TELECONFERENCE WITH DR CHRIS PLEATSIKAS, 10 AUGUST 2012

Commissioners present:
Dr Jill Walker, Chairwoman
Mr Stephen Bartos, Member

Secretariat officers present:
Mr Chris Samuel
Ms Anita Robinson

Other Attendees:
Ms Jennifer Orr (ACCC)

The Commission held a teleconference with Dr Chris Pleatsikas to discuss his views on the Qantas application to allow South African Airways (SAA) to continue to code share on its Sydney-Johannesburg services until 31 March 2016.

Dr Pleatsikas said that, on the basis of the information before him, he is prepared to believe, subject to a more detailed analysis of data on traffic, revenues and costs, that:

- only two airlines can sustain direct services between Australia and South Africa;
- most likely the direct services would be confined to the Sydney and Perth routes;
- while lots of outcomes are possible, it is not implausible that eliminating the code share would result in two monopolistic routes;
- the indirect services offered by third country airlines are pretty competitive with the indirect services offered by Qantas and SAA (e.g. services between South Africa and Brisbane/Melbourne); and
- there currently does not appear to be sufficient traffic to sustain direct services by three airlines.

Dr Pleatsikas said that the major concern with the current code share arrangement is that the formula Qantas is using to calculate the cost of seats appears to include cost categories that may be inappropriate given the objective of promoting competition between the airlines on its route. In particular, some cost categories appear to include fixed costs. To promote competition, the code share airlines should focus on the incremental costs associated with operating the specific route and divide those costs by the number of seats (differentiating the costs of providing economy, business and first class seats where appropriate).

Dr Pleatsikas said there is a need for much more clarity and insight into the incremental costs of flying the Sydney-Johannesburg route. The fuel charge seems reasonable, but in relation to the non-fuel charges there appear to be a number of fixed costs included that are inconsistent with a more competitive outcome under the code share arrangement (i.e., because some included costs may not be incremental to the operation of the specific route). Among the cost categories of concern are passenger insurance, in-flight entertainment costs, aviation safety fees, station engineering, cabin crew support (e.g., administrative functions), flight support overheads, port support overheads and technical crew training and support.

He said he is concerned that the calculated cost of a seat is too high relative to the incremental costs associated with operating the specific route, which puts an effective floor under the price at which seats are on-sold to passengers. In his view, given repeated interactions between the airlines, the current arrangement could support a cosy duopoly between Qantas and SAA.

Dr Pleatsikas said the main issue with the current code share arrangement in relation to public benefits is the pricing of seat allocations. If the pricing is too high, the public benefits from the arrangement are not what they could be. However, the crux of the matter is whether the code share arrangement leads to more competition than if the code share were allowed to lapse (particularly if the most likely outcome would be that each airline operated their current respective routes as monopolists). In his view, it would be a tough call to say that there is a significant gain from the code share arrangement. On the other hand, it would not be easy to demonstrate the negative (i.e. establish that the code share agreement on balance results in disbenefits).

Record prepared by Chris Samuel