



28 March 2020

## PUBLIC REGISTER VERSION

Australian Competition and Consumer Commission  
Darrell Channing  
Adjudication Branch  
GPO Box 3131  
Canberra ACT 2601

By email: [darrell.channing@acc.gov.au](mailto:darrell.channing@acc.gov.au)  
[adjudication@acc.gov.au](mailto:adjudication@acc.gov.au)

Dear Darrell

### **Qantas – China Eastern: Application For Variation of Conditions of Authorisation A91470 and A91474**

We refer to the Commission's conditional authorisations A91470 and A91474 of the Joint Coordination Agreement between Qantas Airways Limited (**Qantas**) and China Eastern Airlines Corporation Limited (**China Eastern**) (together, the **Applicants**) dated 21 August 2015 (**Authorisation**). Appendix B of the Authorisation requires the Applicants to maintain minimum levels of capacity and to increase capacity on routes between Australia and Shanghai over the term of the Authorisation (**Conditions of Authorisation**).

We also refer to the Applicants' previous application dated 27 February 2020 for a variation of the Conditions of Authorisation in respect of the Northern Winter 2019 Scheduling Season (**Northern Winter 2019 Variation Application**) and the Commission's approval of that application on 25 March 2020.<sup>1</sup>

As the Commission is aware, the outbreak of the Novel coronavirus (**COVID-19**) – which was first reported in Wuhan, China on 31 December 2019 and was declared by the World Health Organisation to be a pandemic on 11 March 2020<sup>2</sup> (**COVID-19 Pandemic**) – has led to unprecedented and widespread impacts on airlines globally due to ongoing flight and entry restrictions imposed by various Governments worldwide and a precipitous decline in demand for travel. On 18 March 2020, the Australian Government issued 'do not travel' advice to all Australians regardless of their destination.<sup>3</sup> On 24 March 2020, the Australian Prime Minister imposed a ban on all Australians travelling overseas.<sup>4</sup>

As the situation has evolved, the Qantas Group has announced widespread network changes impacting international services operated by Qantas, Jetstar, Jetstar Japan and Jetstar Pacific.<sup>5</sup> The suspension of Qantas flights between Sydney and Shanghai which took effect from 9 February 2020 will continue to apply, at this stage, until at least mid July 2020. Qantas continues to work closely with the Australian Government on this issue and all network decisions are being regularly reviewed based

<sup>1</sup> See: <https://www.acc.gov.au/public-registers/authorisations-and-notifications-registers/authorisations-register/qantas-airways-limited-china-eastern-airlines-corporation-limited-authorisations-a91470-a91471>

<sup>2</sup> World Health Organisation, 11 March 2020. See: <https://www.who.int/emergencies/diseases/novel-coronavirus-2019/events-as-they-happen>

<sup>3</sup> See: <https://www.smartraveller.gov.au/crisis/covid-19-and-travel> (accessed 18 March 2020).

<sup>4</sup> See: <https://www.pm.gov.au/media/update-coronavirus-measures-24-March-2020>

<sup>5</sup> See: <https://www.qantasnewsroom.com.au/>



on the circumstances. There is at least a possibility that Qantas' Sydney-Shanghai cancellations may need to be extended beyond July 2020.

In February 2020, China Eastern announced the cancellation of certain flights between Australia and China as a result of the Coronavirus Outbreak. As at the date of this application, China Eastern currently intends to operate 7 flights per week in respect of the Sydney-Shanghai route and 7 flights per week in respect of the Melbourne-Shanghai route. However, even as this application is being lodged, the Ministry of Foreign Affairs of the People's Republic of China has made further announcements regarding the temporary suspension of entry regarding foreign nationals<sup>6</sup> and the Civil Aviation Administration of China has also published a notice regarding the further reduction of international passenger flights which will apply from 29 March 2020.<sup>7</sup> As a result, China Eastern will need to further modify its schedule to and from Australia.

As a result of the ongoing network changes outlined above and the prospect of potential further changes, pursuant to clause 5(1) of the Conditions of Authorisation, the Applicants seek an urgent variation of the following clauses of the Conditions of Authorisation in respect of the Northern Summer 2020 Scheduling Season (1 April-31 October 2020):

- clause 1(a), which requires that:

*For each Scheduling Season which commences during the Term, the Applicants must make available not less than 100 per cent of the applicable Sydney – Shanghai City Pair Scheduling Season Base Year Seat Capacity.*

- clause 1(c), which requires that:

*For each Scheduling Season which commences during the Term, the Applicants must make available not less than 100 per cent of the applicable Australia – Shanghai Scheduling Season Base Year Seat Capacity. To avoid doubt, this obligation requires the Applicants to make the specified capacity available in aggregate across all Routes between Australia and Shanghai.*

- clause 1(d), which requires that:

*On a rolling basis over the Term, the Applicants must increase the applicable Australia-Shanghai Scheduling Season Base Year Seat Capacity by not less than the Australia-Shanghai CAGR. To avoid doubt:*

- this obligation requires the Applicants to make the specified capacity available in aggregate across all Routes between Australia and Shanghai;*
- any capacity the Applicants make available in accordance with clause 1(b) is also capacity made available in accordance with the Applicants obligations under this clause 1(d).*

### **'Exceptional Circumstances'**

Consistent with the Commission's view in respect of the Northern Winter 2019 Variation Application, the Applicants consider that the COVID-19 Pandemic clearly constitutes 'Exceptional Circumstances' under clause 5(1) of the Conditions of Authorisation.<sup>8</sup> Exceptional Circumstances are defined to include:

- force majeure events, including natural disasters, national emergency, insurrection, riot, war, pandemic; or*
- events or factors outside of the control of the Applicants:*

---

<sup>6</sup> See further: [https://www.fmprc.gov.cn/mfa\\_eng/wjbxw/t1761867.shtml](https://www.fmprc.gov.cn/mfa_eng/wjbxw/t1761867.shtml)

<sup>7</sup> See further: [http://www.caac.gov.cn/en/XWZX/202003/t20200326\\_201748.html](http://www.caac.gov.cn/en/XWZX/202003/t20200326_201748.html)

<sup>8</sup> The Applicants consider that the COVID-19 Pandemic also constitutes a 'Material Change in Market Conditions' for the purposes of clause 5(1) of the Conditions of Authorisation but for ease seek variation on the basis of one ground only (Exceptional Circumstances).

(i) such that the Applicants cannot, or on reasonable grounds anticipate that they cannot, practically comply with the Conditions; or

(ii) which have or are reasonably anticipated to have a material adverse impact on the demand for travel on the Applicants' services or the Applicants' service operating costs, or affecting operations on the Relevant Routes.

## Variations Sought In Respect of Capacity Requirements

### Minimum Capacity Sydney-Shanghai and Australia-Shanghai Routes

For the Northern Summer 2020 Scheduling Season, the Applicants' current planned flight operations outlined above will result in the Applicants falling short of the required Sydney-Shanghai City Pair Scheduling Season Base Year Seat Capacity by 33,463 seats (-14%) but the Australia-Shanghai Scheduling Season Base Year Seat Capacity will be exceeded by a margin of 22,075 seats (7%), as shown in Table 1 below.

**Table 1: Variance Between Northern Summer Scheduling Season Base Line Capacity and Scheduled Capacity for Northern Summer 2020 Scheduling Season: Sydney-Shanghai and Australia-Shanghai Routes**

Northern Summer Scheduling Season Base Line Capacity (Seats)			Northern Summer 2020 Scheduling Season Scheduled Capacity (Seats) Anticipated At Date of Application		Variance in Total
<b>Route</b>					
<b>SYD-PVG</b>	QF	120,878	QF	39,422	<b>-33,463 seats</b> <b>(-14% SYD-PVG)</b>
	MU	111,341	MU	159,338	
	<b>Total</b>	<b>232,223</b>	<b>Total</b>	<b>198,760</b>	
<b>MEL-PVG</b>	QF	0	QF	0	
	MU	103,339	MU	158,877	
	<b>Total</b>	<b>103,339</b>		158,877	
<b>CNS-PVG</b>	QF	0	QF	0	
	MU	0	MU	0	
	<b>Total</b>	<b>0</b>	<b>Total</b>	0	
<b>TOTAL AU-PVG Routes</b>	QF	120,878	QF	39,422	<b>+22,075 seats</b> <b>(+7% AU-PVG Routes)</b>
	MU	214,684	MU	318,215	
	<b>Total</b>	<b>335,562</b>	<b>Total</b>	<b>357,637</b>	

Source: Diio Mi<sup>9</sup>

<sup>9</sup> The figures for the operated and scheduled seats for the Northern Summer 2020 Scheduling Season in Table 1 have been sourced from Diio Mi, which is an industry source using published capacity data collated by the International Air Transport Association (IATA). At this stage, it is not possible to provide equivalent total capacity figures sourced from BITRE.

Importantly, Table 1 indicates the position on the assumption that Qantas will be able to resume flying in mid July 2020 and that China Eastern will be able to continue flying certain services and resume other services to Shanghai throughout April-October 2020. However, as flagged above, it is clear that the rapidly evolving and unprecedented nature of the COVID-19 Pandemic is such that the Applicants need to retain as much operational flexibility as possible to respond appropriately and quickly. Specifically, China Eastern is already in the process of further reviewing its proposed 7 weekly services between Sydney and Melbourne to Shanghai as a result of the Australian Government's recently issued travel ban and the announcements today in respect of entry and operational restrictions being imposed. However, these changes have not yet been finalized as at the date of this application.

The extension of entry and exit restrictions imposed by Governments will lead to further network changes in coming weeks and months and this will result in the Applicants falling further below the minimum capacity requirements on the Sydney-Shanghai route and most likely also below the minimum on Australia-Shanghai routes.

Accordingly, the Applicants seek a variation of the Conditions of Authorisation such that clauses 1(a) and 1(c) of the Conditions of Authorisation are both waived in respect of the Northern Summer 2020 Scheduling Season (i.e. until 31 October 2020).

#### *Australia-Shanghai CAGR Requirement*

Even assuming the Applicants are able to operate some flights during the Northern Summer 2020 Scheduling Season, in practice, the Applicants together will be unable to achieve a total CAGR of over 4% on Australia-Shanghai Routes as required under clause 1(d) of the Conditions of Authorisation.

Prior to the COVID-19 Pandemic, the Applicants had been tracking well against the requirement, delivering significant capacity growth on both the Sydney-Shanghai and Melbourne-Shanghai routes as shown in Table 2 below. In addition, taken alone, China Eastern may meet the CAGR estimate on some specific routes (depending, again, on further changes currently being considered as result of the most recent Government announcements). However, in any event, the alliance's total 5 year estimated CAGR across all routes, will not meet the 4% requirement.

**Table 2: Qantas and China Eastern CAGR on Australia-Shanghai Routes**

Carrier/City Pair	Nov 14 - Oct 15	Nov 15 - Oct 16	Nov 16 - Oct 17	Nov 17 - Oct 18	Nov 18 - Oct 19	Nov 19 - Oct 20 (forecast)	5 year CAGR (estimate)
<b>China Eastern</b>	<b>448,115</b>	<b>564,367</b>	<b>538,802</b>	<b>549,714</b>	<b>645,650</b>	<b>576,805</b>	<b>5.18%</b>
Sydney-Shanghai	210,149	273,673	264,902	275,606	310,972	290,238	6.67%
Melbourne-Shanghai	209,760	255,416	273,900	269,468	318,548	286,567	6.44%
Cairns-Shanghai	28,206	35,278	-	4,640	16,130		-100.00%
<b>Qantas</b>	<b>209,809</b>	<b>208,634</b>	<b>210,466</b>	<b>208,182</b>	<b>190,448</b>	<b>96,414</b>	<b>-14.40%</b>
Sydney-Shanghai	209,809	208,634	210,466	208,182	190,448	96,414	-14.40%
<b>Total Alliance</b>	<b>657,924</b>	<b>773,001</b>	<b>749,268</b>	<b>757,896</b>	<b>836,098</b>	<b>673,219</b>	<b>0.46%</b>

Source: BITRE data available for the period November 2014-December 2019.  
[https://www.bitre.gov.au/publications/ongoing/international\\_airlines-operated\\_flights\\_seats](https://www.bitre.gov.au/publications/ongoing/international_airlines-operated_flights_seats)  
 DiiO MI/OAG published schedule information for the period January 2020-October 2020

Even assuming that Qantas is able to reinstate services to Shanghai in mid July 2020 and that China Eastern will be able to continue flying certain services and resume other services to Shanghai throughout April-October 2020, the resumed schedule is not yet finalised and, as flagged above, will continue to depend on how the current crisis evolves day to day. As mentioned earlier, China Eastern is already determining whether to revise its schedule in light of the Australian and Chinese Government's most recent announcements. In any event, if demand does not sufficiently recover even once all relevant Government restrictions have been lifted, it is likely that there will be further adjustments and flight cancellations in the coming months beyond July.

Accordingly, in order to maximise operational flexibility during the current crisis, the Applicants seek a variation of the Conditions of Authorisation such that clause 1(d) is either:

- removed in its entirety; or
- expressed to be a requirement to achieve a 4% CAGR on Australia-Shanghai Routes measured at four years into the Term (i.e. measured on a rolling basis from November 2015 until October 2019).

#### **Variations Sought In Respect of Audit Requirements**

In addition, the Applicants apply for a variation in respect of clause 6.6(a) of the Conditions of Authorisation, which requires that *'the Approved Independent Auditor must within three months of the end of a Scheduling Season, provide to the ACCC a written Audit Report as set out in clauses 6.6(b) and (c) in relation to the Applicant's compliance with its obligations under clause 1.'*

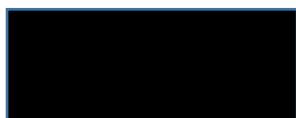
As the Commission is aware, the Applicants' appointed auditor is BDO. On 19 March 2020, BDO advised that it will be unable to complete the audit that is required to be submitted to the Commission in June 2020 in respect of the Northern Winter 2019 Scheduling Season. This is because completion of the audit requires travel by its representatives to Shanghai to conduct reviews and interviews with China Eastern staff. It is also anticipated that there may be other practical difficulties in completing the audit given the need for access to both airlines' staff and resources in the coming months.

Accordingly, the Applicants request that the Conditions of Authorisation are varied to:

- defer the date for submission of a written audit report in respect of the Northern Winter 2019 Scheduling Season until, at this stage, 1 November 2020. Further to the above request in respect of the CAGR requirement in clause 1(d), the Applicants request that the compliance with the CAGR requirement as varied be included in this report; and
- waive the requirement for submission of a written audit report in respect of the Northern Summer 2020 Scheduling Season.

Please let us know if you have any questions or require further information to assess this application.

Yours sincerely,



Michele Laidlaw  
Head of Legal – Competition  
Qantas Airways Limited