



Australian Government

International Air Services Commission

DECISION

Decision: [2008] IASC 216
Variation of : [2004] IASC 120, [2006] IASC 103 and [2006] IASC 124
The route: Japan
The applicant: Qantas Airways Limited
(ACN 009 661 901) (Qantas)
Public Register: IASC/APP/200817

1 The application

1.1 Qantas applied to the Commission on 12 August 2008 for a variation of three determinations (see above) allocating capacity on the Japan route. As background to the application, Qantas noted that Jetstar had commenced services in March 2007 on a Sydney-Osaka-Brisbane-Sydney routing and Japan Airlines began code sharing on Jetstar's services in May 2007. This followed authorisation of the Jetstar – Japan Airlines code share arrangements by the Commission, in Decision [2007] IASC 204 of 14 March 2007, for the period ending 30 June 2009.

1.2 Qantas sought the substitution of the Gold Coast (Coolangatta) for Brisbane on the route being flown by Jetstar. The current conditions of the Commission's authorisation of code sharing between Jetstar and Japan Airlines require the Commission's approval to change the city pairs served. Qantas also sought an extension until 31 December 2010 of the period of authorisation of the code share arrangements. Qantas asked for the variations to take effect from 1 October 2008 when Jetstar substitutes the Gold Coast for Brisbane on its services to Osaka.

1.3 Qantas explained that the change to the Gold Coast was because demand for Jetstar's services came mainly from Japanese holidaymakers, most of whom were destined for the Gold Coast after arriving in Brisbane. Qantas also noted that airport fees at Gold Coast (Coolangatta) airport were lower than at Brisbane airport, providing a cost reduction for Jetstar. Qantas explained that two of the seven weekly Gold Coast services would not extend to/from Sydney, but these two flights would connect with Jetstar's domestic services to Sydney. All of the Gold Coast services would connect to/from Melbourne on daily Jetstar domestic services.

1.4 The existing free sale code share arrangements would continue with the change from Brisbane to the Gold Coast. Japan Airlines would code share on all sectors of Jetstar's services.

1.5 The Commission published a notice on 18 August 2008 inviting submissions about the application. A submission was received on 1 September 2008 from Tourism Queensland supporting the Qantas application. Public material supplied by the applicant is filed on the Register of Public Documents. Confidential data supplied by Qantas as a

condition of approval of the code share arrangements is filed on the Commission's Confidential Register.

2 Traffic Levels

2.1 The table below summarises traffic levels on the Japan route for the year ending June 2008, compared with the previous year. It shows that total traffic fell by over eight percent, year on year. However, there are markedly different trends in traffic growth between the Australian resident and Japanese visitor segments of the market. While the resident market has been rising, the larger visitor component has been falling steadily for some years.

2.2 Visitor numbers in the year to June 2008 declined by nearly 15%. There were about 181,000 fewer Japanese visitors to Australia than in the previous twelve months period. By contrast, the number of Australian resident travellers to Japan in the year ending June 2008 increased by 57,000 over the year before. The result of these opposing trends changes is that Australian resident travel now makes up over 21% of traffic on the route, compared with less than 16% just one year previously.

AUSTRALIA - JAPAN

MONTHLY ORIGIN-DESTINATION TRAFFIC SUMMARY

LATEST YEAR ENDING DATA	JUN 2007 PAX	JUN 2008 PAX	PAX EWEW or OW	% CHG
TOTAL OD TRAFFIC	1,470,061	1,345,992	12,942 EWEW	-8.4%
TOTAL VISITORS (ARR & DEP) (Proportion of Total OD Traffic)	1,237,566 (84.2%)	1,056,506 (78.5%)	10,159 EWEW	-14.6%
TOTAL RESIDENTS (ARR & DEP) (Proportion of Total OD Traffic)	232,492 (15.8%)	289,492 (21.5%)	2,784 EWEW	24.5%
TOTAL ARRIVALS (VIS & RES)	732,430	671,499	12,913 OW	-8.3%
TOTAL DEPARTURES (VIS & RES)	737,631	674,493	12,971 OW	-8.6%
TOTAL VISITOR ARRIVALS	618,594	527,983	10,154 OW	-14.6%
TOTAL RESIDENT DEPARTURES	118,658	145,974	2,807 OW	23.0%
SHORT TERM VISITOR ARRIVALS	609,302	518,932	9,979 OW	-14.8%
SHORT TERM RESIDENT DEPARTURES	114,453	141,958	2,730 OW	24.0%

Source: Australian Bureau of Statistics

3 Provisions of the relevant air services arrangements

3.1 The air services arrangements between Australia and Japan permit code sharing between the designated airlines of Australia and Japan. Where airlines of the two countries code share with each other, capacity is counted as being exercised only by the operating carrier. Accordingly, the Commission's approval is required for Japan Airlines to code share on flights operated by Jetstar between Sydney/Gold Coast and Osaka.

4 Summary of submission received

4.1 Tourism Queensland supported approval of the code share arrangements between Jetstar and Japan Airlines. Although the number of Japanese visitors to Queensland had declined in recent years, Japan remained the single largest international source market to Cairns and the Gold Coast. In the year ended March 2008, there were 328,000 Japanese visitors to Queensland, which attracts almost two of every three Japanese tourists to Australia. This generates an estimated \$479 million in direct visitor expenditure and supports about 4,600 tourism jobs in Queensland. Japan is also an important export market for Queensland, with much of the market made up of time sensitive perishable products which depend on regular air services.

4.2 In Tourism Queensland's view, stand alone Jetstar's services are sustainable only through co-operative arrangements with the incumbent carriers in the Australia – Japan market. In particular, the proposed arrangement provides access to Japan Airlines' distribution system. The code share arrangement would facilitate a smooth transition from Qantas to Jetstar's services and sustain strong Japanese visitor numbers.

5 Commission's consideration

5.1 When considering applications to vary determinations, the Commission must decide whether the determinations, as varied, would be of benefit to the public. Under section 6.3 of the Minister's policy statement, where a carrier requests a variation of a determination to allow it flexibility in operating its capacity, including to use Australian capacity in a code share arrangement with a foreign carrier, and no submission is received about the application, only the criteria in paragraph 4 of the policy statement are applicable. Under paragraph 4, the use of entitlements by an Australian carrier that is reasonably capable of obtaining the necessary approvals and of implementing its proposals is of benefit to the public.

5.2 Under Section 15(2)(e) of the Act, the Commission must include a condition in determinations stating the extent to which the carrier may use that capacity in joint services with another carrier. The Minister's policy statement indicates that the Commission would generally be expected to authorise code sharing but where it has serious competition concerns about a particular proposal is able to subject it to detailed consideration against the public benefit criteria contained in paragraph 5 of the policy statement.

5.3 The Commission has for some years assessed thoroughly applications from Qantas for code sharing with Japan Airlines on the Japan route because of concerns about the potential impact of such arrangements on competition in this large market. Most recently, in June 2008, the Commission reviewed code sharing by Japan Airlines on Qantas' services between Tokyo and Cairns and between Tokyo and Melbourne.

5.4 In that review, the Commission noted the ongoing weakness in Japanese visitor demand for travel to Australia. While partially offset by growing numbers of Australian residents flying to Japan, the overall traffic trend continued a downward decline that has persisted for some years. The Commission also took account of Qantas' announcement that it would withdraw its Tokyo – Melbourne services from September 2008 and end its Cairns – Tokyo services from December 2008, with Jetstar taking over flying on the Cairns – Tokyo sector. In light of these circumstances, the Commission authorised a continuation of code sharing on the Cairns and Melbourne to Tokyo services to the end of 2008, without subjecting the application to the detailed paragraph 5 criteria of the Minister's policy statement. Qantas has now applied to the Commission for Jetstar to code share with Japan Airlines on the Cairns – Tokyo sector. That application is the subject of a separate Commission decision.

5.5 Previously, in March 2007, the Commission had authorised code sharing by Japan Airlines on Jetstar's Sydney/Brisbane – Osaka services, the route which is the subject of Qantas' current application. The introduction of this code share arrangement coincided with the withdrawal of Japan Airlines' services between Australia and Osaka. The Commission found in its March 2007 decision that the code share arrangements were likely to assist the viability and maintenance of frequency of the services in difficult market circumstances, without leading to adverse public benefit outcomes. The change from Brisbane to the Gold Coast in the Osaka services, as now proposed by Qantas, reflects a further adjustment to the major Qantas-group scheduling changes announced by Qantas in June 2008.

5.6 Little has changed in the Australia – Japan market since the Commission's June 2008 review. The decline in overall traffic has continued over recent months, with no sign of recovery in the Japanese visitor market to Australia. The Commission refers interested readers to Decision [2008] IASC 212 of 16 June 2008 for discussion of the possible reasons for the ongoing weakness in the Japanese visitor market. In the continuing weak market circumstances, there is no cause for the Commission to subject the current application to the paragraph 5 criteria in the Minister's policy statement.

5.7 The Commission has reviewed confidential commercial data reported to it by Qantas for Jetstar's operations on the Sydney/Brisbane – Osaka services, since the implementation of the code share arrangements with Japan Airlines in May 2007. Yields on the Brisbane–Osaka sector are slightly higher than on the Sydney–Osaka sector and other sectors on which Qantas reports data to the Commission. However, broadly speaking, yields remain subdued on all of these Japan sectors.

5.8 Overall, this review suggests to the Commission that the code share partners have not been pricing in a way which is detrimental to public benefits on the route. Looking to the future, the Commission notes that attractive fares are being offered for sale by Jetstar on the new Gold Coast – Osaka sector. This may result in lower yields on

this sector compared with Brisbane–Osaka, at least for some time. On the cost side, the Commission is aware of the impact on operating costs on the route over the past year as a result of significantly higher fuel prices. The combination of weak yields, falling demand and cost pressures have been the catalyst for the major changes to the Qantas-group’s operations on the Japan route through 2008.

5.9 The Commission sees little potential for adverse competitive outcomes to develop from the code share arrangements continuing to the end of 2010 as sought by Qantas, given the continuing weak state of the Australia–Japan market. Accordingly, the Commission considers that there is likely to be no lessening of public benefit from allowing Jetstar to continue to use the relevant capacity in code share services with Japan Airlines until 31 December 2010. The Commission will grant authorisation for this period.

5.10 The Commission will also authorise the change in point to be served on the Osaka services from Brisbane to the Gold Coast. The change does not represent a fundamental alteration to the existing competitive circumstances, since most Japanese visitor traffic arriving in Brisbane is already destined for the Gold Coast. Accordingly, there is also likely to be no lessening of public benefit associated with the shift in services to the Gold Coast.

5.11 The Commission will vary the three determinations concerned, as sought by Qantas. The variations will take effect from 1 October 2008, when the operational substitution of the Gold Coast for Brisbane occurs. The Commission will maintain the same conditions of approval as currently apply in relation to the existing code share arrangements.

6 Decision ([2008] IASC 216)

6.1 In accordance with section 24 of the Act, the Commission varies Determinations [2004] IASC 120, [2006] IASC 103 and [2006] IASC 124 as requested by Qantas, by:

6.2 *deleting with effect from 1 October 2008*

- “Jetstar may use the capacity to provide services jointly with Japan Airlines until 30 June 2009 in accordance with:
 - the codeshare agreement of 9 February 2007, signed by Jetstar and Japan Airlines, with such additional conditions (if any) as the Commission may require, prior to code share services commencing, or as varied except in relation to:
 - Sydney/Brisbane – Osaka being the city pair served; or
 - any financial adjustment; or
- Jetstar must submit to the Commission reports six-monthly on the number of code share seats sold by Japan Airlines on Jetstar-operated services between

Sydney/Brisbane - Osaka; and its yields per revenue passenger kilometre for all passenger classes on these services”.

6.3 *adding with effect from 1 October 2008*

- “Jetstar may use the capacity to provide services jointly with Japan Airlines until 31 December 2010 in accordance with:
 - the codeshare agreement of 9 February 2007, as amended, with such additional conditions (if any) as the Commission may require prior to code share services commencing, or as varied except in relation to:
 - Sydney/Gold Coast – Osaka being the city pair served; or
 - any financial adjustment; or
- Jetstar must submit to the Commission reports six-monthly on the number of code share seats sold by Japan Airlines on Jetstar-operated services between Sydney/Gold Coast–Osaka; and Jetstar’s yields per revenue passenger kilometre for all passenger classes on these services”.

Dated: 12 September 2008

John Martin
Chairman

Philippa Stone
Member