QANTAS

15 March 2018

Ms Marlene Tucker
Executive Director
International Air Services Commission
GPO Box 630
Canberra ACT 2601

Dear Ms Tucker,

Code share arrangements between Qantas and Air Niugini

On 2 March 2018, Virgin Australia provided comments in relation to Qantas' application regarding code sharing arrangements with Air Niugini between Australia and Papua New Guinea (PNG). Qantas submits the following comments in relation to Virgin Australia's submission.

Firstly, it is relevant to provide an update to Virgin Australia's overview of the PNG route based on the most recent Bureau of Infrastructure, Transport and Regional Economics (BITRE) statistics available (12 months ending December 2017). Between 2016 and 2017, the number of passengers travelling on the PNG route fell by 1% based on seat capacity growth of 2%. Passenger and freight volumes on the Brisbane-Port Moresby market grew by 2% and 4% respectively in 2017.

Qantas increased its seat capacity share by 5% to represent 22% of total seats on the route in 2017 with its entry on the Brisbane sector, almost equivalent to its change in market share which grew from 17% to 24%. Both Air Niugini and Virgin Australia passenger and capacity market shares fell in 2017.

Virgin Australia's passenger and capacity market shares were 18% and 20% respectively in 2016. In 2017, Virgin Australia's passenger market share was 13%, compared to capacity market share of 19%. Air Niugini's passenger and capacity market shares on the PNG route fell by 2% (to 63%) and 4% (to 59%) respectively.

Total freight volumes on the PNG route increased by 2% between 2016 and 2017. Virgin Australia and Air Niugini were the only carriers to increase freight volumes and market share in 2017. For Virgin Australia, volumes increased by 15% to record market share of 6%. Air Niugini's freight volumes rose 5% and recorded a 75% market share. The amount of freight carried by Qantas fell by 34% in 2017 representing a 2% market share and Pacific Air Express Australia volumes decreased by 9%.

Virgin Australia's submission noted Qantas' reference to the uniqueness of the PNG route. Many of these characteristics have been highlighted in its submission including the high proportion of price-inelastic passengers travelling for business purposes. As a result, it is unlikely that the availability of lower airfares can meaningfully stimulate demand. These characteristics are evident in the relatively low load factors experienced by all carriers on the PNG route in 2017 – Qantas 56.8%, Air Niugini 54.1% and Virgin Australia 34.7%.

Virgin Australia's submission attributed the deterioration of its performance on the Brisbane sector to the support the code share services are providing to Qantas and Air Niugini. However, it is by no means clear that the code share arrangements rather than the entry of Qantas' operated services between Brisbane and Port Moresby or commercial considerations unrelated to the code share arrangements have influenced Virgin Australia's current position.

The Commission has continuously approved the Qantas and Air Niugini code share arrangements since 2002 and in doing so has confirmed that public benefit has derived from the code share. An important benefit for business travellers – a significant customer segment on the PNG route – is access to frequent flyer programs. While as Virgin Australia has noted, Qantas frequent flyer points are available for travel on Air Niugini operated flights absent the code share, the ability to earn status credits and access to Qantas lounges for tiered passengers is not. **[CONFIDENTIAL INFORMATION REDACTED].**

Virgin Australia's submission argues that the route service possibilities would still be available for passengers absent the parallel code share services on the Brisbane sector. However, passengers would lose connectivity to 11 destinations across Australian domestic and international sectors gained by Qantas placing its code on Air Niugini's Port Moresby-Brisbane services, in addition to the connectivity that Qantas operated services provide.

The current environment has led to highly competitive pricing by all three carriers on the PNG route. **[CONFIDENTIAL INFORMATION REDACTED].**

Despite Virgin Australia questioning the relevance of Air Niugini's viability, the Commission has previously indicated its concern that a reduction in Air Niugini's services or withdrawal entirely, would result in a substantial lessening of competition. In its submission to the Commission, Air Niugini has again highlighted its potential vulnerability including the potential material risk to the Sydney sector and likelihood of substantially withdrawing from operating wide body aircraft on the Brisbane route absent the code share.

Virgin Australia suggests that Air Niugini has a commercial interest in maintaining wide-bodied services on the Brisbane sector absent a code share arrangement with Qantas. However, in its comments to the Commission, Air Niugini is emphatic that both the passenger and air freight component of the code share arrangement is crucial to the sustainability of wide-bodied operations on the route. **[CONFIDENTIAL INFORMATION REDACTED].**

Virgin Australia asserts that it can uplift individual items of freight up to a maximum weight of 60kg on its narrow-bodied aircraft. Qantas' uplift is limited to a maximum weight of 32kg per piece for workplace safety reasons, but there are also significant instances of freight movements more than 60kg that are not suitable for a narrow-bodied aircraft and require loading into a Unit Load Device onto a wide-bodied aircraft. For example, it would not be possible to load mining equipment, perishable products and aviation parts and machinery into a B737 passenger aircraft, which are regularly exported from Australia.

With respect to the markets between each of Cairns, Sydney and Townsville and Port Moresby, Virgin Australia asserts that the code share services are potentially acting as a barrier to entry by another carrier in the future. However, it is possible that absent the code share arrangements these routes could continue to be served by a single direct carrier, as we have seen with the Cairns sector, with the potential for significantly higher prices and lower frequency as a result. In the absence of the entry of a new operator on the route, greater public benefits would be delivered through retention and proposed expansion of the code share arrangements.

In these circumstances, it is not necessary to impose commercially restrictive and administratively burdensome conditions. In Qantas' view, the application of conditions has contributed to the market distortions on the PNG route and is not appropriate.

Yours sincerely,

Rohan Garnett
Executive Manager, International Affairs