AUSTRALIAN COMPETITION & CONSUMER COMMISSION

Airline competition in Australia

Report 11: March 2023

accc.gov.au

Australian Competition and Consumer Commission
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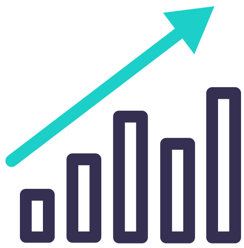
Glossary

ABS	Australian Bureau of Statistics
BITRE	Bureau of Infrastructure and Transport Research Economics
CASA	Civil Aviation Safety Authority
CCA	*Competition and Consumer Act 2010* (Cth)
Larger city	Sydney, Melbourne, Brisbane, Adelaide, Perth, Canberra or the Gold Coast.
Load factor	The total number of passengers as a proportion of the total number of seats flown across all airlines.
LCC	Low-cost carrier
Qantas	Qantas domestic passenger airlines that include Qantas Domestic and QantasLink airlines.
Qantas Group	Qantas Domestic, QantasLink and Jetstar Domestic airlines.
Regional	Domestic locations other than Sydney, Melbourne, Brisbane, Adelaide, Perth, Canberra and the Gold Coast.
TANS	Tourism and Aviation Network Support Program. An Australian Government program introduced in response to COVID-19 to reduce the costs for consumers to fly to key tourism regions.
Virgin Australia	Virgin Australia domestic passenger airlines that include Virgin Australia and Virgin Australia Regional Airlines (VARA). Virgin Australia also operated Tigerair until March 2020.

Key industry insights and developments

Airfares fall from historic highs in late 2022

After reaching a 15-year high in December 2022, discount fares declined 34% in January 2023. Average revenue per passenger, which represents average prices across all fare types, fell by 13% in January 2023, but remained 13% higher than pre-pandemic levels (29% higher in nominal terms).



Airlines increase their flying without compromising on-time performance

The domestic airlines flew 5.9 million seats in January 2023, the most since May 2022. Despite the increase in flying, most airlines reported a lower rate of delayed flights, indicating a growing operational capability as the aviation industry rebuilds its workforce. Jetstar reported relatively poorer performance.

Airlines report profitable operations

The airlines have reported profitable operations on the back of strong demand and high airfares. Qantas Group reported an underlying profit before tax of $1.43 billion for the first half of 2022–23, which is close to the company's record for a full year of operations. Rex's intercity jet operations have also been profitable.

New airline Bonza commences operations

Bonza's launch in late January 2023 made it the first high-capacity airline to enter the Australian domestic market in 15 years. Bonza's network of 27 routes connects regional hubs to holiday destinations across Queensland, New South Wales and Victoria. Bonza is predominantly flying routes that would otherwise be unserved.

Low-cost carriers have been an important driver of competition around the world

Bonza's entry as an independent low-cost carrier will help to provide Australian budget travellers with more route choice and competition on certain routes. Jetstar has been the only low-cost domestic operator since Tigerair exited in 2020. Globally, the emergence of low-cost carriers in recent decades has led to new competition in air travel and more people flying.

Overview

Airfares have begun to drop following historic highs at the end of 2022. Average revenue per passenger, which represents average prices across all fare types, fell by 13% between December 2022 and January 2023. The fall was most evident in the price of discount fares, which fell by 34% between December 2022 and January 2023. Restricted economy and business fares decreased slightly over this same period. Discount, restricted economy and business fares remained at a similar level in February.

While it is common for airfares to fall after the Christmas peak due to a seasonal decline in demand, some of the change in airfares can be explained by the airlines increasing seat capacity.

The industry increased seat capacity to 5.9 million in January 2023, the highest level since May 2022. Qantas flew 102% of the capacity it flew pre-COVID-19 (January 2019), compared to 96% for Virgin Australia and 84% for Jetstar.

While the airlines increased their capacity, this did not result in more passengers flying. 4.4 million passengers flew in January 2023, 89% of pre-pandemic levels (January 2019). Increased capacity and a seasonal reduction in demand resulted in more empty seats, with the industry-wide load factor falling to 75% in January 2023, 8 percentage points below October 2022 (83%).

Jet fuel prices are trending downwards, which should enable airlines to reduce airfares in coming months. Jet fuel prices decreased to $166 per barrel in February 2023, a 35% fall since a record high in June 2022, but still remain above 2019 levels.

The airlines managed to increase their flying in January 2023 without significantly compromising on-time performance, suggesting that most airlines are getting closer to their pre-pandemic operational capability. The industry reported that 23.3% of flights arrived more than 15 minutes late in January, the best result in over 9 months. The industry cancellation rate did not improve to the same extent, with the airlines cancelling 3.1% of all flights in January. Both the delay and cancellation rate remain above the long-term average (18.5% and 2.1% respectively). While most airlines improved their delay and cancellation rates over the last few months, Jetstar's performance was relatively poorer. Jetstar reported the highest rate of delayed (34.6%) and cancelled flights (7.3%) in January of the airlines and has consistently reported the highest cancellation rate since July 2022.

In a significant development for competition in the industry, new low-cost carrier Bonza launched in late January 2023. Bonza is the first high-capacity passenger airline to enter the Australian market since Tigerair 15 years ago. Bonza is also the first independent low-cost carrier in the market since Virgin Australia acquired Tigerair in 2013.

Bonza's network covers 27 routes across Queensland, New South Wales and Victoria. Bonza is launching predominantly unserved routes that directly connect regional centres to holiday destinations.

Bonza's entry as a low-cost carrier will provide Australian budget travellers with more route choice and competition on certain routes. In recent decades, low-cost carriers have been responsible for much of the new competition in global air travel which in turn has led to more people flying. Budget travellers in Australia once benefited from dynamic competition between Virgin Blue, Jetstar and Tigerair. Jetstar has dominated this customer segment over the past decade with the transition of Virgin into a full-service carrier and then the exit of Tigerair in 2020.

Where an airline enters or alters capacity or pricing on a route serviced by Bonza, or where an airline enters into exclusive arrangements with service providers, the ACCC may investigate whether this practice is anti-competitive and breaches competition law.

The airlines have reported profitable operations for the first 6 months of the financial year. Qantas Airways reported a very high underlying profit before tax of $1.43 billion for the first half of the 2022–23 financial year. This figure was close to the company's record profit for a full year of operations. While reporting an overall statutory loss for the first half of 2022–23, Rex's intercity operations have been increasingly profitable within the period. While Virgin Australia CEO Jayne Hrdlicka said she expected the airline to report revenue of around $2.5 billion, and a profit margin of around 5%, in its half-year results. Virgin Australia's owner Bain Capital announced it was seeking advice on a potential initial public offering and relisting of the airline.

In 2021–22 the ACCC received 1,740 contacts involving Qantas, the most of any company and 68% higher than the previous year. While the broader industry struggled with processing COVID-19 related cancellations and remedies, and the surge in demand since pandemic-related restrictions were eased, the ACCC received fewer contacts about Jetstar (down 33% to 544) and Virgin Australia (down 27% to 359). While a contact does not necessarily mean there has been a breach of the law, an increased number of contacts is generally indicative of a high level of dissatisfaction with that company. As Australia's largest airline, and an airline that generally charges a premium to fly, consumers expect a better service. Qantas needs to do more to adequately invest in its systems, processes and people to dramatically improve its customer contact services and customer dispute resolution.

The ACCC produces these reports under a direction from the former Treasurer to monitor the prices, costs and profits of domestic air passenger transport services. The direction was issued in June 2020 and is due to expire in June 2023. This Airline Competition in Australia report is the ACCC's 11th and penultimate report under the existing direction.

1. Introduction

The Australian Competition and Consumer Commission (ACCC) is an independent Commonwealth statutory agency that promotes competition, fair trading and product safety for the benefit of consumers, businesses and the Australian community. The primary responsibilities of the ACCC are to enforce compliance with the competition, consumer protection, fair trading and product safety provisions of the *Competition and Consumer Act 2010* (Cth) (CCA), regulate national infrastructure and undertake market studies.

On 19 June 2020 the former Treasurer issued a direction to the ACCC under subsection 95ZE(1) of the CCA to monitor prices, costs and profits relating to the supply of domestic air passenger transport services.

The direction requires the ACCC to report on its monitoring at least once every quarter. This is the ACCC's 11th and penultimate report on its findings from monitoring domestic air passenger transport services. The direction is due to expire in June 2023.

In announcing the direction, the former Treasurer stated that the ACCC's monitoring will assist in protecting competition in the sector for the benefit of all Australian airline travellers.[1] The former Treasurer also said that the reporting role and focus by the ACCC would provide another avenue for those wishing to raise concerns about anti-competitive conduct in the sector.

The ACCC's monitoring and reporting on the domestic airline industry is separate, but related, to its enforcement of competition law under Part IV of the CCA. We will prioritise investigations about anti-competitive agreements and practices, and the misuse of market power. We will consider enforcement action where we form the view that conduct is likely to breach the CCA.

In its monitoring, the ACCC may find that the level of competition within the industry is insufficient to meet the needs of consumers, or it may identify anti-competitive behaviour that falls short of thresholds for enforcement action. We will recommend potential policy options to government should we identify practical action the government could take to improve competition.

Under the direction, the ACCC can compel information from industry participants. We have established arrangements to collect monthly and quarterly data from the Qantas Group (including Jetstar), Virgin Australia and Rex. These airline groups supply the vast majority of regular domestic air passenger services in Australia. We also seek qualitative information from the airlines from time to time, such as Board papers about company strategy. The ACCC has legislative obligations in relation to how it manages and discloses confidential information so only some information collected from the airlines will be presented in the public monitoring reports.

The ACCC's first report published in September 2020 contains further information about our approach to the monitoring direction and potential investigations.[2]

1 The Hon. Josh Frydenberg (the former Treasurer), *ACCC directed to monitor domestic air passenger services* [media release], 19 June 2020, accessed 21 November 2021.

2 ACCC, *Airline competition in Australia – September 2020 report*, 17 September 2020.

2. Industry developments

2.1 Improvements in capacity and on-time performance signal airlines may be getting closer to pre-pandemic capability

After extensive operational challenges for much of 2022, the airlines managed to increase their seat capacity in January 2023 without significantly compromising on-time performance. The industry increased capacity to 5.9 million seats January 2023, the highest level since May 2022. Qantas flew 102% of its pre-COVID-19 capacity (January 2019), compared to 96% for Virgin Australia and 84% for Jetstar.[3]

Virgin Australia increased its flights between Perth and the east coast cities over December and January.[4] The recovery in industry capacity is expected to continue. In February the Qantas Group announced it expects both Qantas and Jetstar will fly 103% of their pre-COVID-19 capacity levels by April–June 2023.[5] This is aided by Qantas adding more flights to the 'golden triangle' routes connecting Sydney, Melbourne and Brisbane, and replacing the aircraft on its Sydney and Melbourne to Perth routes with A330 wide-bodied aircraft from late March.[6]

Rex will also be in a position to increase its capacity when it acquires an additional 2 x Boeing 737 aircraft in June–July 2023. The new jets will take Rex's total jet fleet to 9 in addition to its 61 x Saab 340 turboprops.[7]

In January 2023 the industry reported the lowest rate of delayed arrivals (23.3% or 9,931) in over 9 months (table 1). The industry cancellation rate did not improve to the same extent, with the industry cancelling 3.1% of all flights (1,381 flights). The industry cancellation rate has remained between 2.9–4.4% over the last 6 months. Both the rate of cancellations and delays remain above the long-term averages (2.1% and 18.4% respectively).

Table 1: Domestic cancellations and delays – October 2022 and January 2023

	Cancelled flights (%)		Delayed arrivals (%)	
	October 2022	January 2023	October 2022	January 2023
Qantas	2.2	2.8	25.8	18.3
Rex	2.2	0.7	31.7	18.9
Virgin Australia	3.6	2.2	35.1	26.2
Jetstar	3.9	7.3	35.6	34.6
Industry total	**2.9**	**3.1**	**30.7**	**23.3**
Long-term ave		**2.1**		**18.4**

Note: A delayed arrival is a flight that arrives 15 minutes or more after the scheduled arrival time shown on the airline's schedule. A flight is regarded as a cancellation if it is cancelled or rescheduled less than 7 days prior to its scheduled departure time. The industry total and long-term average is weighted across all airlines and all airports.

Source: BITRE, Australian domestic on time performance monthly reports. Qantas figures include QantasLink and Virgin Australia figures include VARA.

3 Figure for Virgin Australia excludes Tigerair; Jetstar's recovery figure may be understated because it flew unusually high capacity in January 2019.

4 Cockburn, G, The West Australia, 'Virgin Australia reveals it is working at capacity during holiday travel surge', 21 December 2022, accessed 2 February 2023.

5 Based on capacity measured by Available Seat Kilometres; Qantas, '1H23 results presentation', 23 February 2023, accessed 23 February 2023.

6 Qantas, *Qantas encourages customers to use travel credits with double points offer* [media release], 15 December 2022, accessed 23 February 2023.

7 Rex, *Rex signs LOI for two more Boeing 737-800NG jets* [ASX release], 14 February 2023, accessed 14 February 2023.

While most airlines improved their delay and cancellation rates over the last few months, Jetstar has struggled with its performance. Jetstar's frequency of delayed flights improved from October 2022, but it still had the highest rate of late (34.6%) and cancelled (7.3%) flights of the airlines in January 2023. Jetstar's January 2023 cancellation rate was 2.4 percentage points above its October 2022 result, and it has consistently reported the highest cancellation rate of the airlines since July 2022.

Qantas reported the lowest rate of delayed arrivals in January 2023 at 18.3%, its best result in almost a year. Similarly, Virgin Australia reported its best in almost a year, with 26.2% of delayed arrivals in January 2023. Following a few months of higher delays, Rex reported 18.9% delayed arrivals in January 2023, in line with Rex's pre-pandemic performance (2019).

Rex reported the lowest cancellation rate in January 2023 at 0.7%, followed by Virgin Australia with 2.2% and Qantas 2.8%. While Rex and Virgin Australia decreased their cancellation rates between October 2022 and January 2023, Qantas' increased marginally.

With the airlines increasing capacity and most airlines reporting improvements in their performance over the last few months, the industry appears to be getting closer to its pre-pandemic operational capability.

The industry is not having to deal with high levels of sick leave due to COVID-19 and other illnesses like it did in mid-2022. However, Qantas reported the industry continues to face operational challenges, including from aircraft manufacturer delays, supply chain dislocations and labour availability and training.[8] Airline cancellations and on-time performance are also impacted by the performance of aviation partners, including air traffic controllers, security and other airport personnel. It was reported that there is a high level of absenteeism among air traffic controllers, particularly at Sydney Airport, causing disruptions to travel operations.[9]

Performance should continue to improve as the broader aviation industry rebuilds its workforce. The next challenge for the industry will be the Easter holiday period, typically a peak time for leisure travel.

2.2 New low-cost carrier Bonza takes off

New low-cost carrier Bonza completed its regulatory approval process in January 2023 and started flying regularly scheduled flights from mid-February 2023.

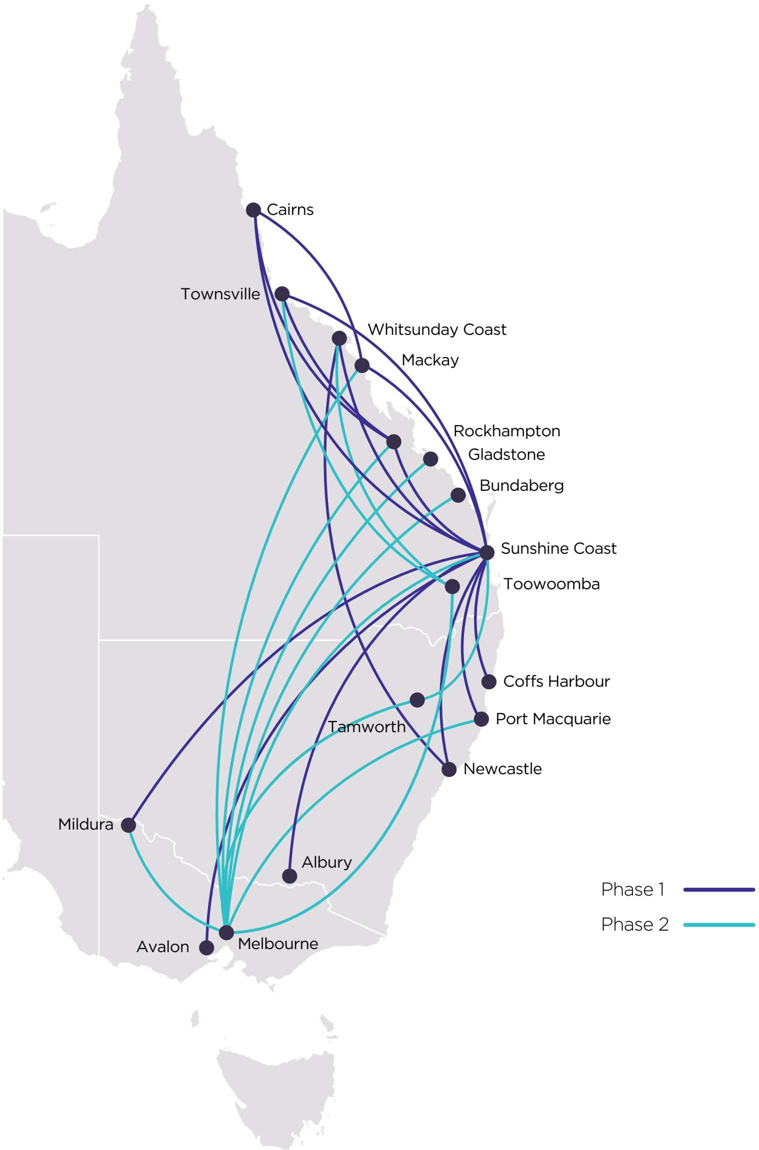
Bonza is offering low airfares on predominantly new routes

Bonza's network covers 27 routes to 17 destinations across Queensland, New South Wales and Victoria (figure 1). Bonza is currently flying 15 routes from its Sunshine Coast hub (Phase 1) and will start flying the remaining 12 routes from its Melbourne (Tullamarine) hub from the end of March 2023 (Phase 2). Bonza has 4 x 186-seater Boeing 737 MAX 8 aircraft, with a 5th arriving shortly. Bonza hopes to expand to 8 jets in its first year of operations.

8 Qantas, 'Qantas Group HY23 Appendix 4D and interim financial report', 23 February 2023, accessed 23 February 2023.

9 Baird, L, Australian Financial Review, 'The 'alarming' workforce trend causing flight delays', 19 February 2023, accessed 23 February 2023.

Figure 1: Bonza's route network



Bonza is owned by US private investment firm 777 Partners which owns Canada's low-cost carrier Flair. Bonza is leasing its aircraft from 777 Partners, which has ordered 134 x Boeing 737-MAX aircraft since 2021.[10] This suggests that the airline will have access to a pipeline of available aircraft if or when it expands.

Bonza's cheapest available fares range from $49–89 per person, which is consistent with earlier statements by CEO Tim Jordan that passengers could expect to pay around $50 for every hour they are in the air. Consumers will need to pay extra for checked baggage, seat selection and food & drink. This 'no-frills' fare-type is similar to Jetstar's 'Starter' fare and Virgin's 'Lite' fare.

Bonza is distinguishing itself from the other airlines by launching predominantly new routes that connect regional centres to holiday destinations, allowing passengers to travel directly rather than via a major city. In contrast, Qantas, Jetstar, Virgin and Rex primarily service the major city trunk routes in addition to routes connecting larger cities with regional locations in the same state or territory.

Bonza is operating 2–5 flights per week on each route. This relatively infrequent schedule allows Bonza to service its 27 routes with only 4–5 aircraft. While the larger airlines have more aircraft, they also

10 Boeing, *777 Partners expands 737 MAX fleet, ordering up to 66 more fuel-efficient jets* [media release], 19 July 2022, accessed 30 January 2023.

prioritise frequency of service alongside network reach, operating numerous daily services on the majority of their routes. Even smaller airline Rex services only 7 routes with its 7 x Boeing 737 aircraft, allowing Rex to offer more daily services on busy larger city routes. More frequent services enable the airlines to attract passengers that prioritise flexibility and convenience, in particular business travellers.

In contrast, Bonza is targeting price-sensitive leisure passengers that are likely to be more flexible with the time of day or week they travel. Further, Bonza is hoping to generate new demand, attracting holidaymakers that would ordinarily choose not to travel, or to travel via an alternative form of transport.[11] As such, establishing new connections to build new markets is a bigger priority for Bonza than offering a frequent schedule.

Bonza hopes to be able to maintain low prices for consumers with its low-cost model. The MAX 8 aircraft, which Jordan says Bonza acquired for a 'phenomenal' deal[12], are brand new and therefore should incur minimal maintenance costs. Bonza should also be able to keep operating costs down as the aircraft are 14–20% more fuel-efficient than other Boeing 737 models.[13] To keep airport charges down, Bonza sought expressions of interest and favourable arrangements from a wide range of airports before settling on its network. Bonza is also aiming to consistently fill its planes to above 90%, allowing it to recoup its costs across more passengers.[14]

Bonza is reducing costs by not having a call centre, with Bonza's phone app the only means of contacting the airline if a consumer has a dispute. Bonza is not selling tickets through its website, rather the only way consumers can book flights direct is through the app.[15] Consumers will need to use the app for food & drink purchases as Bonza is not operating a trolley service on board.

CEO Tim Jordan reported that Bonza sold over 10,000 tickets within a few days of launching.[16] 777 Partners founder Steve Pasko said he expects Bonza to run at a loss for 12 months but hopes it will become profitable in its second year.[17]

Consumers will benefit from more direct flights

Bonza's launch is a significant development in the history of Australia's airline industry. Bonza is the first high-capacity passenger airline to enter the domestic market since Tigerair 15 years ago. Bonza is also the first independent low-cost carrier in the market since Virgin Australia acquired Tigerair in 2013.[18] Tigerair has since exited the market. See chapter 4 for further discussion on low-cost carriers and their history in Australia.

For many consumers, the primary benefit of the new airline is through the additional connectivity. Once Bonza's 27 routes are operational, the number of domestic routes in Australia will increase by 16% from current offerings. Consumers living near one of the 17 locations will have more direct flights for holidays and visiting family and friends. Some of these direct flights will replace long car trips, or otherwise encourage tourists to new destinations.

Bonza's launch also benefits consumers through competition. Most notably, Bonza will directly compete with other airlines on the following 2 contested routes:

- Melbourne – Sunshine Coast, currently operated by Qantas, Virgin and Jetstar
- Melbourne – Mildura, currently operated by Qantas and Rex.

11 Jordan, T, CAPA Centre for Aviation, 'CAPA Live: Exclusive interview with new Australian LCC Bonza', 13 October 2021, accessed 17 February 2023.

12 Thorn, A, Australian Aviation, 'Bonza got a 'phenomenal deal', on the 737 MAX, says founder', 27 October 2021, accessed 2 February 2023.

13 Boeing, 'Boeing 737 MAX' website, accessed 2 February 2023.

14 Dye, J, ABC News, 'The US private equity giant funding Australia's new budget airline Bonza', 1 February 2023, accessed 2 February 2023.

15 Consumers can book indirectly through certain travel agents.

16 Bonza, *It's a Bonza day as Bonza gets wheels up* [media release], 31 January 2023, accessed 10 February 2023.

17 Dye, J, ABC News, 'The US private equity giant funding Australia's new budget airline Bonza', 1 February 2023, accessed 2 February 2023.

18 Virgin initially acquired 60% of Tigerair in 2013, and the remaining 40% in 2014.

In addition to having an additional choice of airline, travellers on these 2 routes may also benefit from some form of competitive response from the other airlines such as reduced airfares. However, any response may be somewhat limited given that Bonza will only be offering a few flights per week on each route, at least initially.

While Bonza's stated strategy is to operate on unserved and underserved routes, Bonza may expand into more contested routes in the future, including possibly larger intercity routes. This would represent a more significant competitive threat to the other airlines.

The other impact of the new competition is the potential for consumers to be persuaded by the cheap airfares to travel to a destination offered by Bonza instead of an alternative destination with another airline. This could create some competitive pressure on other airlines to offer more attractive airfares on certain routes that may be seen as similar in the minds of travellers. Further, Bonza's low airfares may also influence consumer expectations of what constitutes an attractive airfare that can entice someone to fly, putting pressure on the other airlines to keep their fares low.

To date, none of the other airlines have entered or withdrawn from the 27 routes in Bonza's network.

Where an airline enters or alters capacity or pricing on a route serviced by Bonza, or where an airline enters into exclusive arrangements with service providers, the ACCC may investigate whether this practice is anti-competitive and breaches competition law.

2.3 Many consumers have contacted the ACCC about Qantas

Qantas figured prominently in reports made to the ACCC by the general public in 2021–22. The ACCC received 1,740 contacts involving Qantas in 2021–22, the most of any company and 68% higher than the previous year. The number of contacts involving Qantas was over a third higher than the second most reported company. Key causes of the increased reports included issues around remedies for flights cancelled due to COVID-19 travel restrictions and the high levels of cancelled or delayed flights in mid-2022 that occurred during the post-pandemic surge in demand.

While it has been well recognised that the broader travel industry struggled with processing COVID-19-related cancellations and remedies, and has also struggled with a surge in demand since pandemic-related restrictions were eased, both Jetstar (down 33% from 2020–21 to 544) and Virgin Australia (down 27% from 2020–21 to 359) were the subject of fewer contacts in 2021–22.

These contact numbers are raw data. Contacts do not always mean that a business has acted in breach of the Australian Consumer Law (ACL) or broader *Competition and Consumer Act 2010* (the CCA). These figures will include:

- contacts where consumers have enquired about their rights on an issue (as opposed to making a complaint about an airline's conduct)
- contacts where consumers are complaining about conduct that would not give rise to a breach of the ACL or the CCA
- contacts where an airline is perceived to be responsible for parts of the aviation supply chain they do not control (e.g. airport facilities, air traffic control)
- complaints about the airlines' conduct where the allegations have not been confirmed or verified.

Notwithstanding these caveats, such an increased level of contacts is generally indicative of a high level of dissatisfaction with that company, and issues with that company's ability to handle and resolve customer complaints. Qantas' customer service issues, in particular long call wait times, have been well reported in the media. As Australia's largest airline, and an airline that generally charges a premium to fly, consumers expect a better service. Qantas needs to do more to adequately invest in its systems, processes and people to dramatically improve its customer contact services and customer dispute resolution.

The ACCC is continuing to investigate a number of issues that consumers have raised about Qantas, and whether these issues raise concerns under the ACL.

2.4 International capacity on the rise as China reopens

The international travel market continues to recover as more airlines, and seat capacity, return to the market.

Most notably, China opened its international border in January 2023 after nearly 3 years. Within weeks of opening, 6 mainland Chinese airlines increased flights to Melbourne and Sydney, including the 3 largest China Southern, China Eastern and Xiamen Air.

China was Australia's leading visitor market pre-pandemic, with 1.3 million visitors in Australia in 2019 (15% of all arrivals).[19] With China's main airlines increasing services, Melbourne Airport chief executive Lorie Argus said she expected Melbourne Airport's international capacity to reach 80% of its pre-COVID-19 levels by the end of March 2023.[20]

The return of Chinese carriers is expected to have an impact on international airfares, with travel agent Flight Centre noting that the Chinese airlines that service Australia are 'very price-focussed'.[21] Further, China serves as a base for serval airlines flying to and from other destinations, with the Australian Federation of Travel Agents noting that China had been one of the most cost-effective ways to get to Europe because so many carriers flew there.[22]

However, it will take time for the airlines to plan networks and staffing to return to pre-pandemic levels.

Qantas reported it expects to return to 79% of international capacity by April–June 2023.[23] To support Qantas ramping up its international capacity, it is in the process of reactivating 10 of the A380s that it grounded during the pandemic. However, Qantas CEO Alan Joyce said it will take time before the A380s are ready to fly. Qantas uses these high-capacity, long-haul aircraft to fly to destinations such as Los Angeles, Dallas, Hong Kong and Singapore. Qantas also announced it will be acquiring an additional 3 x Boeing 787-9 Dreamliners in June this year to expand its international services. Joyce said the new aircraft would allow Qantas to 'keep its fares lower'.[24]

Similarly, Emirates, the fourth largest airline operating to and from Australia in 2019[25], reported it would return to pre-pandemic capacity in the first half of this year.[26]

The additional capacity is expected to bring down airfares, although high prices are still being driven by strong demand and relatively high jet fuel prices.

The most recent available figures show that international arrivals and departures recovered to 67% and 68% respectively of pre-pandemic levels in December 2022.[27] These figures do not take into account recent developments, in particular, China's reopening.

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19 Tourism Research Australia, 'International visitor survey results 2022 – 2019 comparison' spreadsheet, 21 December 2022, accessed 2 February 2023.

20 McGuire, A, The Age, 'Melbourne Airport to hire 2000 people to cope with the return of China's airlines', 16 January 2023, accessed 2 February 2023.

21 Hannam, P, The Guardian, 'Travel between China and Australia tipped to rebound rapidly as Chinese airlines ramp up flights', 11 January 2023, accessed 1 February 2023.

22 Moore G & Bennett, T, Australian Financial Review, 'China's reopening could bring down cost of Europe flights: agents', 28 December 2022, accessed 1 February 2023.

23 Based on capacity measured by Available Seat Kilometres; Qantas, '1H23 results presentation', 23 February 2023, accessed 23 February 2023.

24 Croft, D, Australian Aviation, 'Qantas to receive three additional Boeing 787 Dreamliners', 7 February 2023; Booth, J, Dmarge, 'Alan Joyce reveals when flights prices will go back to normal', 9 February 2023, accessed 10 February 2023.

25 Based on seat capacity market share; BITRE, Australian Government, 'Seat utilisation factors by airline 1991 to current International Airline Activity – flights seats – October 2022' spreadsheet, accessed 1 February 2023.

26 Cant, A, The New Daily, 'Emirates boosts flights to pre-pandemic levels in Australia', 23 January 2023, accessed 1 February 2023.

27 Figures are the number of border crossing rather than the number of people; ABS, Australian Government, 'Overseas arrivals and departures, Australia, December 2022', accessed 17 February 2023.

2.5 Domestic airlines report profitable operators

After several years of significant losses due to the pandemic, the major domestic airline groups have recently reported profitable operations. These results have been driven by months of strong demand, full aircraft and higher airfares.

Qantas Airways reported an underlying profit before tax of $1.43 billion for the first half of the 2022–23 financial year. This result captures performance across the whole business, including international and domestic flying (including Jetstar), freight and the loyalty program. The underlying profit was 49% higher than the prior first half record result from 2017–18. The company's record underlying profit before tax for a full year of operations is $1.6 billion (2017–18). The domestic operations of Qantas and Jetstar were responsible for most of the recent result with underlying earnings before interest and tax of $915 million.[28]

While reporting an overall statutory loss, Rex reported 4 months of increasing profits before tax on its intercity operations in September–December 2022. Rex stated its regional operations had not performed as well, however; they were expected to return to profitability this quarter (January–March 2023).[29]

In January 2023 Virgin Australia CEO Jayne Hrdlicka said she expected the airline to report revenue of around $2.5 billion, and a profit margin of around 5%, in its half-year results.[30] This would be the first time in over a decade that Virgin Australia reports a profit.[31] Virgin Australia also reported record demand from the small-medium enterprise business market, with bookings from this customer segment surpassing 110% of pre-pandemic levels in January 2023.[32]

Virgin Australia's owners Bain Capital announced it was seeking advice on a potential initial public offering and relisting of the airline. Bain Capital stated it would retain a significant shareholding in the event Virgin Australia is relisted.

2.6 Government is seeking views on future aviation policy

The Australian Government has asked for submissions to help it develop long-term policies to guide the future development of the aviation sector. The government will develop an Aviation White Paper to articulate its policies on desired aviation outcomes in relation to safety, competitiveness, sustainability and efficiency.

The government published the terms of reference for the process on 7 February 2023. Topics to be explored include the economic reforms needed to improve productivity across the sector, including addressing skills shortages, competition in relation to airports and airlines, and charting a course out of the pandemic. Stakeholders can provide initial views responding to the terms of reference by 10 March 2023. These submissions will inform the development of a Green Paper.

Following the release of the Green Paper in mid-2023, a second round of more detailed consultation will be undertaken, which will be considered during the development of the White Paper. The White Paper is expected to be released in the first half of 2024.

In a separate process, the Australian Government has been reviewing the demand management scheme at Sydney Airport. The review, which commenced in late 2020 under the previous government,

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28 Qantas, 'Qantas Group HY23 Appendix 4D and interim financial report', 23 February 2023, accessed 23 February 2023.

29 Rex, 'Half year financial report: 31 December 2022', 28 February 2023; Rex, Rex announces 1HFY23 financial results [ASX release], 28 February 2023, accessed 28 February 2023.

30 Yun, J & Bonyhady, N, The Age, 'Virgin Australia shuffles top ranks ahead of IPO campaign', 31 January 2023, accessed 1 February 2023.

31 With the exception of 2020–21 when Virgin Australia reported an after-tax profit of $3.7 billion which was largely reflective of a one-off $4.4 billion return recognised on the release of claims owned to Virgin Australia's creditors after administrators executed the sale to Bain Capital in 2020.

32 Virgin Australia, *Virgin Australia drops epic sale on half a million fares from $55 one-way and announces record business traveller growth* [media release], 31 January 2023, accessed 2 February 2023.

is looking at whether various aspects of the scheme remain fit-for-purpose, including implementation of the cap on aircraft movements, measures to ensure access for regional services, and the system for allocating take-off and landing slots to airlines.[33] The review was established following a recommendation by the Productivity Commission in its 2019 inquiry into airports.[34]

At capacity-constrained Sydney Airport, new and expanding airlines can find it very difficult to obtain slots at peak periods, which in turn acts as a barrier to entry and expansion, limiting competition. Reform to the way that slots are allocated between airlines, and measures which better enable the airport to operate closer to its permitted cap on aircraft movements, offers a significant opportunity to improve airline competition into and out of Sydney Airport and Australia more broadly. Better utilisation of slots within the current cap could offer productivity improvements across various sectors.

After a broad consultation process, review Chair Peter Harris reported to government in February 2021 with a series of recommendations to improve the operation of the demand management system. Some stakeholders including the ACCC then participated in a number of working groups organised by the Department of Infrastructure, Transport, Regional Development, Communications and the Arts up until early 2022 to refine details of the Harris recommendations.

33 Department of Infrastructure, Transport, Regional Development, Communications and the Arts, 'Review of Sydney Airport Demand Management Scheme', accessed 10 February 2023.

34 Treasury, 'Australian Government response to the Productivity Commission Inquiry into the Economic Regulation of Airports', December 2019, accessed 10 February 2023.

3. Key industry metrics and analysis

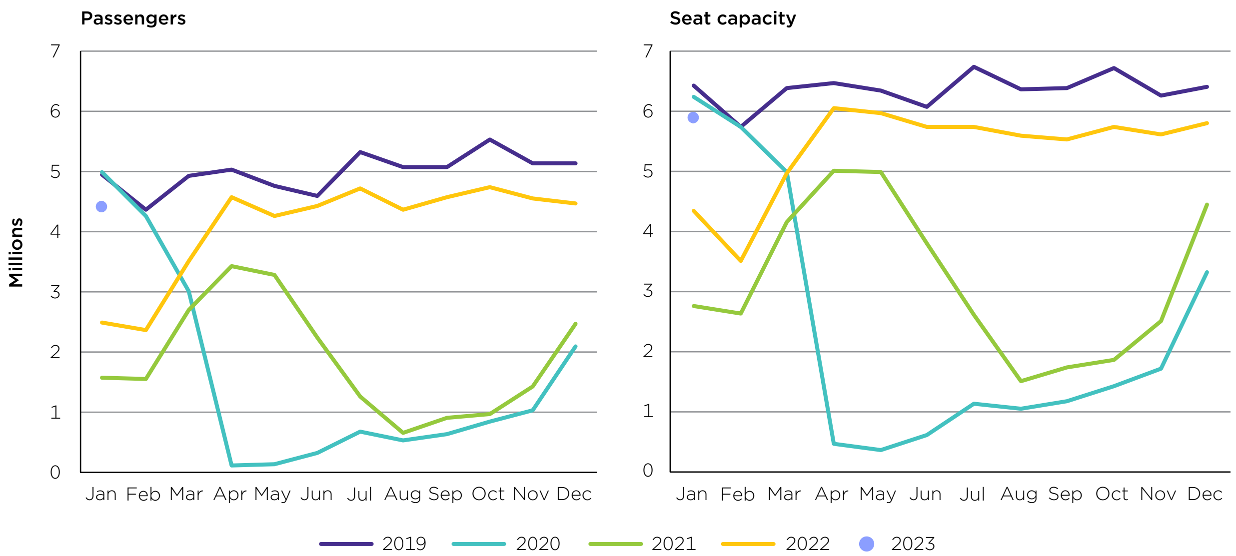
This chapter presents analysis of key industry metrics. Unless specified otherwise, we calculate these metrics from data supplied to the ACCC from the Qantas Group (comprising Qantas and Jetstar), Virgin Australia (including Tigerair until March 2020) and Rex on a monthly and quarterly basis. Data relates specifically to regular passenger transport services and does not include charter services.

This chapter includes analysis on the airline industry up to January 2023. The industry data does not include Bonza because the airline did not commence its regular services until February 2023. Section 3.6 includes analysis of airfare trends using BITRE data up to February 2023.

3.1 Passenger numbers decline despite airlines increasing capacity in December and January

The domestic airline industry carried 4.4 million passengers in January 2023. This represented a decrease of 7% since the recent peak in October 2022. Figure 2 shows that the pattern in the number of domestic passengers over the past year is increasingly looking like it did pre-pandemic in 2019, with peaks around school holidays in April, July and October. While many people fly at Christmas time for leisure, this is typically offset by fewer business travellers.

Figure 2: Australian domestic air services – January 2019 to January 2023



Source: Data collected by the ACCC from Qantas, Jetstar, Virgin Australia and Rex.

While the pattern of monthly domestic passengers is similar to 2019, there are still fewer people flying than they were prior to the pandemic. In January 2023 the number passengers represented around 89% of the number who flew at the same time in 2019, prior to the pandemic. The recovery in passenger numbers continues to remain at or below 90% since it reached a high of 97% in June 2022.

In contrast to passengers, domestic seat capacity has increased in recent months to reach 5.9 million in January 2023. This was the highest number of seats made available since May 2022. On the larger city routes, all airlines increased capacity between November 2022 and January 2023 other than Qantas. Qantas typically reduces capacity at this time of year due to the drop in demand for business travel. This fall in capacity was more than offset by its leisure-based subsidiary Jetstar.

Figure 2 shows that unlike for passenger numbers, the recent pattern of monthly seat capacity does not reflect trends pre-pandemic, in 2019. Capacity did not increase during the school holiday periods in July and October 2022. The high rates of cancellations and delays demonstrated that the aviation supply chain was not able to offer higher levels of flying. However, the increase in capacity in recent months, alongside improved on-time performance, suggests that the aviation sector is improving its operational capability (see section 2.1).

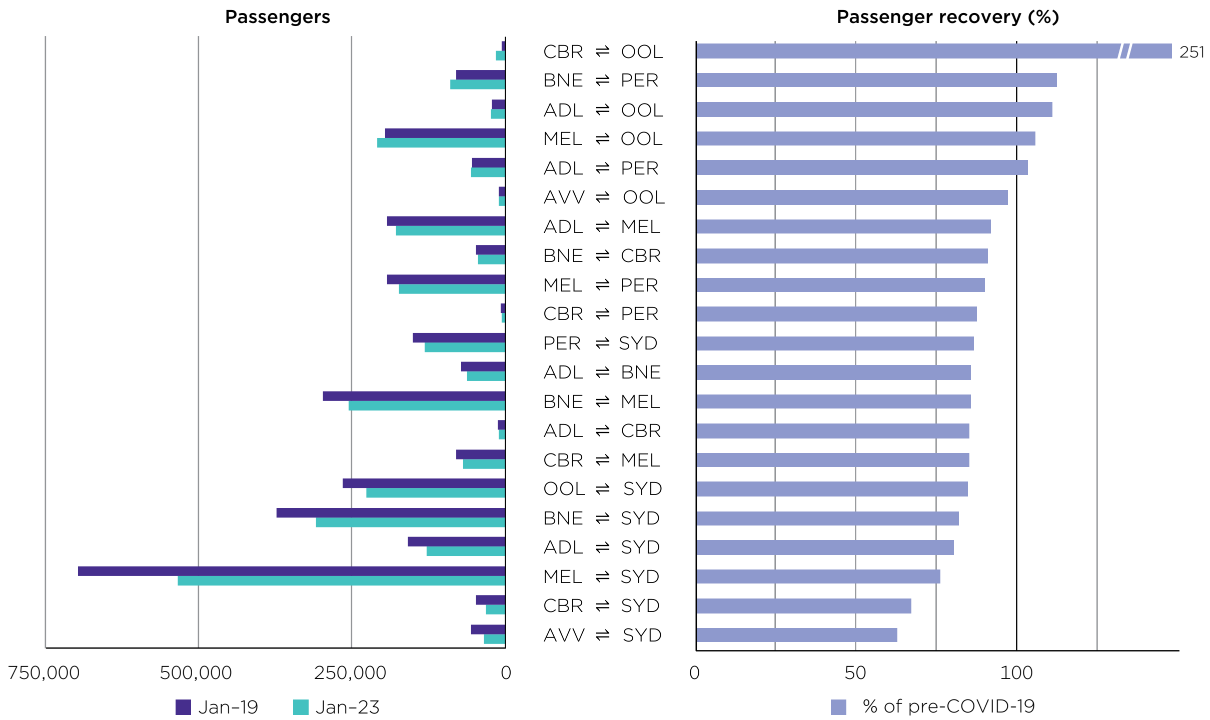
3.2 Relatively fewer routes reported full flights in January

The increase in capacity combined with a decrease in passenger numbers resulted in the load factor decreasing to 75% in January 2023. This was the lowest load factor since May 2022 and was 2 percentage points below the pre-pandemic load factor of 77% in January 2019.

Only 2 routes reported a load factor of 90% or higher in January, in contrast with 17 in October 2022 and 7 in January 2019. The 2 routes were both interstate routes linking popular tourist destinations the Sunshine Coast and Ballina Byron Bay to separate capital cities.

Some routes are recovering from the pandemic faster than others. Figure 3 ranks the routes connecting larger cities by the degree to which they have recovered their pre-COVID-19 levels of passengers. There were 5 routes which reached 100% of pre-COVID-19 passenger levels in January 2023. Of these routes, 3 were to and from the Gold Coast.

Figure 3: Passenger numbers on routes connecting larger cities – January 2023 relative to January 2019



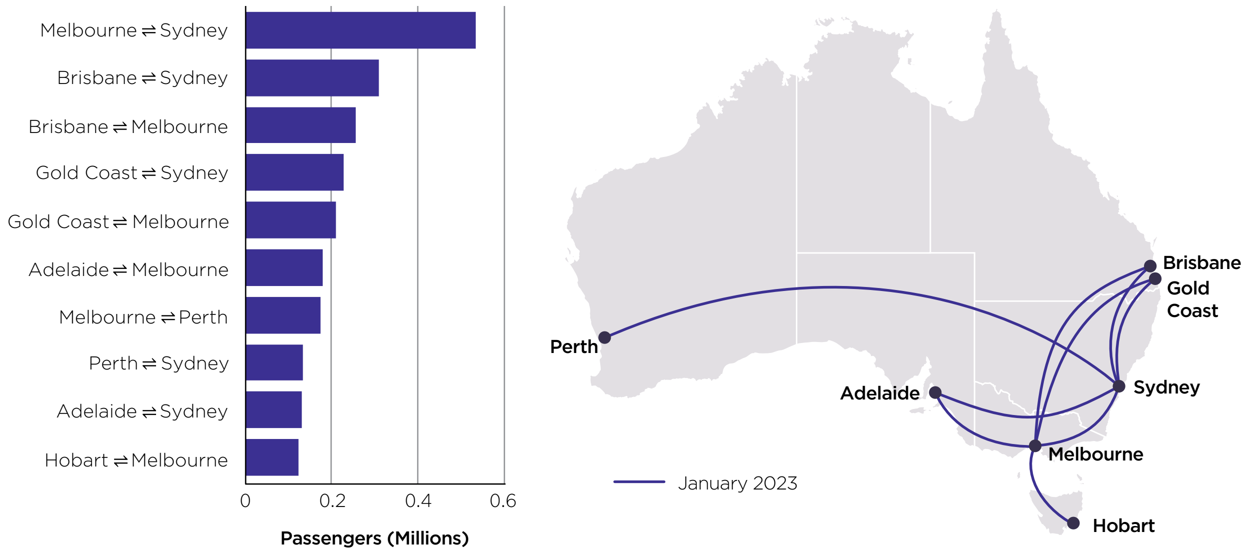
Source: Data collected by the ACCC from Qantas, Jetstar, Virgin Australia and Rex.

Note: ADL – Adelaide, AVV – Avalon, BNE – Brisbane, CBR – Canberra, MEL – Melbourne, OOL – Gold Coast, PER – Perth, SYD – Sydney; Virgin Australia data for 2019 includes data for Tigerair.

The 3 largest routes in Australia – those connecting Brisbane, Melbourne and Sydney – are lagging in their passenger volume recovery compared to other routes connecting larger cities. Melbourne – Sydney was the worst performing of the 3 with passengers in January 2023 equivalent to just 77% of pre-COVID-19 levels. This continues to reflect the greater significance of business travel on these routes, with demand for business travel returning more slowly than leisure travel.

Figure 4 shows the 10 busiest routes in Australia in January 2023 by passenger volume. The top 10 routes list was the same as that in 2019 after Hobart – Melbourne replaced the intrastate Brisbane – Cairns service as the 10th busiest route. Melbourne – Sydney was the busiest route with 533,000 passengers, representing 12% of all domestic passengers in the country.

Figure 4: Busiest routes by monthly passengers – January 2023

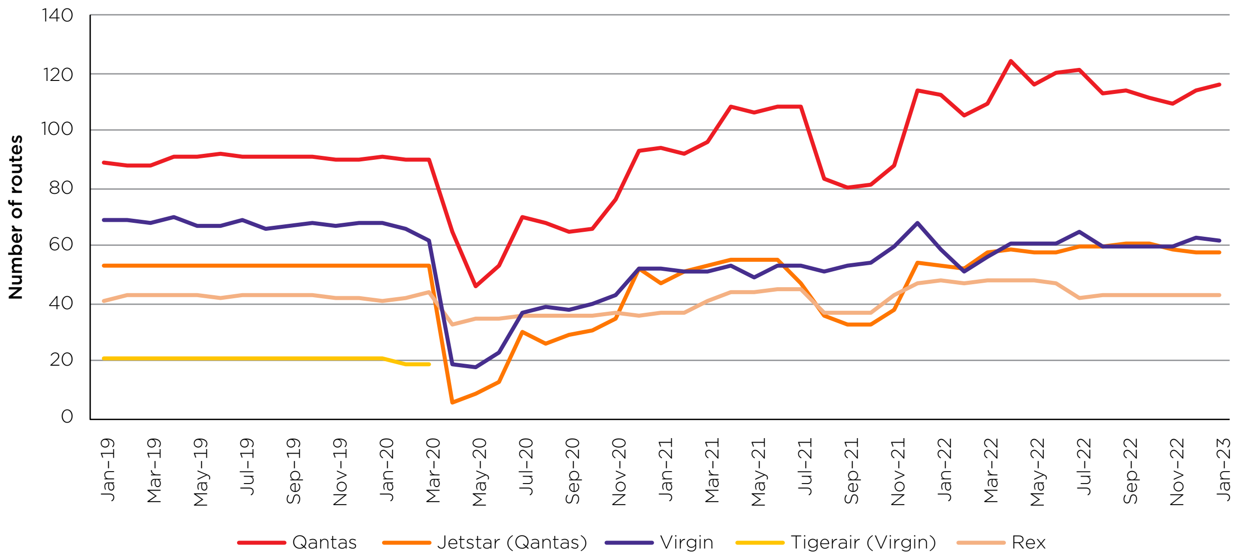


Source: Data collected by the ACCC from Qantas, Jetstar, Virgin Australia and Rex.

3.3 The number of domestic routes has stabilised, but this will change with Bonza

There were 154 domestic routes in operation in Australia in January 2023. This was the same as in October 2022 and was only slightly below the pre-COVID-19 level. The overall size of the domestic network has been relatively stable since April 2022, in contrast to 2020–21 when the airlines frequently changed their route network in response to multiple changes in border restrictions (figure 5). The number of domestic routes will increase from February 2023, once Bonza's entry is taken into account.

Figure 5: Number of domestic routes operated by airlines – January 2019 to January 2023



Source: Data collected by the ACCC from Qantas, Jetstar, Virgin Australia and Rex.

Note: Select multi-hop routes are treated as a single route.

Qantas had the largest domestic network in January 2023 with 116 routes, an increase from 111 routes in October 2022. The airline suspended and resumed some if its seasonal services since October. This includes the suspension of its sole-operated Broome – Sydney service, and resumption of its

Brisbane – Coffs Harbour service in competition with Link Airways, the Melbourne – Merimbula service in competition with Rex, and its Canberra – Sunshine Coast sole-operated service.

Virgin Australia serviced 62 routes in January 2023, which was 2 more than in October 2022. The airline commenced servicing its new Cairns – Perth route on a consistent basis in December, following the initial announcement in May 2021. It also resumed several seasonal interstate services to Tasmanian destinations. Virgin has exited both the Cairns – Gold Coast and the Melbourne – Townsville routes.

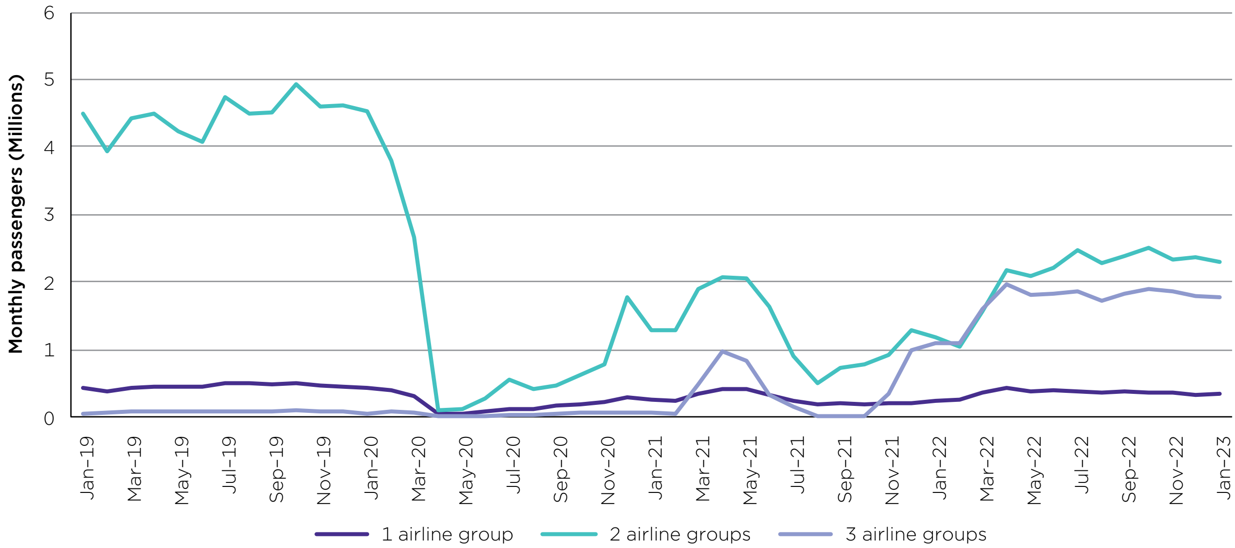
Qantas subsidiary Jetstar operated 58 routes in January 2023, a decrease of 3 routes since October. All 3 were seasonal interstate routes to Uluru, Cairns and the Gold Coast. This includes the Cairns – Newcastle seasonal service, which the carrier will resume in late June 2023.[35]

Rex continued to serve 43 routes in January 2023, the same as in October 2022.

3.4 Most domestic passengers fly on routes with 2 competing airline groups

Consumers are most likely to benefit through better services and more attractive pricing on routes where there are more competing airline groups. Figure 6 shows that 40% of domestic passengers flew on routes with 3 competing airline groups in January 2023. This figure has remained around 40% since July 2022. The increase in this figure in recent years is due to Rex's expansion on major intercity routes since early 2021 in competition with Qantas and Virgin Australia. The proportion of passengers travelling on routes with 2 airline groups was 52% in January.

Figure 6: Number of passengers on routes serviced by 1, 2 and 3 airline groups – January 2019 to January 2023



Source: Data collected by the ACCC from Qantas, Jetstar, Virgin Australia and Rex.

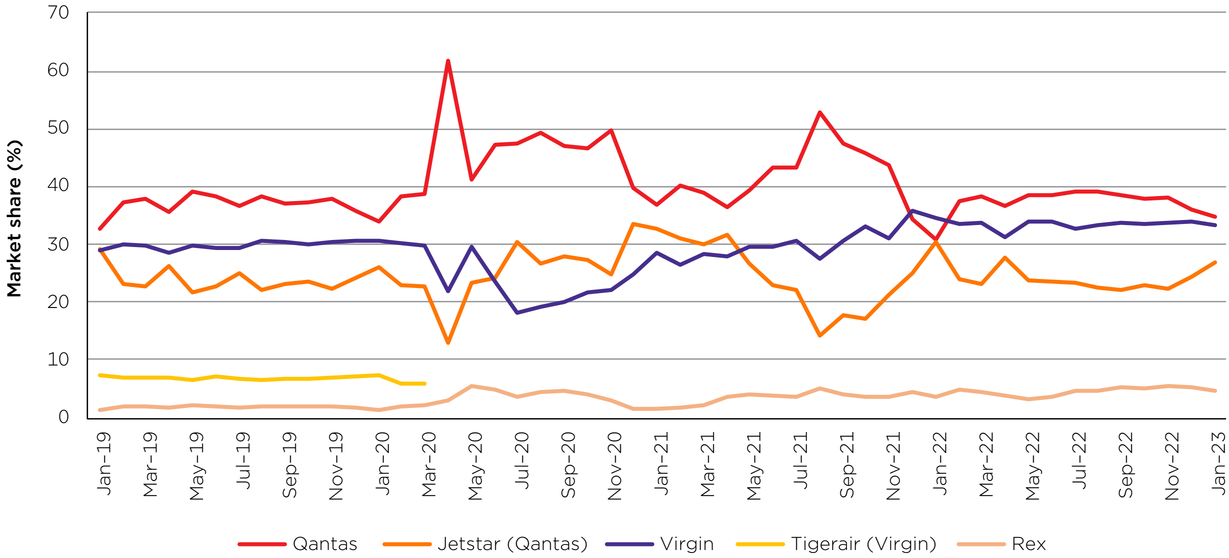
Note: The 3 airline groups are Qantas Group (including Jetstar), Virgin Australia (including Tigerair) and Rex.

35 Jetstar, *Jetstar to recommence seasonal flights between Cairns and Newcastle* [media release], 14 February 2023, accessed 16 February 2023.

3.5 Jetstar recorded higher market share over the summer holiday period

Figure 7 shows that Jetstar's market share increased by nearly 4 percentage points since October to 26.9% in January 2023. This was Jetstar's largest market share since April 2022, and it reflects the seasonal uptick in leisure travel demand the low-cost carrier typically captures during these holiday periods.

Figure 7: Airline passenger market shares across all domestic routes – January 2019 to January 2023



Source: Data collected by the ACCC from Qantas, Jetstar, Virgin Australia and Rex.

In contrast to Jetstar, Qantas' market share decreased by around 3 percentage points since October 2022 to 34.8% in January 2023. This was its lowest market share since January 2022 and reflects a seasonal decrease due to relatively less business travel demand over the holiday period. Despite the decrease, the combined market share of the Qantas Group was 61.7% in January 2023, which was slightly higher than in October.

Virgin Australia's market share of 33.4% in January 2023 was around the same as in October. Virgin Australia continued to fly the highest number of passengers on routes connecting larger cities, which has been the case each month since August 2022. Its 38.1% share of passengers on larger city routes in January 2023 was over 4 percentage points above Qantas' share.

Virgin Australia's CEO Jayne Hrdlicka said in December 2022 that the airline will increase flying at a quicker rate than rivals in the early parts of 2023 to capitalise on demand and help ease the supply side crunch impacting airfares.[36] This was evident in December 2022 and January 2023, as Virgin made more seats available than Qantas on routes connecting the larger cities.

Rex's market share reached a new record high of 5.8% in November 2022 before decreasing to 4.9% in January 2023. The airline reported it began generating profits from September 2022 onwards on the larger city routes it expanded into following the pandemic. It reported a record high market share on the larger city routes in November 2022 (5.7%), which decreased only slightly to be 5.4% in January 2023.

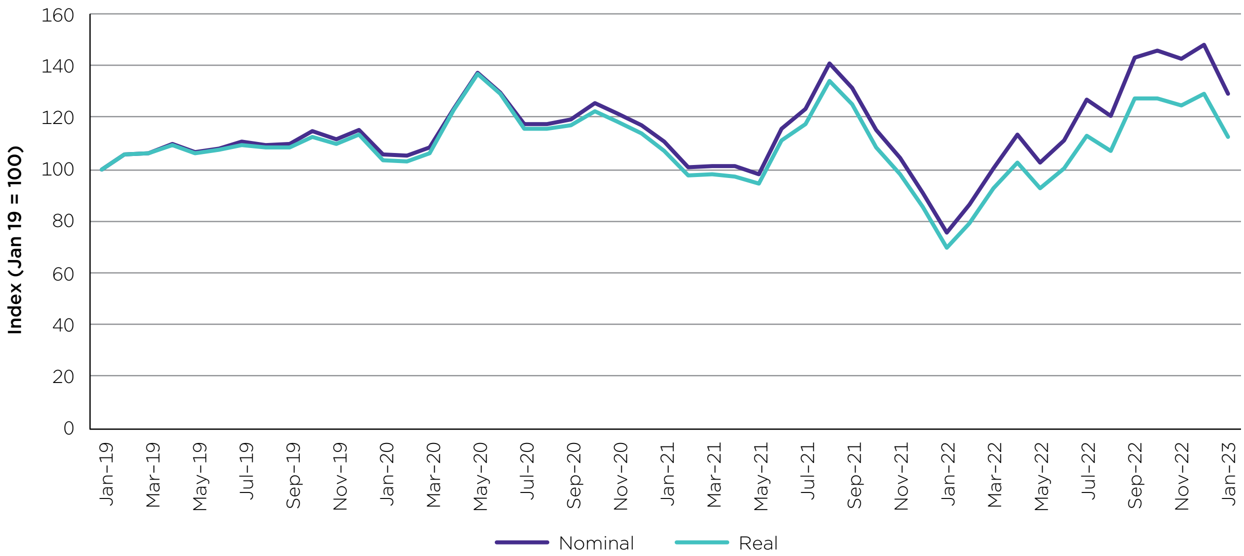
36 Baird, L & Wiggins, J, Australian Financial Review, ''Fair enough': Alan Joyce reflects on criticism as airlines mull 2023', 28 December 2022, accessed 16 February 2023.

3.6 Airfares fall from historical highs

Airfares have fallen in recent months after reaching historically high levels in late 2022. This fall can be explained by typical seasonal trends as well as the airlines increasing capacity.

Average revenue per passenger is a useful proxy measure for average airfares paid by passengers. In 2022 average revenue sustained significant increases due to soaring demand, constrained capacity, and high jet fuel prices (figure 8). After peaking in December 2022, average revenue decreased by 13% in January 2023. This figure was still 13% higher (29% higher in nominal terms) than January 2019.

Figure 8: Index of average fare revenue per passenger across all routes – January 2019 to January 2023

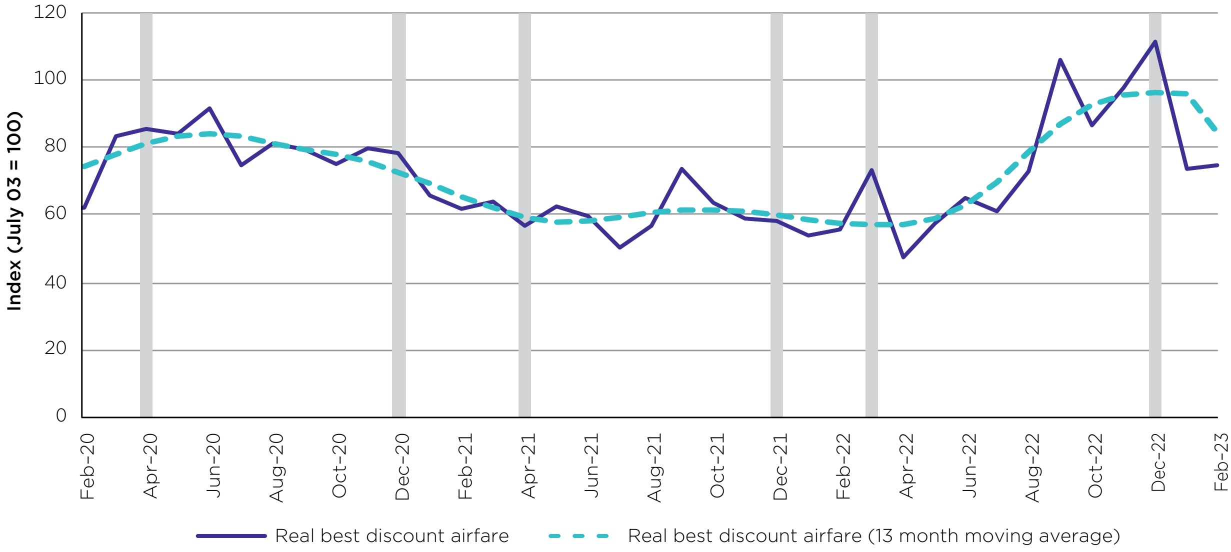


Source: ACCC calculations using data from the ABS and data collected by the ACCC from Qantas, Jetstar, Virgin Australia and Rex.

Note: The average revenue per passenger includes both economy and business fare revenue. It excludes ancillaries and Tigerair data. Data has been adjusted for inflation using the latest ABS CPI quarterly data up to December 2022.

The post-Christmas fall in airfares was also evident in data from BITRE. BITRE's price index for the cheapest discounted airfares has fluctuated greatly since the start of 2022. Figure 9 shows that after a historical high in December 2022, the index was roughly a third lower in both January and February 2023.

Figure 9: Price index of discount economy airfares weighted across 70 busiest domestic routes – February 2020 to February 2023



Source: BITRE Domestic Air Fares (Best Discount) index (cheapest available economy airfares).

Note: Grey bars indicate December and Easter holiday periods. Airfares recorded April 2021–February 2022 may be impacted by the government's half-price ticket program (TANS).

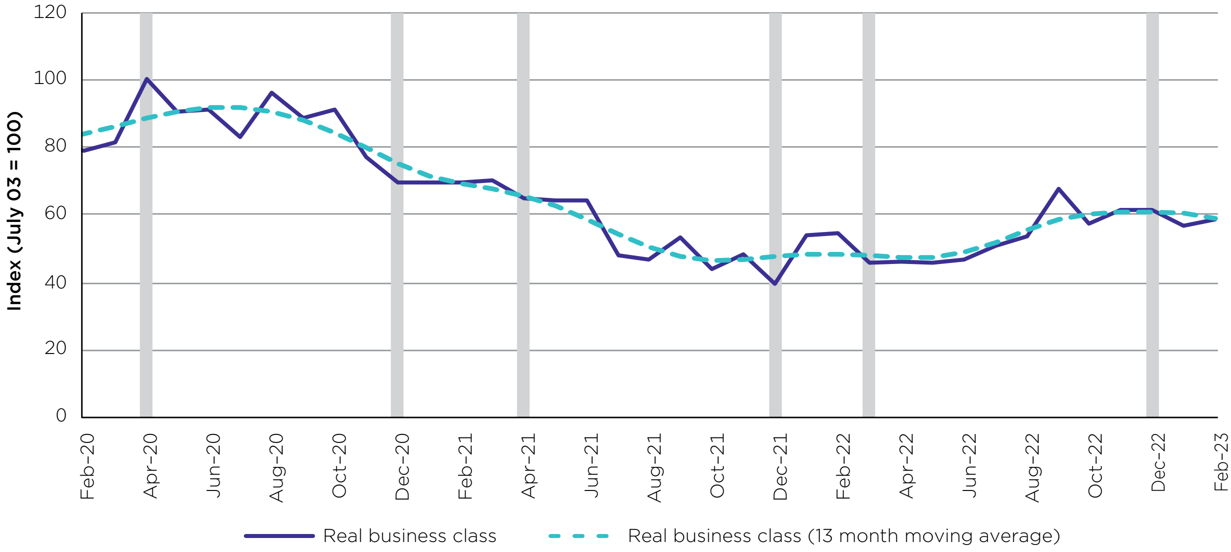
Despite this recent fall, the index for discounted tickets was 25% higher in February 2023 than the same month pre-pandemic (February 2019). Some routes continue to be significantly higher compared to pre-pandemic. Over this period the cheapest return fares for Coffs Harbour – Sydney almost tripled to $338. Many flights to and from Adelaide were double or almost double, such as Adelaide – Melbourne (up 102% to $298) and Adelaide – Brisbane (up 100% to $455). Other significant increases were on Cairns – Melbourne (up 90% to $481) and Newcastle – Gold Coast (up 82% to $230).

Other fare types such as restricted economy (flexible, but fees or restrictions apply) and business also fell in recent months, but by more marginal levels. Between December 2022 and February 2023, the BITRE price index for restricted economy decreased by 9% and the price index for business airfares fell by 5%. In contrast to discounted tickets, the price indices for both of these ticket types remained more than 20% below pre-pandemic levels in February 2023.

Figure 10 shows BITRE's price index for business airfares. The relatively slower recovery in business travel demand may explain why business airfares remain low. Another factor may be that following Virgin Australia's restructure in late 2020, the airline changed its strategy to target 'value-conscious' travellers rather than premium customers. Analysing airfares purchased by corporate customers between March and June 2022, travel consultancy Butler Caroye found that Virgin Australia's business airfares on capital city routes were 56% lower than Qantas.[37]

37 Findings based on airfares purchased March–June 2022 by a sample of corporate customers travelling capital city routes; Butler Caroye, Blue Paper, 'Update: Australian domestic business airfares in 1st half 2022: The market settles across a fare divide'; August 2022, accessed 21 February 2023.

Figure 10: Price index of business airfares weighted across 70 busiest domestic routes – February 2020 to February 2023



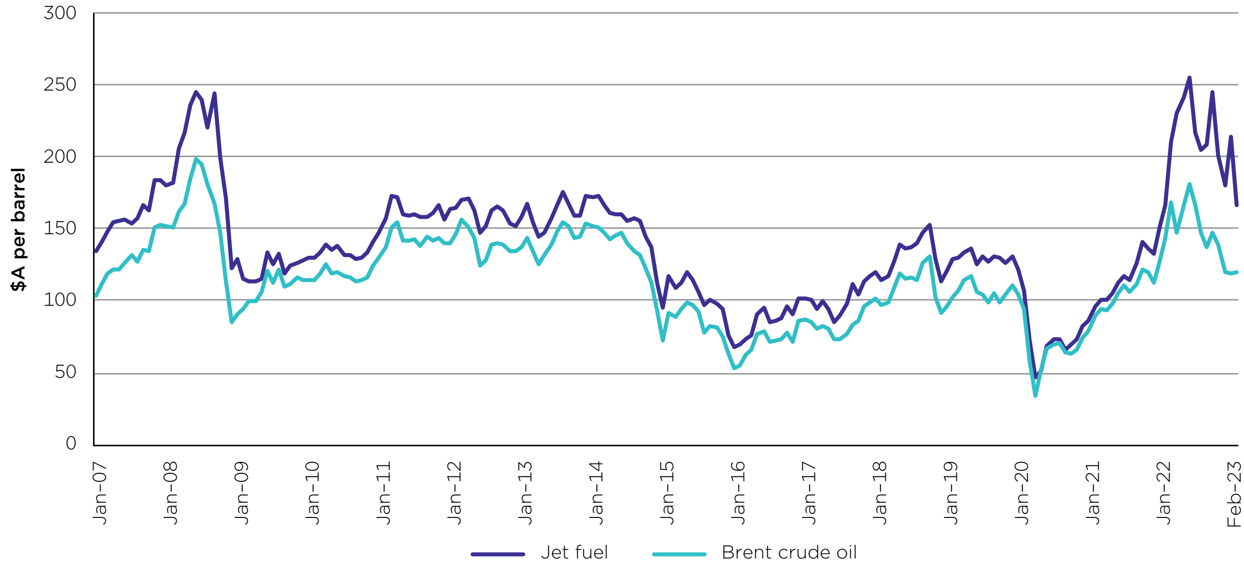
Source: BITRE Business Air Fares index.

Note: Grey bars indicate December and Easter holiday periods. Airfares recorded April 2021–February 2022 may be impacted by the government's half-price ticket program (TANS).

The recent fall in airfares more generally reflects seasonal factors. There is typically a fall in airfares at this time of year as demand for leisure travel subsides from its peak at Christmas, while business travel is also relatively subdued this early in the year. Another factor is that airlines have continued to increase seat capacity since late 2022 as they become more confident in their ability to fly higher frequencies without cancellations and delays.

The high price of jet fuel has been another contributor to higher airfares over the past year due to the war in Ukraine. However, the price is now trending down. The price of jet fuel has fallen by 35% in real terms to $166 per barrel in February 2023 since reaching a record high of $255 per barrel in June 2022 (see figure 11). The refining margin between jet fuel and Brent crude oil prices has fallen from $63 per barrel in November to $47 in February. The falling price of jet fuel should enable airlines to further reduce airfares in coming months.

Figure 11: Real jet fuel and Brent crude oil prices – January 2007 to February 2023



Source: ACCC calculations using ABS, RBA and US EIA data.

Note: US Gulf Coast Jet Fuel prices converted into current Australian dollar terms. The price an airline pays for jet fuel will also vary depending on the ports to which its aircraft operate and the respective region-specific jet fuel benchmarks. The latest month of data is to 21 February 2023.

4. The impact of low-cost carriers on consumer choice and competition

The emergence of low-cost carriers (LCCs) over the last 3 decades has helped to transform the global airline industry and make air travel more accessible. With cheaper airfares and direct flights, LCCs have encouraged more people to fly, while also forcing traditional carriers to innovate and better align their product offerings with consumer preferences.

With the launch of new Australian LCC Bonza, this chapter looks at the nature of LCCs, their growing global importance over time, their history in Australia, and the benefits they can offer for consumers through product offerings and competition.

4.1 Low-cost carriers target leisure travellers through low airfares

Airlines traditionally offered a full range of services to customers. These full-service carriers would provide several cabin classes, complimentary food and drinks, and connectivity to a wide range of destinations branching out from a central hub airport (under what is known as a 'hub-and-spoke' model). While this traditional model can provide high quality services, it is also more costly to operate and so can result in higher airfares.

In contrast, the LCC business model is focused on offering low airfares and a simplified product to generate demand. To do this, LCCs operate in a different manner to full-service carriers in order to reduce costs. While each LCC can vary in this regard, it may see them only offering food and drink available at extra charge, flying a collection of 'point-to-point' routes instead of an interconnected network, and only operating flights over a relatively short distance (see table 2).

Table 2: Common features of low-cost carriers

Unbundled products	Meals and drinks, checked luggage and choosing a seat are optional extras with a charge
Single cabin class	Relatively full aircraft with a single economy cabin class
Point-to-point routes	Network design may be based around profitable, leisure routes rather than a broad interconnected network.
No interline connectivity	May not have interline or code-share agreements with other airlines to enable passengers to change flights without collecting bags or checking in again
Short-haul flights	Flights are typically 3 hours or less, for which airfares are likely to be lower and have the potential to tempt people to fly
Single aircraft type	Fleet consists of one aircraft type to achieve economies of scale in maintenance and training, and flexibility in allocating aircraft and crew between routes
Secondary airports	Fly in and out of secondary airports that may offer lower charges and faster aircraft turnaround times, as well as less competition with full-service carriers
Tickets sold online	Seats are typically sold directly online to avoid additional costs and commissions
Passengers not cargo	Do not generally carry much cargo in the belly of the aircraft

Over time, many LCCs have adopted practices typically associated with full-service carriers and vice versa, depending on the relevant market environment. For example, Australian LCC Jetstar offers some long-haul international routes with multiple cabin classes and some interline connectivity. Other airlines described as ultra-low-cost carriers have also emerged which place even greater focus on offering the lowest price.

With a business model focused on reducing operational costs and competing on the basis of price, LCCs may deliver poorer customer experiences than full-service airlines. For example, a low-cost airline may not have a large call centre for handling customer queries or problems. Australian LCCs Tigerair and Jetstar have also generally performed worse in terms of on-time performance and cancellations than other airlines.[38]

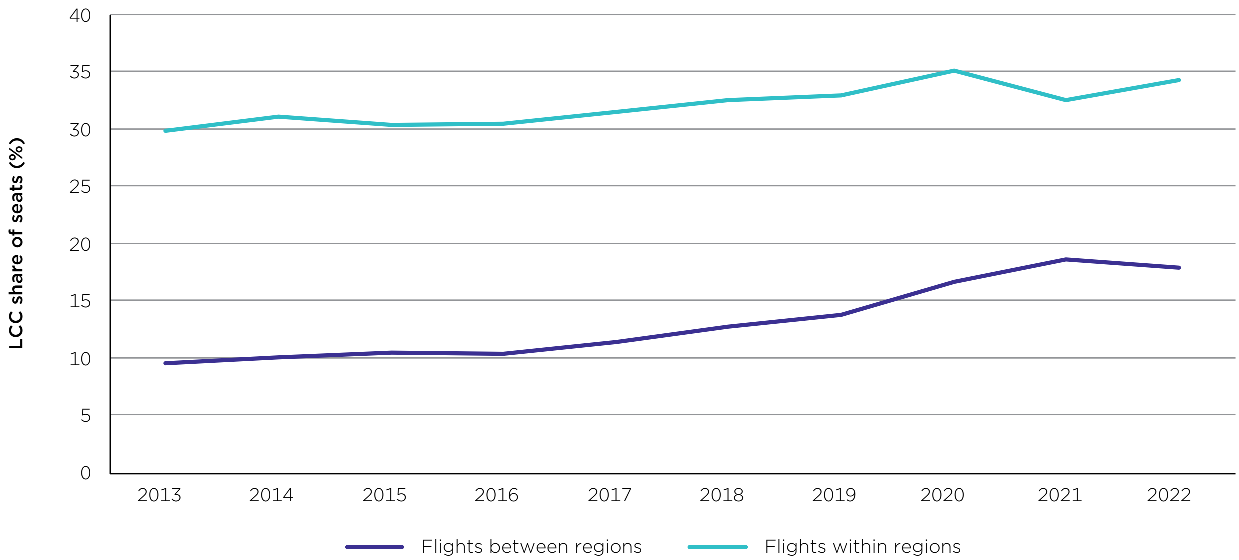
However, LCCs can outperform full-service carriers in terms of customer satisfaction. This is because LCC customers have more choice over what aspects of the service they wish to pay for, plus they often have different expectations of the service than if they were flying with a full-service carrier.[39] Furthermore, the simplified LCC product offering means there are fewer elements over which a problem may arise (e.g. quality of airport lounge or the complimentary meal).

4.2 The LCC business model has been very successful worldwide

The LCC business model has been very successful since it was first pioneered by Southwest Airlines in the United States in 1971. Its success led to the emergence of other LCCs around the world, with growth in more recent decades supported by more fuel-efficient aircraft, the deregulation of airline markets, and increasing levels of disposable income. LCCs further benefited from the development of websites enabling passengers to easily compare airfares.

Figure 12 shows that LCCs had been flying a growing percentage of seats worldwide in the years leading up to the pandemic. In 2020 LCCs accounted for 35.1% of seats on flights within the same region of the world and 16.6% of seats on flights between regions. LCCs have been particularly successful in Western Europe with LCCs providing 45.7% of the seats flown within that region in 2020.[40] The proportion of *passengers* flown by LCCs would be even higher than the proportion of seats given that a key part of the LCC strategy is to fill their flights.

Figure 12: Share of seats worldwide flown by LCCs – 2013 to 2022



Source: ACCC calculations using data from CAPA – Centre for Aviation and OAG.

38 BITRE, Australian Government. 'Airline on time performance annual reports', various years, accessed 8 February 2022.

39 Baker, D. A., 'Service quality and customer satisfaction in the airline industry: A comparison between legacy airlines and low-cost airlines', *American Journal of Tourism Research*, Vol. 2, No. 1, 2013, accessed 8 February 2022.

40 CAPA – Centre for Aviation and OAG.

Some of the biggest airlines globally employ a low-cost business model. In February 2023, LCC airlines accounted for 10 of the 30 biggest airlines by capacity including Southwest Airlines (2nd) in the United States, Ryanair (5th) in Europe and IndiGo (8th) in India.[41]

Generally, it appears that LCCs were more financially successful than full-service carriers in the decade leading up to the pandemic. A joint study by the International Air Transport Association (IATA) and McKinsey & Company found that the weighted average returns on invested capital (ROIC) for LCCs were between 6% and 10% in the years between 2012 and 2019.[42] The weighted average returns for LCCs were higher than network (full-service) carriers in each year.

While the pandemic has had a significant impact on airlines around the world, the experiences of LCCs and full-service carriers have not been the same. The IATA/McKinsey & Company study found that the returns for LCCs globally fell more sharply in 2020 because unlike many full-service carriers, they did not get the benefit of the higher returns generated by air cargo at the time.[43]

As airline markets recover from the impact of the pandemic, LCCs have benefitted from the strong demand for leisure travel.[44] The LCC business model also provides greater flexibility for moving to new routes in response to changing demand patterns or travel restrictions. Low-cost airlines Ryanair and Wizz Air took advantage of the high demand for intra-European leisure traffic to expand operations throughout 2022 to beyond their 2019 levels, with Ryanair operating more flights in Europe than any other airline.[45] However, the high price of jet fuel since early 2022 has likely been more detrimental to low-cost airlines than full-service airlines, with fuel accounting for a higher proportion of total cost for LCCs.

4.3 The history of LCCs in Australia

In January Bonza became the most recent low-cost airline to enter the Australian domestic market in a history of LCCs spanning over 3 decades.

The first phase of LCC entry occurred shortly after deregulation of the Australian airline industry. Compass Airlines began offering low-cost services in 1990 in a market dominated by Qantas and Ansett Australia. Linking up 7 major airports, at one point Compass had captured 10% of the total domestic market and up to 21% on the routes that the airline served.[46] However, Compass experienced problems in gaining access to airport slots and delays with the delivery of aircraft, while facing a strong competitive response from the incumbent airlines.[47] It ran out of funds and collapsed within a year.

In 1992, not long after Compass collapsed, a second low-cost airline called Compass Mark II entered the Australian domestic market. This airline operated for about 6 months when it too failed for similar reasons. No other airline entered the Australian domestic market for the rest of the decade (see figure 13).

41 CAPA – Centre for Aviation and OAG.

42 IATA, McKinsey & Company, 'Understanding the pandemic's impact on the aviation value chain', December 2022.

43 ibid.

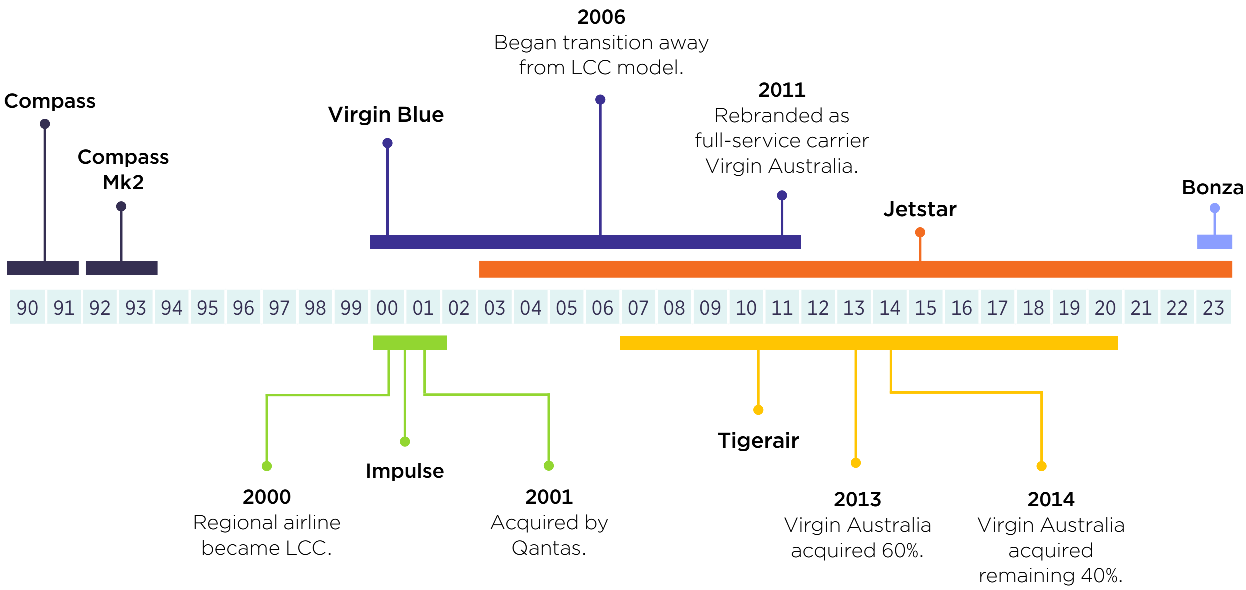
44 OliverWyman, 'Airline economic analysis: 2021–2022', June 2022, accessed 8 February 2022.

45 CAPA – Centre for Aviation, 'EUROCONTROL Data Snapshot #34 on the rise of low cost carriers in Europe', 25 October 2022.

46 Srisaeng, P, Baxter, G, Wild, G, 'The evolution of low cost carriers in Australia', *Aviation* 18(4), December 2014, accessed 20 December 2022.

47 ibid.

Figure 13: Timeline of LCCs in the Australian domestic market – 1990 to 2023



The next phase of market entry commenced in 2000 when both Impulse Airlines and Virgin Blue began offering low-cost services on some major intercity routes. Impulse had previously been a successful regional operator based in New South Wales but began intercity services after acquiring jet aircraft. By early 2001 it was experiencing some liquidity problems and was acquired by Qantas in late 2001. The ACCC had competition concerns but did not oppose the acquisition on the basis that it was preferable to Impulse going into receivership.[48] Qantas also committed to free up some take-off and landing slots at Sydney Airport in an undertaking to the ACCC.

Virgin Blue was established shortly after Impulse in 2000 and proved to be significantly more successful. While the global Virgin brand may have helped in this regard, the far more notable factor was that Virgin Blue was still operating when Ansett Australia collapsed in September 2001. Not only did this leave Australia with a significant shortfall in domestic seat capacity, but it enabled Virgin Blue to obtain valuable take-off and landing slots at major airports and Ansett's old terminal space.[49]

Over time, Virgin Blue increasingly moved away from a low-cost business model such as by opening airport lounges (in 2003) and launching a frequent flyer program (in 2005). This transition, designed to appeal to a broader part of the market and compete more directly with Qantas, was completed in 2011 when the airline rebranded as Virgin Australia.

Qantas established its own LCC Jetstar in 2003. The motivation for Qantas was that a new airline with a lower cost structure would be able to compete more effectively with Virgin Blue for the growing leisure travel market.[50]

While many attempts around the world by traditional airlines to establish low-cost subsidiaries have not worked, Jetstar has been very successful for the Qantas Group. Jetstar initially focused on connecting Australia's capital cities with leisure destinations. As the airline grew, it shifted its focus to linking Australia's major population centres.[51] It is now approaching 2 decades of operations, spans 58 routes and flies approximately one in every four of Australia's domestic passengers. Jetstar was regularly

48 ACCC, *ACCC not to oppose Qantas/Impulse merger* [media release], 18 May 2001, accessed 17 January 2023.

49 Srisaeng, P, Baxter, G, Wild, G, 'The evolution of low cost carriers in Australia', *Aviation* 18(4), December 2014, accessed 20 December 2022.

50 White, R, Lohmann, G, The carrier-within-a-carrier strategy: An analysis of Jetstar, Journal of Air Transport Management, 2015, accessed 20 December 2022.

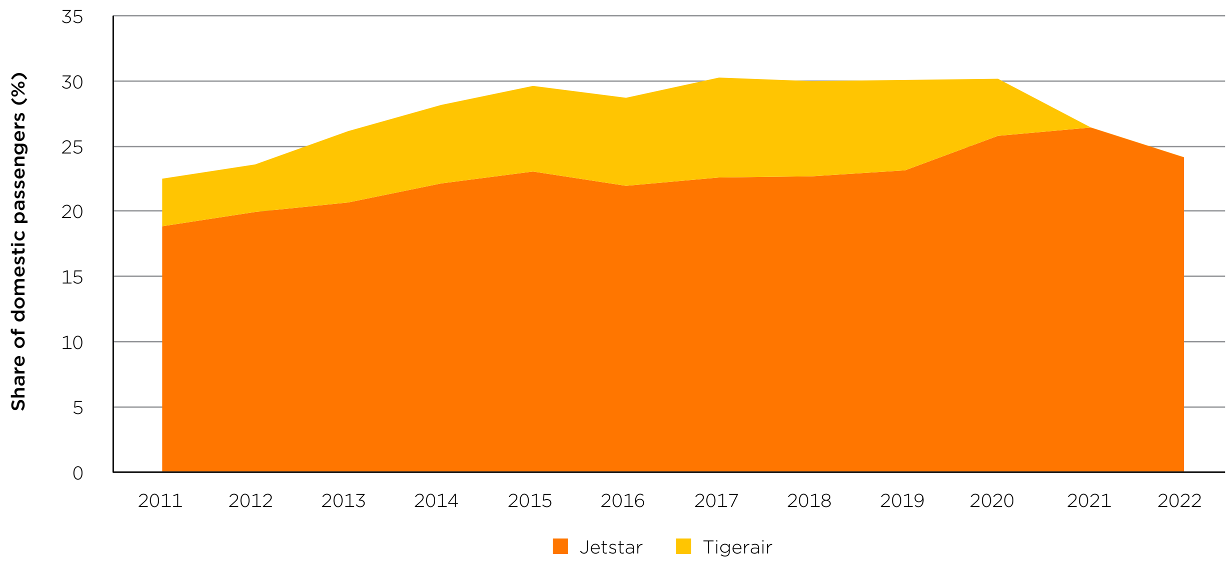
51 Thomas, G, 'Jetting to the top', *Air Transport World* 43(10), 2007, as cited in White, R, Lohmann, G, The carrier-within-a-carrier strategy: An analysis of Jetstar, Journal of Air Transport Management, 2015, accessed 20 December 2022.

profitable prior to the pandemic in 2020[52] and its domestic operations recently reported underlying earnings before interest and tax (EBIT) of $130 million in the first half of 2022–23.[53]

The next LCC to enter the Australian domestic market – and the last for 15 years prior to Bonza – was Tiger Airways in 2007. The Singapore-based airline was entirely foreign owned, permissible under Australia's liberal domestic airline ownership laws.[54] Tiger Airways sought to offer the lowest airfares in the market but developed a poor reputation following its temporary grounding in 2011 by the Civil Aviation Safety Authority (CASA) due to safety concerns. It was later acquired by Virgin Australia – 60% in 2013 and then the remaining 40% in 2015 – to provide Virgin with a dual brand strategy to rival the Qantas Group, with the newly renamed Tigerair to compete with Jetstar in the leisure market. However, the business ceased operations in April 2020 during Virgin Australia's voluntary administration process.

At their peak in 2010, LCCs nominally flew 64% of Australian domestic passengers with competition between Virgin Blue, Jetstar and Tigerair.[55] However, this figure inflates the importance of LCCs because Virgin Blue was operating more like a full-service carrier by that time (with the transition formalised in 2011). The combined LCC domestic market share has been between 22.5% and 30.3% in the time since (see figure 14), which is slightly below the LCC share of global seats on flights within regions of the world (as shown earlier in figure 12). Jetstar has dominated this segment of the Australian domestic industry over this period and has not had a direct LCC rival since early 2020.

Figure 14: Share of Australian domestic passengers flown by LCCs – 2011 to 2022



Source: ACCC calculations using data from CAPA – Centre for Aviation and OAG, and data collected by the ACCC from Qantas, Jetstar, Virgin Australia and Rex.

Low-cost airlines have also featured on international routes to and from Australia since the mid-2000s. Virgin Blue established a subsidiary Pacific Blue in 2003 to provide services between New Zealand and Australia as well as the Pacific Islands. Jetstar then became somewhat of a pioneer in long-haul low-cost services with Jetstar launching wide-body services to Thailand in 2006, followed by services to Vietnam and Bali. Australia now has a number of LCCs providing international services to the Asia Pacific such as Jetstar, AirAsia X, Scoot, Cebu Pacific and Vietjet. Low-cost airlines accounted for 17.9% of international passengers to/from Australia in October 2022, up from 15.0% in October 2019.[56]

52 ACCC, *Airline competition in Australia – December 2022 report*, 7 December 2021

53 Qantas, *Qantas Group returns to profit with record half year result* [media release], 23 February 2023, accessed 23 February 2023.

54 Srisaeng, P, Baxter, G, Wild, G, 'The evolution of low cost carriers in Australia', Aviation 18(4), December 2014, accessed 20 December 2022.

55 ibid.

56 BITRE, Australian Government, 'International airline activity: October 2022', January 2023.

4.4 LCCs increase airline competition which benefits consumers

A key reason for the LCC business model transforming the global airline industry over the last 3 decades is because of how it supports competition. Most of the new market entries over this time have been by airlines adopting the low-cost model, with many developing into some of the largest airlines in the world.

The emergence of LCCs has increased competition around the world

While barriers to entry into the airline industry remain, they appear to be lower for an LCC compared to a full-service carrier. Unlike a full-service carrier, a new LCC does not immediately need to offer features such as a broad interconnected series of routes, a network of airport lounges, a frequent flyer program or interline agreements with other airlines. An LCC can begin by offering a small number of point-to-point routes and then incrementally expand to other routes should it prove to be successful.

The LCC business model also supports competition by increasing the number of airlines that can sustainably operate in a particular market. Markets with more operators will generally be more competitive. Firstly, with LCCs operating on a lower cost structure, it is likely that a market of a certain size will be able to sustain more airlines if some are low-cost operators than if all airlines in the market were full-service operators. This is because LCCs generally need less capital to enter and less revenue in order to cover their costs and remain profitable. Secondly, LCCs have tended to grow the overall size of markets as their lower airfares have encouraged more people to fly.

The emergence of LCCs throughout the world has clearly impacted traditional full-service carriers. Once they were provided with a low-cost choice, many of the full-service carriers' traditional customers have instead chosen to fly with LCCs. Losing these customers has made it more challenging for full-service carriers to cover the high costs of their operations. Many full-service carriers have been forced to reduce their airfares to retain some of these price-conscious customers. Even on routes where LCCs do not operate, a full-service carrier may be partially constrained in its pricing behaviour if there is a real threat of an LCC choosing to enter that route in future, given the network flexibility of LCC's point-to-point operations.

This competition has resulted in significant benefits for consumers. Globally, traditional airlines have introduced lower airfares, the unbundling of services included in a ticket price, and loosened conditions on tickets (e.g. the need to buy a return flight). Some full-service carriers were not able to survive this new competition and were forced to exit the market.

LCCs have played a role in key competitive developments in the Australian domestic market

The competitive impact of low-cost airlines has extended to the Australian domestic market. Perhaps the most notable development was the collapse of Ansett Australia in 2001. While the airline had its management and ownership challenges[57], it was also under pressure from new competition from LCCs Impulse Airlines and Virgin Blue. Perhaps underscoring the potential productivity benefits of new competition, as well as the difference in business models, former Virgin Blue chief executive Brett Godfrey said in 2004 that the airline would carry more passengers in that financial year than what Ansett did in its last full year of operations on the major trunk routes, despite having only one-third of the staff.[58]

LCCs have also contributed to other key competitive developments in Australia. It was the rapid rise and market acceptance of Virgin Blue that led to rival Qantas establishing its own LCC Jetstar in 2003. Jetstar was then driven to respond to new competition when Tiger Airways commenced operations

57 Thomas, G, Australian Aviation, 'From the Archives: The Ansett collapse', 14 September 2019, accessed 20 January 2023.

58 ibid.

in 2007 from Melbourne Airport.[59] In response, Jetstar moved services across from Melbourne's secondary airport Avalon to the larger airport at Tullamarine. The Qantas Group also ended its policy of having Qantas and Jetstar operate on different routes, with Jetstar being deployed alongside Qantas on some intercity routes to better compete with Tiger Airways.

The CEO of Bonza, Tim Jordan, considers that Australian domestic travellers have missed out because of a lack of independent LCCs. Since Virgin Australia acquired a majority ownership of Tiger Airways in 2013[60], the Australian domestic market has only had LCCs which have been subsidiaries of larger airline groups. These 2 groups – Qantas Group and the Virgin Australia group – have accounted for the overwhelming majority of domestic passengers over this time.

In May 2022, Jordan said that despite being the eighth largest domestic aviation market in the world, Australia had been the only one without an independent low-cost operator.[61] He further said that while other markets saw significant growth in low-cost routes over the decade leading up to the pandemic, the number of routes operated by Jetstar and Tiger/Tigerair was the same in 2019 as it was in 2010 (58 routes).[62] This is despite continued growth in the Australian population over the same period.

Bonza is offering its low-cost services over 25 new routes in additional to 2 routes already served by existing airlines. Jordan considers that the Bonza business model and very low-cost product enables it to feasibly consider certain routes that may not work for the incumbent airlines.[63] In contrast, the other airlines have publicly questioned whether Bonza can succeed on the previously unserved routes.[64]

Jetstar shares a growing number of routes with Qantas, while Rex has filled some of the gap left by Tigerair

The ACCC analysed the domestic routes offered by LCCs Jetstar and Tigerair in January 2020, prior to the pandemic. Jetstar's network comprised a mix of routes connecting larger cities with both other larger cities and smaller regional centres. Only half of the 53 routes were shared with Qantas. In contrast, Tigerair's 21-route network predominantly provided connections between larger cities and generally comprised routes also offered by its parent airline Virgin Australia (86% of Tigerair's routes). Tigerair faced competition from Jetstar on 16 of the 21 routes.

The competitive dynamics of the industry had changed by January 2023, most notably from the departure of Tigerair. The gap left by Tigerair was primarily filled by Rex, which expanded into 8 of the old Tigerair routes. Jetstar also expanded into 3 of the 5 Tigerair routes it did not already offer in January 2020, while Qantas entered one. Virgin Australia did not pick up any of the 3 Tigerair routes it did not already service. No routes previously operated by Tigerair were left unserved. In January 2023 Jetstar shared 72% of its routes with parent airline Qantas, primarily reflecting Qantas' expansion in recent years.

59 Srisaeng, P, Baxter, G, Wild, G, 'The evolution of low cost carriers in Australia', *Aviation* 18(4), December 2014, accessed 20 December 2022.

60 At the time of the acquisition, former ACCC Chair Rod Sims said: 'The ACCC would always prefer to see a greater number of independent airlines competing in the domestic market. However, our investigations showed that Tiger Australia had been unable to establish itself as a viable competitor despite substantial investment and numerous changes of management and strategy over the years. We concluded that it was highly likely that Tiger Australia would leave the market if this acquisition didn't go ahead, and accordingly blocking the acquisition would not serve to protect competition.' See ACCC, *ACCC to not oppose Virgin Australia's proposed acquisition of 60% of Tiger Australia* [media release], 23 April 2013, accessed 20 January 2023.

61 Bishop, A, TravelBulletin, 'Will they get bums on seats?', May 2022, accessed 23 January 2023.

62 Bailey, J, Simple Flying, 'Bonza's launch will grow Australian low-cost routes by 40%', 7 March 2022, accessed 23 January 2023.

63 Dowling, H, Australian Aviation, 'Exclusive: Bonza says rivals won't be able to compete on its routes', 7 December 2021, accessed 23 January 2023.

64 ibid.

4.5 Policy settings that support competition by minimising barriers to independent LCC entry and expansion

Much of the new competition seen in airline markets around the world in recent decades has come from low-cost airlines. Optimal policy settings encourage the entry and expansion of LCCs which in turn lead to a competitive market that benefits consumers through lower prices, better schedules and increased choice.

Access to take-off and landing slots – An important policy consideration for LCCs is whether take-off and landing slots at congested airports are allocated between airlines in a pro-competitive manner. Consistent with the Worldwide Airport Slot Guidelines, the slot allocation schemes at many airports enable existing airlines to retain their slots from season to season in order to provide some investment certainty. However, this can make it difficult for new and expanding airlines to access desirable slots. As mentioned in section 2.6, the ACCC is engaging with the Australian Government in its long-running review of demand management at Sydney Airport. This review is considering the process for allocating slots between airlines, the rules around slot use and the re-allocation of unused slots.

Investment in additional airport capacity – Low-cost airlines benefit when airports operate under a regulatory regime that sufficiently incentivises airports to invest in infrastructure that provides efficient additional capacity for new entrants. An adequate level of facilities can also help minimise congestion and therefore support quick turnarounds between an aircraft landing and then taking off on the next flight, which is very important for low-cost airlines.

Reasonable airport charges – Importantly, the airport regulatory regime also needs to prevent airports from charging excessively, with LCCs unlikely to be able to operate out of high-cost airports. Excessive charging arises where an airport uses its market power to seek more of a return on its investment than justified by the risk of the project. Excessive charges can also relate to an airport investing in a higher standard of facilities than required by airlines or passengers, a practice often referred to as 'gold plating'.

The ACCC has expressed concerns that the current regulatory regime for airports, based on ACCC monitoring of Brisbane, Melbourne, Perth and Sydney airports, does not adequately constrain airports from using their market power in setting airport charges.[65]

Removing harmful clauses in airline/airport agreements – LCCs can also be particularly disadvantaged where airports are prevented from offering discounted rates due to restrictive clauses in their contracts with rival airlines. Following a recommendation by the Productivity Commission in its review of airport regulation in 2019, the Australian Government said that it had amended the Aeronautical Pricing Principles (APPs) to specify the exclusion of these 'most favoured customer' clauses in airport/airline contracts.[66] However, the ACCC understands that the amended APPs have not been formally re-issued.

Flexible ownership rules – In contrast to many countries, Australia allows domestic airlines to be 100% foreign owned, if the airline is registered in Australia and subject to the same laws and regulations governing the operation of domestic flights in Australia.[67] These ownership rules have enabled the launch of LCCs Virgin Blue, Tiger Airways and now Bonza.

Safety regulation – As a new airline, Bonza had to meet certain safety requirements before obtaining its Air Operator's Certificate from CASA before commencing operations. While Bonza had initially hoped to commence services from September 2021, the duration of the process will depend on the time taken to provide and review information in support of safety standards requirements.

65 For example, see ACCC, 'Productivity Commission inquiry into the economic regulation of airports: ACCC submission in response to the draft inquiry report', March 2019.

66 Australian Government, 'Australian Government response to the Productivity Commission inquiry into the economic regulation of airports', 11 December 2019, accessed 24 January 2023.

67 Acquisition of an Australian domestic airline is subject to the *Foreign Acquisitions and Takeovers Act 1975*.

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