



Airline competition in Australia

Report 2: December 2020



Australian Competition and Consumer Commission
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Overview

This is the second of a series of reports to be produced under the direction from the Australian government to monitor competition in the supply of domestic air passenger transport services.

Data provided to the ACCC by Qantas, Virgin and Regional Express (Rex) for September 2020 reveals an industry operating at a fraction of its pre-COVID capacity. For example, total passenger numbers for the month of September 2020 were 87% below September 2019 and industry revenues were accordingly lower. The data also shows Qantas and Rex generally gaining market share at the expense of Virgin during the period, although market shares may be volatile given the depressed state of the industry.

We have also seen airlines take an opportunistic and agile approach to network management, seeking to tap into demand for particular routes and services to bring in much-needed cash in this environment, even if expected revenues are insufficient to cover fixed costs and therefore make a profit. At this stage, it is difficult to identify exactly how competition will evolve as the industry emerges from this period.

With signs that all states including Victoria have COVID-19 under some control, and key state borders opening up in November and early December, there is growing optimism that the industry can now begin its recovery. Airlines are increasing capacity to meet pent-up demand for travel as people come out of lockdowns and other travel restrictions wanting to see family and friends or just get away for a holiday. As this happens, the extent to which the industry relies on government support is diminishing. Some among the industry have suggested that with the holiday season, and continued growth into 2021, activity may approach pre-COVID levels on some leisure routes.

However, optimism is still cautious and the path to recovery is fragile. This was highlighted by the level of disruption caused by COVID-19 cases in South Australia in mid-November. Airlines observed a 'freeze' in sales and were forced to cancel flights as movement restrictions were reinstated.

There have been a number of significant developments in the industry since our first report in September 2020. Bain Capital officially became the owner of Virgin in November 2020 as the airline emerged from voluntary administration. Upon her commencement, new CEO Jayne Hrdlicka announced plans to position Virgin as a mid-market carrier. We note that various aspects of Virgin's product and service offering are under review and will become clearer as the airline implements its strategies. Bain Capital's direction for Virgin is likely to have significant implications for competition in the domestic airline industry.

During the course of the administration process, Virgin simplified its fleet and reduced its network coverage. The ACCC has also granted interim authorisation for Virgin to cooperate with Alliance Airlines on 41 domestic routes, which we expect will enhance its ability to compete with Qantas.

Regional operator Rex has further progressed its plans to expand into major domestic routes. On 1 December 2020 it began selling tickets for Sydney-Melbourne flights which are due to commence from 1 March 2021. It has also stated that it will further expand across the broader Sydney-Melbourne-Brisbane triangle.

One of the key inputs Rex will need to compete on these routes is access to airport slots. It has secured slots for its launch in March 2021, and is continuing to work on gaining access to slots for April 2021 onwards. The Australian government has initiated a comprehensive review of demand management at Sydney Airport. The ACCC's submission highlights ways in which slot management can impede competition through inefficient slot use and incentives to hoard slots, including by hindering opportunities for new and expanding airlines.

Key themes emerging in the airline industry

The ACCC continues to engage with key Australian airlines on the state of the industry and their recovery plans. Some of the key messages we have heard recently are set out below.



Domestic borders have re-opened

Major Australian border openings in November and December led to an influx of demand for interstate travel which resulted in Qantas and Virgin significantly increasing capacity. At the same time, the sudden South Australian border closure in November showed how fragile the situation remains.



International borders remain closed

International borders will remain closed for the foreseeable future. This is causing Australian airlines to turn to unique domestic flying opportunities to generate cash where possible.



Consumer demand for leisure flying is strong

Despite concerns that consumers would be reticent to fly, consumer demand is stronger than expected. Consumers appear to be comfortable with getting back in the air and experimenting with new domestic travel destinations, especially given the suspension of international travel.

The resources market in Queensland and Western Australia is similarly strong while government travel is subdued and corporate travel remains a fraction of what it was.



The airlines are optimistic about the future

Stronger than expected returning demand has given the airlines a positive outlook about the future of domestic travel. Qantas has added more flights and new routes to its domestic network. New Virgin CEO, Jayne Hrdlicka, has stated that Virgin is 'very focused on being successful' and 'will be fiercely competitive' to Qantas.

Rex's domestic network expansion plans are on-track with sales of Sydney-Melbourne flights for March 2021.



Access to take-off and landing slots

Access to airport slots continues to be a key issue for all airlines. A review of demand management at Sydney Airport is underway, which will include consideration of the Sydney Airport slot management scheme (the ACCC's submission to this review is outlined in section 4.1 of this report).

1. Introduction

This is the ACCC's second report on its findings from monitoring domestic air passenger transport services.

On 19 June 2020, the Treasurer issued a direction to the ACCC under subsection 95ZE(1) of the *Competition and Consumer Act 2010* (the Act) to monitor prices, costs and profits relating to the supply of domestic air passenger transport services.

The direction includes a requirement for the ACCC to report on its monitoring at least once every quarter. The direction is for a period of 3 years.

In announcing the direction, the 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 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 Act. We will investigate and prioritise enforcement action where we form the view that conduct is likely to breach the Act. Consistent with normal practice, we will not be publicly commenting on active investigations.

In carrying out its functions, it may be that the ACCC identifies that the level of competition within the industry is diminishing and/or identifies anti-competitive behaviour, but short of thresholds for enforcement action. We will recommend potential policy options to government should there be signs that competition is not effective.

The monitoring direction provides the ACCC with the ability to compel information from relevant companies within the industry. We have established arrangements for collecting monthly and quarterly data from the Qantas Group, Virgin and Rex. These three airline groups supply the vast majority of regular domestic air passenger services in Australia. We will also seek qualitative information from airlines from time to time, such as Board papers relating to company strategy.

Further information about our approach to fulfilling our obligations under the monitoring direction and potential investigations can be found in the first public report published in September 2020.²

The structure of this second report is as follows:

- discussion of relevant industry developments, notably the finalisation of the sale of Virgin to Bain Capital and its authorised coordination with Alliance Airlines (Alliance)
- analysis of key industry metrics including passenger numbers, the number of routes in operation, the degree to which people have a choice of airline group, and each airline's share of total passengers
- an exploration of potential changes to the scheme for allocating take-off and landing slots at Sydney Airport in order to promote competition between airlines.

1 The Hon Josh Frydenberg MP (the Treasurer), 'ACCC directed to monitor domestic air passenger services', media release, 19 June 2020.

2 Available at: <https://www.accc.gov.au/publications/report-airline-competition-in-australia>.

2. Industry developments

2.1 Opening up of state borders drives domestic airline activity

2020 has been a year of upheaval for the aviation sector, which has likely suffered more as a result of COVID-19 than any other industry. However, there is cautious, but growing optimism within the industry that the opening of state borders will drive significant domestic travel over Christmas and into 2021.

Activity in recent months remains well down on pre-COVID levels. Some signs of life in July were largely snuffed out with the second wave of COVID-19 infections in Victoria, which resulted in state border closures being reinstated or retained throughout the country. Domestic traffic was also hurt by the absence of international travellers, business meetings continuing to be conducted via video, and the lack of major events that attract interstate visitors.

Over this period, airlines have significantly scaled back their network routes and frequencies with a significant reliance on Australian government funding to maintain a minimum level of connectivity across the country. The reduction in network coverage and capacity was particularly acute for Virgin, in the context of its fleet simplification and the administration and sale process.

However, we have also seen airlines take an opportunistic and agile approach to network management, seeking to tap into demand for particular routes and services to bring in much-needed cash in this environment, even if expected revenues are insufficient to cover fixed costs and therefore make a profit.

Although outside the scope of the ACCC's monitoring, chartered aviation services appear to have been resilient in response to the challenges posed by COVID-19. Alliance publicly reported that its total flight hours were stable in the 2020 financial year against 2019 levels, with its charter flights increased due to social distancing requirements and a lack of availability of services from other operators.³ Alliance expects heightened revenue from charter services will continue through the 2021 financial year.⁴ It has also recently expanded its regular passenger transport offering with flights between Canberra, the Sunshine Coast, and Cairns.⁵

With signs that all states including Victoria have COVID-19 under some control, and key state borders opening up in November and early December, there is growing optimism that the industry can now begin its recovery. Airlines are increasing capacity to meet pent-up demand for travel as people come out of lockdowns and other travel restrictions wanting to see family and friends or just get away for a holiday. As this happens, the extent to which the industry relies on government support is diminishing. Some among the industry have gone as far as suggesting that with the holiday season, and continued growth into 2021, activity may approach pre-COVID levels on some leisure routes.

However, optimism is still cautious and the recovery is fragile. This was highlighted by the level of disruption caused by COVID-19 cases in South Australia in mid-November. Airlines observed a 'freeze' in sales and were forced to cancel flights as movement restrictions were reinstated.

For much of 2020, airlines have been making decisions with a view to limiting the extent of losses and striving just to survive. However, a sustained recovery, supported by effective management of COVID-19 cases and minimal movement restrictions, may enable airlines to move towards profitable operations and compete against each other for market share. This kind of competition, if it eventuates, will result in the best outcomes for consumers.

3 Alliance Aviation Services, *Annual report: For the year ended 30 June 2020*, 6 August 2020, pp. 5–6; Alliance Aviation Services, *Investor presentation: Capital raising*, 11 June 2020, p. 20.

4 Alliance Aviation Services, *Investor presentation: Capital raising*, 11 June 2020, p. 20.

5 Canberra Airport, *Media release: Sunshine Coast flights take-off from Canberra Airport*, 23 October 2020.

2.2 New owner Bain Capital sets the future direction for Virgin Australia

Bain Capital officially became the new owner of Virgin in November 2020 as the airline emerged from a 7-month period of voluntary administration. The transfer of ownership followed the announcements that CEO Paul Scurrah and several members of Virgin's Board would step down, with Jayne Hrdlicka appointed as the new CEO.

The relaunched airline is now able to view the aviation market with greater certainty over its future and without the burden of significant debts. The potential for the airline to take a new approach to the sector led to some commentators to speculate that Bain Capital would operate Virgin as a low-cost carrier (LCC) focused on leisure markets. In particular, this speculation was due to the appointment of ex-Jetstar CEO Ms Hrdlicka as well as the airline's profitability prior to its transformation into a full service carrier. Virgin had also closed its LCC subsidiary Tigerair after entering administration.

Nonetheless, upon her commencement on 18 November, Ms Hrdlicka announced plans to position Virgin as a mid-market carrier.⁶ Virgin said that it will serve 'all segments of the market', including price conscious corporate travellers, small to medium businesses, premium leisure travellers and holidaymakers.

Virgin outlined major elements of its plan including:

- an intention to retain a domestic market share of roughly one third (as was the case pre-COVID)
- rolling out a new-look lounge across its lounge network, beginning with Adelaide in early 2021
- aligning its business class offering with its core customers' expectations
- restructuring Virgin Australia Regional Airlines (VARA) to become a more sustainable and profitable business following a comprehensive business review.

As Australia's second largest airline, Bain Capital's direction for Virgin is likely to have significant implications for competition in the domestic airline industry. Were Bain Capital to change its view and transition Virgin to an LCC, it would likely provide direct competition for Jetstar in the leisure market, but leave Qantas facing limited competition for corporate customers. This could provide Qantas with an opportunity to modify its corporate offering, such as increasing fares and/or lowering service standards.

Furthermore, if Virgin was to withdraw from a significant number of routes it used to serve prior to COVID-19, it may lead to fewer passengers having an effective choice of airline and therefore reduced competition between airlines. Qantas expects that its share of the domestic market will grow from around 60% to up to 70% as the market recovers, owing to Virgin reducing its fleet and closing Tigerair.⁷ In this regard, it is notable that Virgin has received interim authorisation from the ACCC to cooperate with Alliance. This may allow Virgin to provide services to a wider network in regional Australia than would otherwise be possible with its streamlined fleet of Boeing 737s.

Authorisation for Virgin and Alliance to coordinate services

On 19 November 2020 the ACCC granted interim authorisation to Virgin and Alliance allowing them to cooperate on 41 regional routes and two short-haul international routes. The cooperation will allow the airlines to share information, agree on service capacity and schedules, and potentially share revenues on the routes on which they operate, including for new routes not currently serviced by either airline.

The ACCC's preliminary view was that these arrangements are likely to result in a public benefit by assisting in the re-establishment of Virgin's national network of routes, thereby promoting competition in airline services. Cooperating to provide services on these regional routes will assist Virgin and Alliance to efficiently manage capacity and quickly respond to increases in demand as travel restrictions ease.

6 Virgin Australia, *Media release: Ready for take-off: Virgin Australia Group sours out of administration, unveils future direction*, 18 November 2020.

7 Qantas, *Qantas Group FY20 financial results—navigating exceptional conditions*, 20 August 2020.

The cooperation will mean that Virgin and Alliance will not compete with each other on the routes covered by the agreement. The ACCC's preliminary view was that any public detriment resulting from reduced competition between Alliance and Virgin is likely to be limited, given Alliance's limited number of scheduled regular passenger services. The ACCC also considers that other airlines, including Qantas Airways and Qantas-owned Jetstar, are likely to compete strongly with Alliance and Virgin on many of the routes covered by the agreement.

The ACCC will consider this issue further in the course of its review of the substantive application for authorisation.

2.3 Continued government support for certain services

Since September 2020, the government announced it was extending two support programs for the airline industry in response to challenges presented by COVID-19. It extended its support under the Regional Airline Network Support (RANS) program from 31 December 2020 to 28 March 2021.⁸ In December 2020, it further extended its Domestic Aviation Network Support (DANS) program from 31 January 2021 to 28 March 2021.⁹

The DANS program supports airlines to provide services on the 50 domestic routes with the most traffic. Qantas and Virgin have been awarded contracts worth \$309 million and \$243 million under the program respectively.¹⁰

The RANS program provides support for air services to connect regional Australia to freight, medical testing, supplies and essential personnel. Qantas, Virgin, Rex and a number of smaller airlines have received funding to provide services on select routes. Although the government extended the RANS program, the \$198 million in available funding has not increased.

The extension of the RANS program reduces the need for airlines to coordinate their services. The ACCC granted Rex authorisation in September 2020 to coordinate flight schedules and share revenue with other airlines on 10 regional routes. Authorisation is granted until 30 June 2021. However, the airlines are unlikely to coordinate services on the regional routes when they can provide services with RANS support. The airlines may choose to coordinate services in April–June 2021, once RANS support expires.

2.4 Rex's planned entry to the domestic market

Regional operator Rex has further progressed its plans to expand into major domestic routes. On 1 December 2020 it began selling tickets for Sydney–Melbourne flights which are due to commence from 1 March 2021. It has also stated that it will further expand across the broader Sydney–Melbourne–Brisbane triangle.¹¹

Rex took delivery of its first Boeing 737-800 aircraft in November 2020, which followed its announcement in September to lease six 737 aircraft.¹² The remaining five aircraft are to be phased in over the following four months. Rex announced it had signed an agreement for up to \$150m funding for these domestic jet operations¹³; and hopes to expand its 737 aircraft fleet to ten by the end of 2021.¹⁴ Its 737s will be configured with business class seats.

8 Minister for Infrastructure, Transport and Regional Development, *Media release: Budget support for aviation soars to new heights*, 28 September 2020.

9 Minister for Infrastructure, Transport and Regional Development, *Media release: Further Government support for aviation and appointment of expert advisory panel*, 14 December 2020.

10 In addition, Rex and Airnorth Regional Airlines have been awarded contracts worth \$795,000 and \$6.3 million respectively under the DANS program. Further information is available on the AusTender website: <https://www.tenders.gov.au/>.

11 Regional Express, *Media Release: Rex Launches Into Sydney–Melbourne–100,000 Tickets On Sale From \$79*, 2 December 2020.

12 Regional Express, *Media Release: Rex locks in six Boeing 737-800 NG for domestic jet operations*, 30 September 2020.

13 Regional Express, *Media Release: Rex signs binding agreement with PAG on funding for domestic jet operations*, 19 November 2020.

14 Regional Express, *Media Release: Rex Launches Into Sydney–Melbourne–100,000 Tickets On Sale From \$79*, 2 December 2020.

2.5 Refund policies of each airline are a point of competition

Given the possibility of further border closures if COVID-19 outbreaks occur, consumers will need to have confidence that they will receive a refund for a cancelled flight if they are to feel comfortable booking flights for early 2021. It may also be the case that an airline's terms and conditions providing for refunds will become a more important differentiator from a competition perspective than before. While all airlines have similar obligations under the Australian Consumer Law, the ability of a consumer to rebook or receive a refund also depends on the specific terms and conditions of the purchase.

Airlines have different policies on refunds for flights disrupted by COVID-19 which are outside the airline's control. We understand that Qantas, Virgin and Rex provide flight credits or refunds due to events beyond their control, including COVID-19 disruptions, however Jetstar only provides flight credits.¹⁵

Where the airlines' terms and conditions allow for refunds, the general conditions are:

- if a flight is significantly delayed¹⁶ or cancelled, the airline may offer a direct refund, or offer an alternative flight arrangement. If the alternative arrangement is not suitable, the passenger is entitled to a refund
- if multiple flights were booked, the airline will refund the proportion of the ticket for flights not yet flown.

The ACCC has been working with the airlines to ensure they provide refunds consistent with their refund policies.

Virgin is unable to provide refunds for bookings made on or before 20 April 2020 due to its voluntary administration process. However, affected customers are eligible for credits under its Future Flight credits program.¹⁷ Customers who had booked a Tigerair flight are eligible for a Future Flight credit for use on Virgin-operated services for the value of the Tigerair credit.

15 Qantas, *Conditions of Carriage*, section 9.2, viewed 20 November 2020; Jetstar, *Conditions of Carriage*, section 9.2, viewed 20 November 2020; Rex, *Conditions of Carriage*, section 11, viewed 24 November 2020; Virgin, Virgin Australia Guest Compensation Policy, section 4, viewed 10 December 2020.

16 Policies on what constitutes a 'significant delay' differs by airline, but is generally defined as either a set number of hours, or a delay that impacts upon the passenger's travel plans, for example a delay that would force the passenger to cancel their trip.

17 For further information see: <https://travel.virginaustralia.com/au/coronavirus-update/future-flight-credits>, viewed 19 November 2020.

3. Key industry metrics and analysis

This section of the report presents analysis of key industry metrics. Unless specified otherwise, the metrics are calculated using information collected from Qantas Group, Virgin and Rex on a monthly and quarterly basis. The data presented here includes activity up to the end of September 2020.

3.1 Domestic aviation recovery stalled with border restrictions following Victorian outbreak

Despite airlines having cautious optimism about the future (as discussed in section 2.1), figure 1 shows that Australian domestic activity up to September 2020 was still well down on pre-COVID levels. Services started to recover in June 2020 as some state border restrictions were eased. However, the recovery was disrupted following a second outbreak of COVID-19 in Victoria, with movement restrictions resulting in lower passenger and capacity numbers in August relative to July.

Figure 1 Australian domestic air services—September 2019 to September 2020



Source: Bureau of Infrastructure, Transport and Regional Economics; Australian domestic airline activity.

Note: Data is for regular public transport (i.e. commercial flight operations on fixed schedules and specific routes available to the general public) and does not include charter operations.

Monthly capacity and passenger numbers in September 2020 were down 81 and 87% respectively compared to September 2019. The greater decrease in passenger numbers results in a lower average load factor. Through 2019, each flight was 79% occupied on average. This figure fell to 28% in April 2020 as governments' introduced movement restrictions and flights began to be driven more by government subsidies than passenger numbers. The average load factor remained around at 55-60% in the July-September 2020 period.

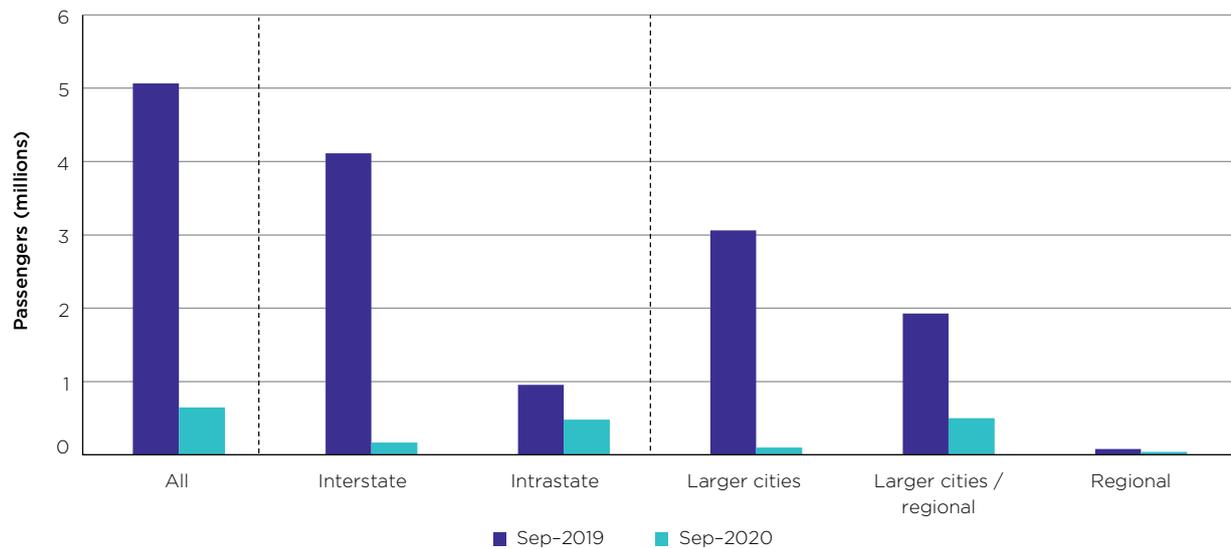
3.2 COVID-19 and associated border closures have changed where people are flying

This year has not only resulted in a significant reduction in the number of overall passengers, but also changed where they are flying. This change has been driven by a mix of border closures, government subsidy programs, airlines reviewing the ability for a route to bring in much-needed cash, and changing passenger demand in a pandemic.

Activity moved away from the ‘golden triangle’ to holiday destinations in northern Australia

The Australian domestic aviation sector is typically heavily dominated by interstate routes between the larger capital cities. Figure 2 shows that in September 2019, 81% of all passengers flew interstate. However, the chart also illustrates how the sector has moved towards intrastate flights in September 2020 in response to border closures. Intrastate flights accounted for 76% of all passengers in September 2020.

Figure 2 Monthly passenger numbers by route category—September 2019 and September 2020



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

Note: ‘Larger cities’ are Sydney, Melbourne, Brisbane, Adelaide, Perth, Canberra and the Gold Coast. Remaining locations are considered to be ‘regional’.

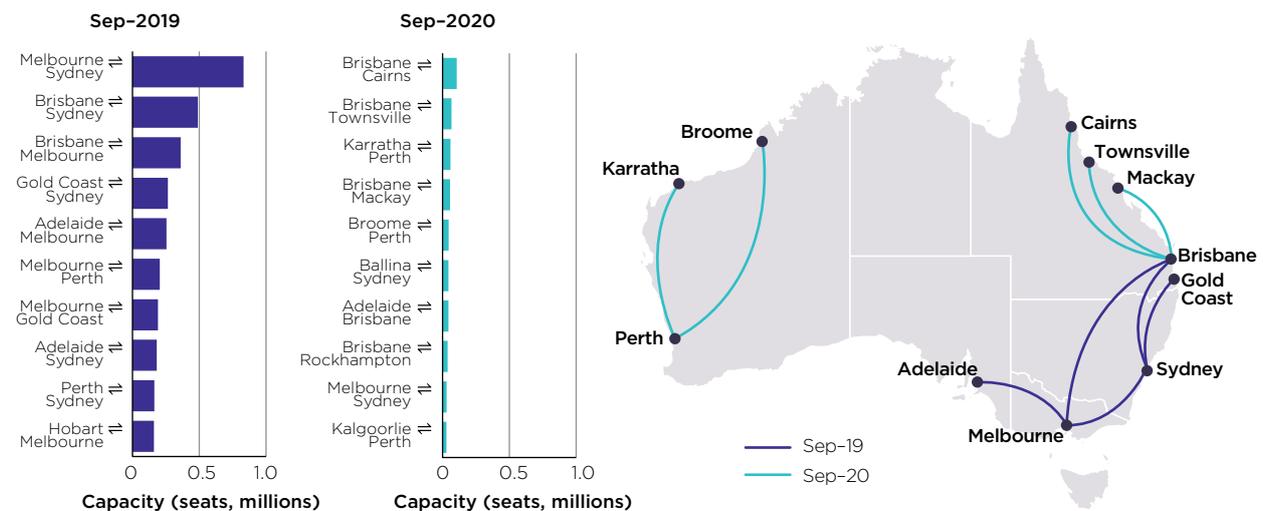
Figure 2 also provides a breakdown of routes by classifying locations into larger cities and regional destinations. It shows that while fewer people travelled to regional destinations than larger cities pre-COVID (September 2019), routes containing a regional destination have been more resilient this year (September 2020) than travel between the larger cities.

Figure 3 shows the busiest routes (by capacity) in September 2019 and September 2020. It depicts a significant transition from the ‘golden triangle’ between Sydney, Melbourne and Brisbane to intrastate routes reflecting demand for leisure travel within Queensland and Western Australia.

Figure 3 Busiest routes by monthly capacity—September 2019 and September 2020

Chart: Top ten routes

Map: Top five routes



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

With border restrictions easing, it is likely that the mix of busiest routes will shortly begin to reflect the pre-COVID situation with Sydney–Melbourne–Brisbane routes again at the top of the list. The airlines report a recent surge in demand for flights out of Melbourne, following the reopening of Victoria’s borders.¹⁸ Leisure routes are also expected to be the first to show signs of recovery as people seek out domestic holidays in lieu of overseas travel, as well as catching up with family and friends that had been behind closed borders earlier in the year.

Some airlines scaling back routes, others expanding

Each of the major airlines have been actively reviewing their domestic network in response to COVID-19 and subsequent border closures. Although each of the respective airlines have reduced their weekly flights, they have also increased services on select routes, or expanded into new routes. Some new services may be short-lived if the intent was to bypass an airport in a state subject to a border closure, though other new services may represent new strategies for the respective airline and therefore may be longer lasting.

Virgin has been particularly active in modifying its network. It has discontinued its Tigerair subsidiary, consolidated its domestic airline fleet to Boeing 737s and has exited some smaller routes, including flights to Uluru, Albury and Tamworth.¹⁹ It has also received interim authorisation to coordinate services with Alliance in the short term in order to maintain services on regional routes.

Airlines including Rex and Alliance are expanding their services. These two airlines have taken advantage of a depressed industry in order to boost their fleet of aircraft at lower cost.²⁰ Rex announced its entry into the Sydney–Melbourne–Brisbane triangle, and has been in discussions to provide services on some routes that Virgin has exited.²¹ Alliance has expanded into regular passenger transport routes between Canberra, the Sunshine Coast, and Cairns.²²

18 Qantas, *Media Release: Qantas and Jetstar help loved ones reunite as NSW/VIC border opens*, 23 November 2020; Virgin Australia, *Media Release: Virgin Australia flights to Queensland take-off as travel opens to Victorians*, 25 November 2020.

19 Virgin Australia, *Media Release: Virgin Australia Group announces plan to focus on core strengths, re-establishing itself as an iconic Australian airline*, 5 August 2020; Virgin Australia, *Media Release*, 9 September 2020, sourced from CAPA.

20 Regional Express, *Media Release: Rex locks in six Boeing 737-800 NG for domestic jet operations*, 30 September 2020; Alliance Aviation Services, *ASX release—Alliance Aviation expands fleet with acquisition of 14 Embraer E190 aircraft*, 3 August 2020.

21 Regional Express, *Media Release: Rex update on regional routes abandoned by Virgin Australia*, 23 September 2020.

22 Canberra Airport, *Media Release: Sunshine Coast flights take-off from Canberra Airport*, 23 October 2020.

Qantas reduced the quantity of flights on most routes, however it continues to operate most of its pre-COVID network unless routes are subject to border closures. Additionally Qantas has expanded into several new routes including:

- Brisbane–Port Macquarie²³, which was previously serviced by Virgin
- Sydney–Orange and Sydney–Merimbula²⁴ in competition with Rex
- Canberra to Sunshine Coast, Cairns, and Hobart²⁵, which have also attracted entry by some smaller airlines.

3.3 Market concentration has increased

Market concentration can be a useful indicator of the level of competition in an industry, which in turn reflects the pressure that a supplier can feel with regards to pricing or improving their service offering. An industry with significant economies of scale such as air passenger transport is unlikely to have a large number of competitors. However, an airline may also feel competitive pressure from the threat of competitors entering a particular route in the future.

The majority of Australian domestic routes are serviced by a single airline group. This characteristic of the industry reflects both the size of the country and the number of routes connecting regional destinations, which do not necessarily have the patronage to support multiple carriers. This means that airline groups serving these routes would likely have little competitive pressure to drive performance. However, some of these routes are state government ‘regulated’ routes, where there may be competition between airline groups in the tender process to operate the route as the sole airline for a fixed period.

Figure 4 depicts data collected from Qantas, Virgin and Rex, which indicates that 92 routes were serviced by a single airline group in September 2019.²⁶ This compares to 66 routes on which there were two airline groups in operation, and three routes on which there were all three. Fewer routes were being serviced in September 2020 relative to September 2019. However the proportion of routes serviced by a given number of airline groups did not change significantly, about 60% of routes continue to be serviced by one airline group. In some cases, an airline group has exited a route, leaving its competitor as the sole operator. In other cases, the sole airline group serving the route has suspended services.

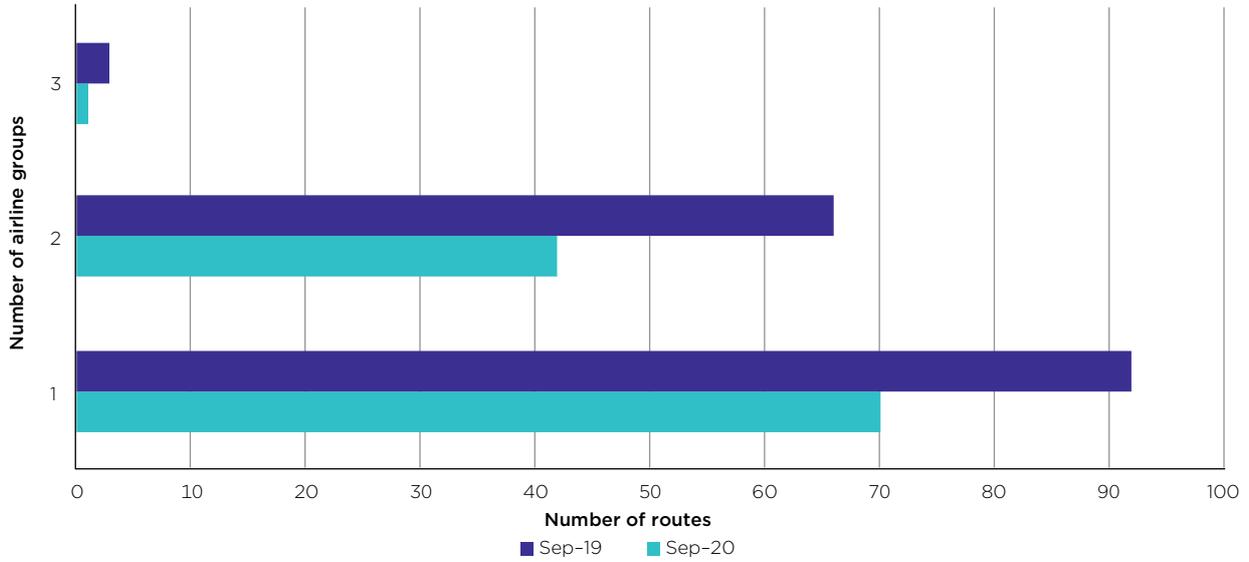
23 Qantas, *Media Release: Qantas to boost regional flights with new Brisbane–Port Macquarie service*, 10 September 2020.

24 Qantas, *Media Release: From the beach to the bush: Qantas launches two new NSW routes*, 1 July 2020; Qantas, *Media Release: Qantas to launch flights to Merimbula in time for summer*, 9 October 2020.

25 Qantas, *Media Release: Qantas adds three new routes from Canberra*, 6 November 2020.

26 Classifying multi-stop flights as a single route.

Figure 4 Number of airline groups by route—September 2019 and September 2020



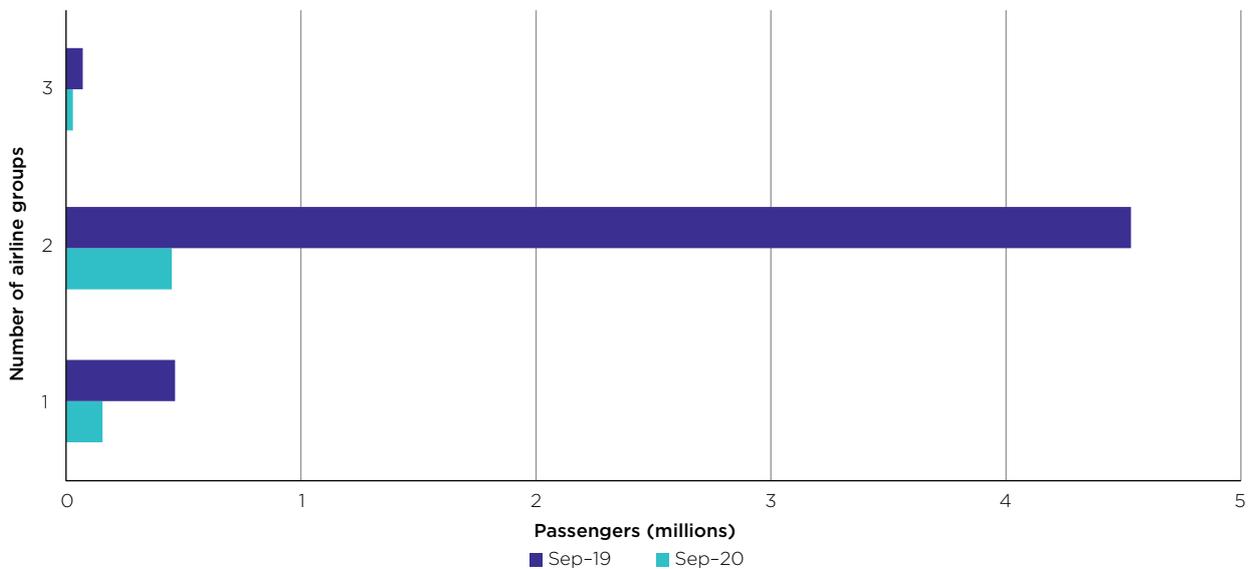
Source: Data collected by ACCC from Qantas, Virgin Australia and Rex.

Note: Multi-stop flights are treated as single routes.

The Qantas Group (including Jetstar) operated on 114 domestic routes in September 2019, the largest of any domestic airline. Virgin (including Tigerair), operated on 74 domestic routes in the same month, whilst Rex operated on 45 routes. By September 2020, Virgin had reduced its operating routes to 39, a reduction of almost half. Qantas and Rex had also reduced their operating routes by 20–30% by September 2020, to 82 and 36 routes respectively.

While the majority of *routes* are serviced by a single airline group, the majority of *passengers* have a choice of airline group they can travel with. This dynamic exists because more passengers fly on routes between major cities on which there are competing airlines. Figure 5 shows that in September 2020, 70% or about 450,000 customers flew on routes with a choice of two airline groups. In the same month, 24% of customers flew on a route operated by only one airline group.

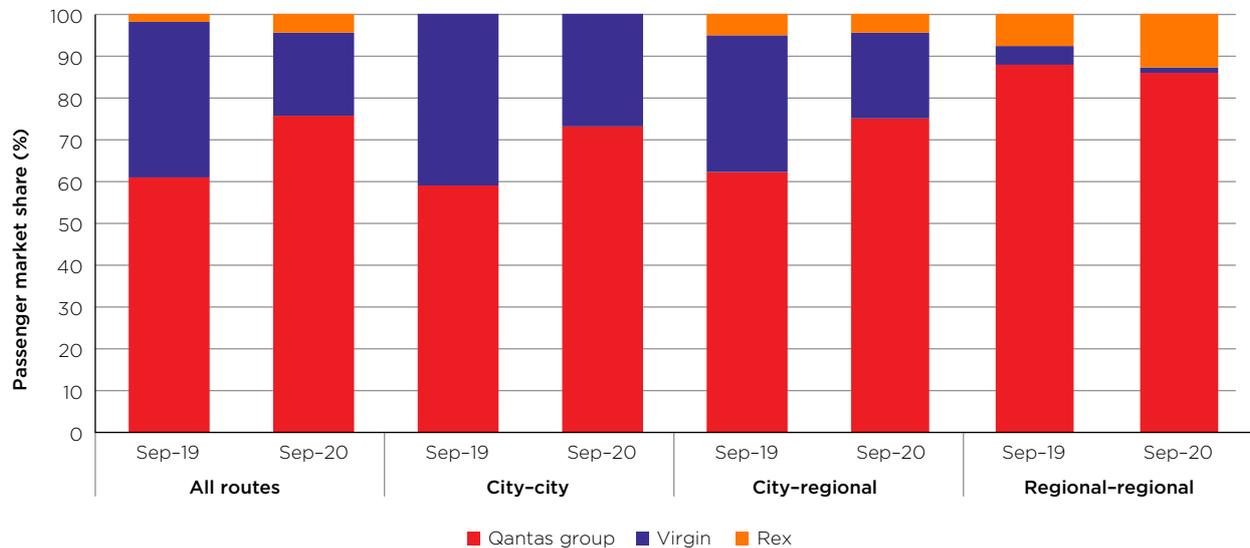
Figure 5 Passenger numbers on routes served by one or more airline groups—September 2019 and September 2020 (millions)



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

In September 2019, Qantas carried 60% of all domestic passengers, as shown in figure 6. Its market share was highest on routes between regional airports, with 87% of passengers. On routes between larger cities and regional airports, where it faced the greatest degree of competition from both Virgin and Rex, it was still the dominant airline with 62% of passengers.

Figure 6 Airline group market share by passengers flown—September 2019 and September 2020



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

Note: Larger cities (referred to as 'City' in figure 6) are Sydney, Melbourne, Brisbane, Adelaide, Perth, Canberra and the Gold Coast. Remaining locations are considered to be 'regional'.

By September 2020, Qantas' overall domestic passenger market share had increased to 75%. This increase may reflect Virgin's proportionally greater reduction in services as a result of both COVID-19 and its administration process. On intra-regional routes, it has been Rex (rather than Qantas) that has increased its share of passengers at the expense of Virgin.

We expect market shares to exhibit continued volatility in the short term as the industry operates at a fraction of pre-COVID capacity. Qantas expects that as the domestic market recovers, its share will grow from 60 to up to 70% as a result of Virgin reducing its fleet and closing Tigerair.²⁷ Meanwhile, Virgin has publicly stated that it intends to 'retain a domestic market share of roughly one third (as was pre-COVID)'.²⁸

3.4 Airlines are generating significantly lower revenues

Airline industry revenues have declined significantly through 2020 due to commensurate declines in passenger numbers. Industry revenues are expected to recover significantly as interstate travel restrictions ease. However, the ongoing uncertainty with the likelihood of further COVID-19 outbreaks and resultant disruptions to the industry may affect the rate of recovery.

The average revenue per passenger—a proxy measure for the average airfare paid—increased between 2019 and 2020 across the three airline groups. However, this does not mean that airlines have been increasing airfares. The airlines have generated revenues in 2020 from a significantly lower number of passengers flying on a different mix of routes (as highlighted in section 3.2), which will affect average revenue calculations. For example, passenger volumes are down significantly on the Melbourne–Sydney route, which has a lower average fare than the network average. Monthly revenues per passenger are expected to fluctuate as the industry recovers and the mix of routes flown reverts to a greater emphasis on interstate travel. More detailed public information on the movement in domestic airfares can be found on the Bureau of Infrastructure, Transport and Regional Economics (BITRE) website.

²⁷ Qantas, *Qantas Group FY20 financial results—navigating exceptional conditions*, 20 August 2020.

²⁸ Virgin Australia, *Media release: Ready for take-off: Virgin Australia Group soars out of administration, unveils future direction*, 18 November 2020.

4. Overcoming barriers to competition

4.1 Opportunity to stimulate competition through the way that slots at Sydney Airport are managed

Slots are an essential input for airlines looking to provide air passenger services. At slot-constrained airports, such as Sydney Airport, access to slots is a key barrier to entry and expansion.

As outlined in section 2.4 of this report, Rex is continuing to progress its plans to expand into major domestic routes. In expanding its services to include routes between Sydney and Melbourne, Rex is relying on access to peak period²⁹ slots at Sydney Airport. Rex has secured slots for its launch in March 2021, which falls at the end of the current slot season, and is continuing to negotiate access to peak period slots for the following slot season commencing in April 2021. Access to adequate peak period slots will be a key consideration for Rex as it continues to roll out its expansion plans.

The government has initiated a review of demand management at Sydney Airport, which will include consideration of the slot management scheme

In November 2020, the Australian government released the Sydney Airport Demand Management: Discussion Paper³⁰ as the first step of conducting a comprehensive review of demand management at Sydney (Kingsford Smith) Airport.

A key purpose of the review is to consider whether the Sydney Airport slot management scheme remains appropriate, including in light of recent changes to the Worldwide Slot Guidelines and the Worldwide Airport Slot Guidelines, many of which were designed to address competition issues.

In the ACCC's September 2020 *Airline Competition in Australia report*³¹, slot hoarding was identified as one of the behaviours that might damage competition in the air passenger services market/s. Sydney Airport is Australia's busiest airport, key hub and international gateway. Access to slots at the airport is crucial for airlines seeking to compete in the Australian air passenger services market/s, such as Rex.

The ACCC's submission highlights ways in which slot management can impede competition

The ACCC has made a submission to the review, focussing on two interrelated ways in which the existing slot management scheme can impede competition:

1. Rules that allow airlines to retain slots in perpetuity limit opportunities for new or expanding airlines to acquire slots needed to launch new services and compete.
2. Airlines are able to exploit the scheme by acquiring and hoarding slots for strategic reasons, resulting in inefficient slot use and further diminishing opportunities for increased competition.

Changes to the slot management scheme should ensure the most efficient use of slots and foster an environment of robust competition

The ACCC considers that a fundamental objective of any reform to the existing slot management scheme should be to ensure that the allocation of Sydney Airport slots results in the most efficient utilisation of slots and fosters an environment of robust competition between airlines.

The legislation governing Sydney Airport's slot management scheme is outdated and does not reflect contemporary worldwide slot management practices. We consider it is important that the scheme is

29 Peak period is defined as 6–11 am and 3–8 pm, Monday to Friday.

30 Available at: <https://www.infrastructure.gov.au/aviation/airport/review-sydney-airport-demand-management/files/sadm-discussion-paper.pdf>.

31 Available at: https://www.accc.gov.au/system/files/20-29RPT_Airline%20competition%20inquiry_FA.pdf, p. 11.

updated to reflect the objectives of the Worldwide Airport Slot Guidelines, particularly those which go to supporting and enhancing competition between airlines.

The scheme should also be refined to minimise opportunities for airlines to misuse slots and to strengthen compliance monitoring and enforcement of the scheme to deter airlines from engaging in slot misuse.

The ACCC will engage closely with the review of demand management at Sydney Airport and continue to advocate for changes that will enhance competition. As the sector recovers, we will continue to monitor the situation relating to Sydney Airport slots, to identify any signs that access to slots may be hindering competition in the airline industry.

Glossary

The Act	<i>Competition and Consumer Act 2010 (Cth)</i>
ACA	Airport Coordination Australia. ACA allocates slots for aircraft runway movements at a number of airports including Sydney Airport.
BITRE	Bureau of Infrastructure, Transport and Regional Economics
Chartered flight	A flight that is chartered for a particular journey and is not part of an airline's published schedule.
DANS	Domestic Aviation Network Support. A Federal Government program introduced in response to the COVID crisis in order to fund a minimum number of flights on key domestic routes.
DITRDC	Department of Infrastructure, Transport, Regional Development and Communications
FIFO	Fly-in, fly-out. The commute of people employed in remote areas where they are flown temporarily to the work site instead of relocating permanently.
Full service carrier	An airline that typically offers passengers in-flight entertainment, checked baggage, meals, beverages and comforts such as blankets and pillows in the ticket price.
Golden triangle	Air routes connecting Sydney, Melbourne and Brisbane.
IATA	International Air Transport Association. IATA supports aviation with global standards for airline safety, security, efficiency and sustainability.
Larger city	Sydney, Melbourne, Brisbane, Adelaide, Perth, Canberra and the Gold Coast.
Load factor	The degree to which seats (i.e. capacity) are filled by passengers.
LCC	Low cost carrier. An airline that operators with an emphasis on minimising operating costs and therefore does not provide the full service and amenities in the fare.
RANS	Regional Airline Network Support. A Federal Government program introduced in response to the COVID crisis in order to fund a minimum number of flights on key regional routes.
Regional	Domestic locations other than Sydney, Melbourne, Brisbane, Adelaide, Perth, Canberra and the Gold Coast.
Regulated route	A low volume route for which government regulation limits provision of air services to a single licensed operator in order to provide stability and ensure that the route is serviced.
RPT	Regular passenger transport. Flight operations performed for remuneration and conducted to fixed schedules over specific routes, and on which seats and/or cargo space is available to the general public.
Slot	A permission which enables an airline to schedule a landing or departure at a particular airport during a specific time period.
VARA	Regional airline operated by Virgin Australia.



AUSTRALIAN COMPETITION
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