil*, 20/7/1998.
- 27 The Ministry of Defense incorporated the three military ministries: the Army, the Air Force and the Marines.
- 28 Cf. *DAC Notícias*, 1999, no. 16:5.
- 29 Airlines argued that the level of taxation in Brazil was above 35% of total revenue, while in other Latin American countries it was around 20%. In Europe, the average was 15%, while in the United States, less than 10%. They also complained about the long time needed to import airplane parts, which forced them to maintain an excessive number of spare accessories, raising costs. North-American, European and Asian airlines also enjoyed better conditions on leasing and insurance contracts, so that Brazilian airlines demanded measures that would minimize such differences.
- 30 The opening session took place on January 23, 2002, with the presence of ministers Sérgio Amaral (Development) and Pedro Malan (Finance), representatives of the Ministry of Defense, airline executives, labor unionists and the DAC.
- 31 Pêgo Fiho (2002) analyzes such measures from an economic perspective, considering them a return to politically-driven, undesired paternalistic measures. He does not discuss, however, the argument of airline businessmen, union leaders and developmentalists about the need to balance the airlines' competitive conditions with their counterparts in other countries.
- 32 Airlines questioned such propositions as the introduction of new taxations, short-term concessions for the exploration of routes, and legal restrictions regarding the use of airport areas. Labor unions, on their part, proposed the creation of consultant bodies that would check on the agency's work.

- 33 The agency would not be created until the beginning of 2006, long after the first version was sent to the Congress and sixteen years after pro-market reforms were introduced in the Brazilian air transport sector.

## Bibliographical References

- Arbix, Glauco. 1997. "A câmara banida". In *De JK a JQ: a reinvenção dos carros*, ed. Glauco Arbix and M. Zilbovicius. São Paulo: Scritta.
- Bacha, Edmar. 1995. "Perspectivas econômicas brasileiras em regime de feijão com arroz à la Marcílio". In *Economia e política da crise brasileira: o pensamento da equipe Fernando Henrique*, H. Jaguaribe et al. Rio de Janeiro: Rio Fundo.
- Berger, Suzanne, and Ronald Dore, ed. 1996. *National diversity and global capitalism*. Ithaca/London: Cornell University Press.
- BID – Banco Interamericano de Desenvolvimento. 2007. *A política das políticas públicas. Progresso econômico e social na América Latina*. Relatório 2006. Rio de Janeiro: Campus.
- Canhedo, Wagner. 1991a. Cortina de fumaça. *Folha de São Paulo*, June 7.
- \_\_\_\_\_. 1991b. Planos de Canhedo vão além da Vasp. *Jornal do Brasil*, June 2.
- DAC – Departamento de Aviação Civil. 1995. *Anuário do transporte aéreo*. Rio de Janeiro: DAC/Ministério da Aeronáutica.
- \_\_\_\_\_. 1992. *Anuário do transporte aéreo*. Rio de Janeiro: DAC/Ministério da Aeronáutica.
- Diniz, Eli. 2000. *Globalização, reformas econômicas e elites empresariais*. Rio de Janeiro: FGV.
- \_\_\_\_\_. 1996. *Crise, reforma do Estado e governabilidade*. Rio de Janeiro: FGV.
- Drache, Daniel. 1996. "From Keynes to K-Mart. Competitiveness in a corporate age". In *States against markets. The limits of globalization*, ed. R. Boyer and Daniel Drache. London/New York: Routledge.
- Evans, Peter. *Embedded autonomy. States and industrial transformation*. Princeton: Princeton University Press, 1995.
- Fay, Claudia. 2001. Crise nas alturas: a questão da aviação civil. Ph.D. thesis, Porto Alegre, RS, PPGH/IFCH/UFRGS.
- Ferer, Aldo. 1997. "Development and underdevelopment in a globalized world: Latin American dilemmas". In *Economic and social development into the XXI century*, ed. L. Emmerij. Washington: Inter-American Development Bank.
- Fligstein, Neil. 2001. *The architecture of markets. An economic sociology of twenty-first century capitalist societies*. Princeton: Princeton University Press.
- Franco, Francisco, Priscila Santana, Celso Almeida, and Ricardo Braga. 2002. *Recent deregulation of the air transportation in Brazil*. Brasília: Secretaria de Acompanhamento Econômico/Ministério da Fazenda.

- Guimarães, Eduardo. 2003. "Aspectos regulatórios do mercado de transporte aéreo no Brasil". In *A regulação do mercado de aviação civil no Brasil*, Eduardo Guimarães and Lúcia Salgado. Rio de Janeiro: IPEA.
- Hall, Peter, and David Soskice, ed. 2001. *Varieties of capitalism: The institutional foundations of comparative advantage*. Oxford: Oxford University Press.
- Nee, Victor, and Richard Swedberg, ed. 2005. *The economic sociology of capitalism*. Princeton: Princeton University Press.
- Oliveira, Alessandro. 2006a. *Liberalização econômica e universalização do acesso no transporte aéreo: é possível conciliar livre mercado com metas sociais e ainda evitar gargalos de infra-estrutura?* São José dos Campos, SP: NECTAR/ITA
- www.nectar.ita.br (accessed May 10, 2007).
- \_\_\_\_\_. 2006b. *Regulação da oferta no transporte aéreo: do comportamento de operadoras em mercados liberalizados aos atritos que emergem da interface público-privado*. São José dos Campos, SP: NECTAR/ITA.
- www.nectar.ita.br (accessed May 10, 2007 and October 5, 2007).
- \_\_\_\_\_. 2005. Performance dos regulados e eficácia do regulador: uma avaliação das políticas regulatórias do transporte aéreo e dos desafios para o futuro. São José dos Campos, SP: NECTAR/ITA.
- www.nectar.ita.br (accessed May 10, 2007 and October 5, 2007).
- Pêgo Filho, Bolivar. 2002. Setor aéreo e as empresas brasileiras: situação atual e perspectivas. *Boletim de Conjuntura do IPEA*, no. 59:73-78.
- Pereira, Aldo. 1987. *Breve história da aviação comercial brasileira*. Rio de Janeiro: Europa.
- Ribeiro, Luciano. 2001. *Traçando os caminhos dos céus: o Departamento de Aviação Civil – DAC. 1931-2001*. Rio de Janeiro: Action.
- Salgado, Lúcia. 2003. "A regulação do mercado de aviação civil no Brasil: evolução e situação atual". In *A regulação do mercado de aviação civil no Brasil*, ed. Eduardo Guimarães and Lúcia Salgado. Rio de Janeiro: IPEA.
- Salomão, Luiz. 1993. *Vasp: voo 171*. Brasília: Câmara dos Deputados.
- Velasco e Cruz, Sebastião. 1998. Alguns argumentos sobre reformas para o mercado. *Lua Nova*, no. 45:5-27.