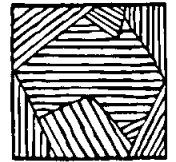


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A·F·T·A
THE AUSTRALIAN
FEDERATION
OF TRAVEL AGENTS
LIMITED

ABN 72 001 444 275

06 June 2003

FILE No:
DOC:
MARS/PRISM:

Mr Tim Grimwade
General Manager
Adjudication Branch
Australian Competition and Consumer Commission
PO Box 1199
DICKSON ACT 2602

BY FACSIMILE: (02) 6243 1211

BY EMAIL: adjudication@accc.gov.au

Dear Sir,

Authorisation Applications lodged by Qantas Airways Limited and British Airways Plc (A30226 and A30227)

I refer to your letter of 12 May 2003 advising that the Australian Competition and Consumer Commission (the Commission) has received the above applications for reauthorisation of a "Restated Joint Services Agreement" (JSA) and inviting written submissions regarding the likely public benefits and affect on competition of the arrangements for which reauthorisation is sought.

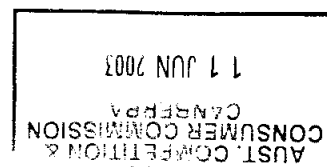
AFTA supports the applications subject to certain reservations which are set out in the following submissions.

The Applications

Qantas Airways Limited (Qantas) and British Airways Plc (British Airways) are parties to the JSA which provides for coordination of air services and business activities on routes between Australia and Europe and intermediate points (the Kangaroo Route). The original JSA received authorisation from the Trade Practices Commission (as it was then) in 1995 and from the Commission in 2000.

Duration of Reauthorisation

The applicants apply for an unconditional reauthorisation of indefinite duration. AFTA does not believe it in the public interest that there be an authorisation of an indefinite period.



Whilst noting that an authorisation is subject to review at any time if there is a material change in circumstances including changes in markets, AFTA submits the reauthorisation should be for a fixed period and in this regard 5 years would be appropriate.

As the Commission will be aware the aviation industry is highly volatile and subject to competitive pressures. AFTA believes that the public benefits cited by the applicants (and with which AFTA is in general agreement) can be maintained even if the reauthorisation is for a specific period.

The investments to which the applicants refer¹ are those which would be expected of an international airline and would not be curtailed by having an authorisation for a fixed period. For example the applicants state that Qantas intends to introduce the larger A380 on the Kangaroo Route in 2006. That investment decision has been taken in the context of an authorisation that expires in 2003. A reauthorisation of 5 years (to 2008) would not have a negative impact on decisions such as these.

Conditions of Authorisation

AFTA believes that it is appropriate that the Commission does not impose conditions on the authorisation. However AFTA believes the Commission should consider a review of the authorisation in the event that:

- (i) There is a significant reduction in the number of economy class seats offered by the applicants on the Kangaroo Route.
- (ii) There is a significant reduction in the weekly frequency of flights operated by the applicants on the Kangaroo Route.
- (iii) There is a significant reduction in city pairs serviced on the Kangaroo Route by the applicants.

Public Benefits

The Kangaroo Route

AFTA agrees with the applicants' assessment of the challenges facing end point carriers on the Kangaroo Route and the advantages geography grants to 6th freedom carriers.

AFTA has noted with concern the disappearance in recent years of a number of European carriers from the Kangaroo Route including major airlines such as Air France, Lufthansa, KLM, Alitalia and Olympic Airways and the consequential loss of choice to the public. As the applicants note, today there are only two European carriers on the Kangaroo Route being British Airways and Lauda/Austrian.

AFTA would be concerned if Qantas and British Airways could not sustain its current flight schedules both in terms of frequency and city pairs. In AFTA's opinion the reauthorisation of the JSA is only one of many factors the applicants would take into account regarding their ability to maintain and possibly expand their range of frequencies and capacity and it is more than likely that such changes would be dependant upon competition within the relevant markets.

Product and Services Benefits

AFTA believes that the JSA has allowed the applicants to offer a broader choice of schedules, more flexible fares, a greater range of product (fare types) and higher levels of consumer support.

Lower Fares

AFTA agrees with applicants' assertions that the JSA is likely to result in greater availability of discount fares to consumers as a result of higher levels of capacity. The setting of fare levels is a complex task. The applicants now operate sophisticated systems to monitor yield and capacity which has lead to a range of discount fare initiatives during the life of the JSA.

¹ Network Economics consulting Group Pty Ltd (NECG) report page 16.

Higher Levels of Tourism

Whilst AFTA does not comment on the quantification prepared by NECG of the possible lost tourism if the JSA is not reauthorised AFTA agrees with the applicants that the operation by Qantas of the JSA routes means that tourist visits to Australia are likely to be higher with the JSA than without it.

Anti-Competitive Effects and Public Detriment

AFTA agrees with the applicants' market definitions as set out in section 5 of the applicants' submission and section 4 of the NECG Report.

AFTA also agrees that it is relevant that the Commission consider the market for travel agency services². AFTA does not believe the JSA lessens competition in this market. However AFTA would be concerned if the applicants jointly and under the guise of the reauthorisation attempted to reduce commissions payable to travel agents.

The Commission has previously been made aware of AFTA's concerns regarding airlines' ability to control income to agents³. AFTA's view is that contrary to the assertions made in the NECG Report a joint reduction in commission would harm travel agents as:

- (i) Qantas, being Australia's only international carrier, accounts for a significant proportion of sales in the relevant markets.
- (ii) The products/service offered by 2nd freedom carriers (Qantas and British Airways) is superior to 5th and 6th freedom carriers in terms of frequency, length of trip (especially to Europe), availability and consumer support and this is reflected in consumer choice.

² NECG Report page 51.

³ AFTA's submission to the Commission in respect of Authorisation A90791, IATA Passenger Agency Programme.

- (iii) Alternative sources of income such as service fees cannot be guaranteed due in part to the fact that this is currently untested and is likely to attract consumer resistance.

AFTA submits that there is a likelihood that competition in the market for travel agency services would be lessened in the event Qantas and British Airways combined their commission programmes on the JSA routes.

The Australian Domestic Market

AFTA agrees with the applicants that the JSA does not lessen competition in the market for the provision of domestic air services. The applicants however point to the start up success of Virgin Blue as evidence in support of this. In AFTA's view Virgin Blue has benefited from the demise of Ansett and its business plan to position the airline as a low cost (value based) carrier offering a limited range of services in opposition to Qantas which operates as a full service airline.

Product Markets: Air Passenger Services

AFTA does not accept the applicants' assertions that there is a single product market for air passenger services with no relevant distinction between business and leisure passengers.

AFTA submits that there are separate markets for different classes of travel or passenger types.

AFTA agrees with the Commission's view on the product market expressed in Determination A30202. In AFTA's experience there is little or no substitutability between economy and premium class air tickets. This view is supported by the following:

- (i) Price bands.

Each class of travel operates in clear and non-contiguous price bands.

(ii) Passenger Composition.

In AFTA's experience premium class passengers are predominantly travelling on business (and therefore the cost of the travel is not born by the individual) or beneficiaries of frequent flyer/loyalty programs, whereas economy class passengers predominantly self fund their purchase.

(iii) Product Differentiation

Airlines offer clear and distinct product within the cabin. What is offered to economy travellers is vastly different to the premium class product. There is clearly no substitutability between even economy and business class travel. The airlines market each class quite separately. Further, the structure of fares offered by airlines is an acknowledgement of the product differentiation: for example economy class fares are offered on a seasonal basis, a differentiation which does not apply to business or first class fares.

In AFTA's experience whilst there has been a downward trend in the price of economy travel on the relevant routes during the term of the JSA the cost of premium class tickets has in fact risen considerably both in dollar and real terms. Further, the evidence contained in the NECG Report regarding yield and inventory management supports the view that there is very clearly separate markets for business and leisure travel.

Barriers to Entry

AFTA agrees with the comments of the applicants and the NECG conclusions that while there are possible barriers to entry for end point carriers there is unlikely to be any material constraint on further expansion by mid point carriers. The reasoning for these conclusions are set out in some detail in the NECG Report.

Competition in the Australian Domestic Market

AFTA does not believe reauthorisation of the JSA is likely to impact on competition in the Australian domestic market. Apart from Qantas, Virgin Blue is the only domestic carrier to operate nationally. As a result of the demise of Ansett, Virgin has been able to capture

approximately 30% of the domestic market. Virgin has shown itself to be adapt at negotiating agreements to secure international passengers.

AFTA does not believe reauthorisation of the JSA would have a significant impact on the ability of airlines to enter the domestic market. In AFTA's opinion there is little likelihood in the immediate future for any new entrant into the domestic market for a host of commercial reasons including the need for significant capital, investment start up costs and the general size of the Australian domestic market.

Market Power

The NECG Report sets out in some detail market share data for the Australian-Europe and Australian –South East Asian Routes⁴. With exception of Australia-Italy there has been a reduction in the applicants' market share on these routes, with a slight increase on the London-Sydney and London-Melbourne routes. In AFTA's opinion this data supports the view that whilst Qantas and British Airways have a marketing advantage over the 5th and 6th freedom carriers (in being able to offer a one plane service with the fastest travel time) this does not translate into a significant degree of market power.

AFTA believes that reauthorisation by the Commission would not significantly increase the applicants' market power. AFTA's only concern is set out above in respect of the potential power the applicants may have in the market for travel agencies services and the potential for the exercise of that power against travel agents by the applicants jointly determining commissions.

AFTA has previously submitted to the Commission ⁵that a condition precedent to authorisation of the Restated JSA should be that authorisation be subject to review if Qantas and British Airways independently or together attempt to reduce commission payable to Australian agents or use their market power to influence consumers to purchase directly from the airlines. AFTAs does not seek any condition precedent of the authorisation the subject of the applications however it does submit that the JSA has the potential to lessen competition in

⁴ Tables 7 to 27 pages 58 to 74.

⁵ AFTA submission to the Commission in respect of Authorisation A30202.

the market for travel agency services in the event there is any further contraction in the number of carriers servicing Australian-Europe city pairs.

Conclusion

Whilst the JSA has the potential to have an effect on competition this is out weighed by the number of public benefits which will be provided, in particular relating to flight frequency, the number of European destinations serviced and capacity.

AFTA submits that the reauthorisation should not be for an indefinite period but for a limited time and suggests 5 years would be suitable.

Yours faithfully

A handwritten signature in black ink, appearing to read "Mike Hatton", with a long, sweeping flourish extending to the right.

Mike Hatton
Chief Executive