PHOTO: SIMON BLAKESLEY

Employee and Stakeholder Information Update

25 February 2022

The coronavirus pandemic first started to impact our business in March 2020, and who would have thought that we would still be dealing with its impact almost two years later. COVID-19 has accounted for more than $18 million in losses for us, and we would have found it difficult, if not impossible, to survive losses of this magnitude without help. We are very thankful for the almost $16 million is assistance received under the Canada Emergency Wage Subsidy Program (CEWS) and the Northern Essential Air Services Program (NEAS), but as financial assistance winds down, our airline, and the industry as a whole, needs to find ways to operate sustainably through the ongoing impacts of COVID-19.

The Yukon market was well on its way to recovery during the second half of 2021, but, as the data below shows, we peaked at 79% of pre-COVID traffic in December and the Omicron variant caused a backslide to 57% in January. February traffic, to date, is showing a slight improvement over January and bookings for March and beyond are looking promising.

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Vuntut Gwitchin First Nation

AIR NORTH Yukon's Airline

Yukon Market COVID Recovery – Total Market Passenger Traffic

Gateway & Regional	2019	2020	2021	2022
January	Baseline	108%	14%	57%
February		103%	13%	65%
March		68%	14%	
April		4%	18%	
May		6%	19%	
June		10%	27%	
July		25%	40%	
August		31%	54%	
September		33%	67%	
October		38%	71%	
November		26%	70%	
December		14%	79%	
		Q4 2021 Average	73%	

While our COVID related drop in traffic has been huge, the Yukon market has likely fared better than other markets, largely due to the essential nature of much of our flying. With mainline carrier COVID related losses well in excess of $10 billion (WestJet does not report their financial results), and with two new carriers about to enter the market and a third expanding substantially, in my opinion, our industry is in for a real bloodbath and we need to make sure that we don't become collateral damage.

Canada is a large country with a small population and an efficient and affordable national air transportation network is essential for the health of our economy and the well-being of Canadians. For the past 24 months, Canadian air carriers have been providing essential services with passenger and cargo loads which have not provided sufficient revenues to meet direct operating costs and overhead expenses. This dynamic is likely to persist for some time and while financial aid has helped to address the economic challenges, as aid programs end, we need to find ways to facilitate the sustainable operation of our national air transportation network at reduced capacity. Mandatory interline agreements between the two large mainline airlines and the many small regional airlines that serve most of Canada's regional communities would go a long way towards accomplishing this because they would provide easy incentives to reduce excess market capacity. They would also increase competition, enhance consumer protection, address environmental protection goals, facilitate regional economic development, reduce travel barriers for remote community residents and, in the Yukon market, address reconciliation commitments.

PHOTO: SIMON BLAKESLEY

We have pointed out before that excess capacity has been troublesome in the Yukon market throughout the pandemic. Our estimates show that the cost of excess capacity during the past 24 months very nearly equals the value of the financial aid provided and this obviously benefits no-one, especially taxpayers. Yukon market data estimates for Q4 2021 provide an excellent illustration of the all-round benefits that could accrue from mutually beneficial interline agreements. During Q4, Yukon market traffic showed a recovery to just over 70% of pre-COVID volumes and while our flights produced a positive margin over our direct operating costs, we were not able to generate enough traffic, or enough flying, to meet our overhead costs and, as a result, we will show a loss for the quarter of more than $1.5 million, before year-end adjustments. During Q4, about 25% of our capacity was dedicated to our "secondary gateways," those being Kelowna, Victoria, Edmonton, Calgary, Yellowknife, and Ottawa. With a mutually beneficial interline agreement, we could have reduced our secondary gateway capacity by more than 50% while increasing our ability to sell travel to those secondary gateways through interline agreements with mainline carriers. Similarly, we estimate that mainline (Air Canada) Yukon market capacity in Q4 also produced sub-optimum results for them, but with a mutually beneficial interline agreement, our competitor could have optimized their capacity without losing any network traffic and they would have picked up feed traffic from us. The net result could have been a "traffic swap" of about 6,700 passengers with reduced capacity and costs for both airlines resulting in improved load factors and a $1 million+ margin improvement for each airline, along with an estimated 13% reduced environmental footprint for the Yukon aviation market, increased and seamless access to the rest of Canada and the rest of the world for the Yukon, enhanced consumer protection for people traveling from and to the Yukon, preservation of Yukon jobs, increased sustainability of the locally provided air travel network, facilitation of fleet upgrades, and steps forward with respect to commitments made to Yukon First Nations in agreements such as the *Vuntut Gwitchin First Nation Final Agreement*.

PHOTO: SIMON BLAKESLEY

Air passenger rights and passenger protection provisions are an important consideration in this discussion. These have recently been introduced in legislation but, without interline agreements, regional communities and regional residents come up short. When regional residents are forced to deal with two or more airlines to get to their final destination, their travel costs increase, their bags cannot be checked through, they end up paying duplicate fees and taxes, and there is no requirement to re-accommodate in the event of a missed connection. Surely, we should expect that passengers originating in northern and other regional communities should be afforded the same degree of legislated passenger protection and the same seamless connections as those passengers travelling between larger southern centres.

While the widespread benefits of interline agreements are significant and self-evident, one has to wonder why they have not evolved naturally. In fact, they have in international markets. Both Canadian mainline carriers have recognized that they cannot fly economically to everywhere in the world and that bilateral air services agreements restrict their ability to do so, even if they wanted to. Air Canada lists 105 interline and/or codeshare agreements on their website, but only four of these are with Canadian domestic carriers. WestJet lists 48 interline and/or codeshare agreements on their website but only three are with Canadian domestic carriers. Because bilateral air services agreements provide some degree of economic control in the international marketplace, carriers tend to use interline and code share agreements to expand their reach. Both Canada and the US have been deregulated for more than 30 years and one of the by-products in both countries has been a significant consolidation of airlines. Canada pretty much has a duopoly and the US is down to a handful of very large carriers and, while this may not be a big problem in a large market and a healthy economy, it is a problem for Canada's smallest communities and the carriers that serve them. From their own mutual experience in dealing with one another, Air Canada and WestJet are likely both pretty sensitive to just how quickly a new market entrant can become a major competitive threat in a deregulated environment and this likely explains their reluctance to entertain domestic interline agreements.

The risk of deregulation leading to consolidation and ultimately leading to reduced competition was acknowledged in the 2000 Commons Transport Committee Report dealing with the takeover of Canadian Airlines International by Air Canada (Committee Report No. 1 - TRAN (36-2) - House of Commons of Canada (ourcommons.ca)). Two of the 42 recommendations contained in the report deal specifically with interlining and code share and read as follows:

> "**Recommendation #12** – The government require, as a condition of approval, that a dominant carrier negotiate interline agreements under commercially reasonable terms and conditions with all new entrants and existing carriers in the domestic market wanting such agreements.
>
> **Recommendation #13** – The government require, as a condition of approval, that a dominant carrier code share with new entrants and existing carriers with which it has interline agreements."

The notion of increasing competition by levelling the playing field warrants further explanation. Approximately 50% of Yukon market traffic is between Whitehorse and the primary gateway city of Vancouver, while the other 50% of the market is travelling between Whitehorse and other cities in Canada, as well as international destinations. Without an interline agreement, we can only effectively compete for traffic to and from the places we fly to directly while our competitor has access to 100% of the market. Furthermore, those people travelling to and from places that we don't fly to have no competitive choice. With an interline agreement we can sell seamless travel anywhere and Yukoners will have a competitive choice no matter where they are going.

Mandatory interline agreements would come at no cost to the government, and would not be breaking new policy ground. Similar provisions are already in place in the rail and telecommunications sectors where powerful dominant carriers are compelled to cooperate with smaller players to ensure competition in the face of potential monopolies or duopolies. Furthermore, mandatory interline agreements would have little impact on mainline carriers as there are less than a dozen routes in Canada where a regional carrier competes with a mainline carrier.

The Yukon is the only territorial or provincial region in Canada that has its own air transportation network, locally headquartered, and locally owned, by more than 1,500 Yukoners, including the Vuntut Gwitchin First Nation. Reconciliation, environmental protection, economic development, and quality of life for Yukoners are all government priorities and the inability of the Yukon air travel network to connect with the rest of the country and the rest of the world is a major impediment to the achievement of these priorities. Modern technology is more than capable of ensuring seamless connectivity to the world from even the most remote communities and there is no reason why Yukoners should not be afforded this access. Air North, Yukon's Airline neither needs nor wants to expand into markets that do not relate directly to the Yukon and we are focusing all of our efforts on sustainability rather than growth. We can achieve all the success we need right here in our own back yard but in order to operate sustainably, including timely fleet upgrades to increase fuel efficiency and enhance customer experience, and to continue to provide the affordable travel that Yukoners and visitors have come to expect, we need to make sure that we can compete for 100% of Yukon market traffic.

Joseph Sparling, PRESIDENT
AIR NORTH, YUKON'S AIRLINE

2020 Travellers' Choice Tripadvisor

Best Airline
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