



Australian Government

International Air Services Commission

DECISION

Decision: [2010] IASC 213
Variation of: [2007] IASC 108
The route: Japan
The applicant: Qantas Airways Limited
(ACN 009 661 901) (Qantas)
Public Register: IASC/APP/201024

1 The application

1.1 Qantas applied to the Commission on 25 November 2010 for a variation of Determination [2007] IASC 108 to enable a new code sharing arrangement with Japan Airlines on Qantas operated services between Perth and Tokyo Narita, for the duration of the determination which ends on 9 August 2013.

1.2 The Commission published a notice on 25 November 2010 inviting submissions about the application. A submission was received on 2 December 2010 from Westralia Airports Corporation Pty Ltd (WAC) in support of the Qantas application.

1.3 All public material supplied by the applicant and submissions are filed on the Register of Public Documents.

2 Provisions of the relevant air services arrangements

2.1 The air services arrangements between Australia and Japan allow code sharing between the designated airlines of Australia and Japan. Under these arrangements, where the designated airlines code share with each other, capacity is counted as being exercised only by the operating carrier. As Qantas is the operating carrier, the Commission's approval is required for Japan Airlines to code share on Qantas' flights.

3 Summary of submission received

3.1 As noted above the Commission received a submission from WAC in support of Qantas' application to permit Japan Airlines to code share on its services. WAC noted that Qantas is the only airline operating non-stop services between Perth and Japan, offering three services per week to Tokyo Narita.

3.2 WAC further noted the decline in Japanese visitors arriving through Perth Airport. However, it said that Japanese visitors are still the seventh largest nationality group passing through Perth Airport and represent an important source of tourism.

3.3 WAC submits that due to the modest size of the Perth – Tokyo market and the

fact that it has been declining, WAC consider it unlikely that Japan Airlines or another airline would chose to serve the market in competition with Qantas. WAC consider that allowing Japan Airlines and Qantas to code share on the route will not affect competition and the arrangements are likely to strengthen the route due to Japan Airlines marketing Perth through its network.

4 Commission's consideration

4.1 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 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. Qantas is an established carrier which clearly meets the paragraph 4 criteria in this case.

4.2 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.

4.3 The Commission has for a number of years subjected to careful scrutiny Qantas' applications for code sharing with Japan Airlines on other sectors of the Japan route. This is because of concerns about the potential impact of such arrangements on competition in this large market where Qantas and Japan Airlines are the only direct operators. However, the continued weakness in demand on the Japanese route has meant that the Commission has not seen sufficient concern with the proposed code sharing arrangements to subject them to the paragraph 5 criteria.

4.4 Recently, the Commission reviewed the code share arrangements between Qantas and Japan Airlines on Jetstar's Cairns – Tokyo , Gold Coast – Osaka, Cairns – Osaka and Gold Coast – Tokyo services. On 11 November 2010, the Commission issued Decision [2010] IASC 210 varying Determinations [2006] IASC 117, [2006] IASC 124 and [2008] IASC 127, allowing Jetstar Airways to code share with Japan Airlines.

4.5 In reviewing the code share arrangements in that case, the Commission noted that the weakness in demand has led to extensive restructuring of services on the Japan route over recent years, with Japan Airlines and Qantas both ending services on a number of sectors.

4.6 The result of the various changes over time is that the scope of code sharing between Qantas Group carriers and Japan Airlines has contracted, with Melbourne and Sydney being dropped from the code sharing arrangements.

4.7 Traffic levels on the Japan route have been volatile since the Commission's 2008 reviews but the downwards trend of the past six years or so has continued. That trend has correlated with a generally rising Australian dollar, making travel to Australia more expensive, and a weak Japanese economy which has seen reduced numbers of Japanese travelling overseas.

4.8 There were very large month on month declines in visitor traffic through the later months of 2008 and throughout 2009. This period coincided with the working through of the effects of the global financial crisis and a weak Japanese economy. The situation stabilised through the first five months of 2010 and strong growth was evident in June, July and August 2010, however visitor number have fallen during the month of September 2010 down to 2008 levels. Australian resident travel has continued to grow steadily and now makes up a substantial proportion of the overall market where once it was a very minor part.

4.9 Overall, the Australia – Japan market remains subdued and in the continuing weak market circumstances, the Commission sees no grounds on which to subject the current application to the paragraph 5 criteria in the Minister's policy statement.

4.10 The proposed free-sale code sharing arrangements will enable Japan Airlines to maintain a presence on the Perth-Tokyo sector through Qantas' three services to Tokyo per week. The Commission has previously considered that Japan Airlines would be unlikely to enter the Cairns – Tokyo and Gold Coast – Osaka sectors in its own right. Similarly, given the subdued market the Commission considers Japan Airlines is unlikely to enter the modestly sized Perth – Tokyo market in its own right in the near future. This view is supported by WAC who consider it unlikely that Japan Airlines or another airline would choose to serve the market in competition with Qantas. The recent withdrawal of Japan Airlines from the larger volume Brisbane – Tokyo sector, as part of an extensive program of international service reductions by that airline, further supports this view.

4.11 Even though the free-sale code share arrangements tend to be less competitive than block space arrangements, the addition of Japan Airlines is likely to introduce an element of competition for Qantas on the modest Perth – Tokyo sector. Further, the marketing and distribution network of Japan Airlines will assist in strengthening the marketing of these services and of Perth as a destination.

4.12 The Commission is satisfied that there would be no lessening of public benefits by allowing code sharing to commence on the Perth – Tokyo sector. The Commission further considers there is little prospect of anti-competitive behaviour arising from the arrangement. In particular, the Commission notes that several airlines offer indirect services between Perth and Tokyo, including Cathay Pacific via Hong Kong, Singapore Airlines via Singapore, and Thai Airways via Bangkok. While indirect services are often considered to add a degree of inconvenience for travellers, indirect flying times on the Perth – Tokyo sector only increase by a couple of hours, in some instances, compared with direct flights. They also provide options for attractive stopovers.

4.13 As noted above, present subdued traffic levels remain at present. Nevertheless, if demand pressures build unexpectedly on the Japan route, there continues to be potential for the emergence of adverse impacts of the arrangements on competition.

However, a positive aspect to the past weakness in the Japan market is that there is now scope for a new Australian entrant. There is substantial capacity now available for allocation as a result of the return of capacity by Qantas over recent years. At one time, virtually all of the Australian capacity entitlements were allocated to Qantas. The potential threat of entry by another Australian carrier might impose some further degree of pricing discipline upon the Qantas Group.

4.14 While the Commission considers there would be no lessening of public benefits, the Commission will authorise the arrangements until 31 December 2012 rather than authorising the arrangements for the remainder of Determination [2007] IASC 108 as sought by Qantas. This will bring the Perth – Tokyo code share arrangement into line with the recently approved code share arrangements on the Cairns – Tokyo , Gold Coast – Osaka, Cairns – Osaka and Gold Coast – Tokyo services which expire on 31 December 2012, making it administratively easier for Qantas to seek approval to continue the arrangements in one application.

4.15 The Commission will maintain its usual conditions requiring Qantas to report on traffic carried by Japan Airlines on Qantas' services and Qantas' revenue yields for the code share sectors.

5 Decision [2010] IASC 213

5.1 In accordance with section 24 of the Act, the Commission varies Determination [2007] IASC 108, as requested by Qantas, by :

adding the following conditions to the Determination:

- the capacity may be used by Qantas to provide services jointly with Japan Airlines in accordance with:
 - the signed code share agreement between Qantas and Japan Airlines for services between Perth and Tokyo Narita, subject to the agreement being received and approved by the Commission prior to services commencing; or
 - any subsequent code share agreement between Qantas and Japan Airlines for operations on the Australia – Japan route with the prior approval of the Commission;
- under any code share agreement with Japan Airlines:
 - Qantas must price and sell its services on the route independently of Japan Airlines; and
 - Qantas must not share or pool revenues on the route with Japan Airlines.
- Qantas must submit, prior to the next Commission review of the code share arrangements, a report on the number of code share seats sold by Japan Airlines on

Qantas-operated services between Perth –Tokyo and Qantas' yields per revenue passenger kilometre for all passenger classes on these services

Dated: 10 December 2010

Ian Smith
Member Presiding

Stephen Bartos
Member