

6.8 . Should the public benefits or expected public benefits outweigh the anti-competitive aspects, the Commission may grant authorisation, or grant authorisation subject to conditions.

7 Commission Evaluation – Market definition

- 7.1 The Commission's evaluation of the applications is in accordance with the statutory test outlined in section 6 of this determination. As required by the test, it is necessary for the Commission to assess the likely benefit and detriment, including the effects on competition, resulting from the proposed arrangements.

Defining markets

- 7.2 Public benefits and, more pertinently, anti-competitive detriments arising from the proposed arrangements sought to be authorised are assessed in the context of a market. In assessing an application for authorisation and applying the relevant public benefit test, the Commission is not required to form a view as to whether the conduct is likely to breach the Act.⁹ Therefore, in an authorisation context, it is only necessary to delineate the relevant market(s) to the extent needed to assess the public benefits and detriments of the proposed arrangements. However, depending on the circumstances, the Commission may not need to comprehensively define the relevant markets as it may be apparent that a net public benefit will or will not arise regardless of this definition.
- 7.3 Section 4E of the Act states that a market for goods or services includes other goods or services that are substitutable for, or otherwise competitive with, the first goods or services.¹⁰ The courts have established that both demand and supply side substitution must be taken into account in determining the relevant market. *QCMA*¹¹ is often cited when seeking to explain how markets are defined:

A market is the area of close competition between firms or, putting it a little differently, the field of rivalry between them... Within the bounds of a market there is substitution between one product and another and between one source of supply and another, in response to changing prices. So a market is the field of actual and potential transactions between buyers and sellers amongst whom there can be strong substitution, at least in the long run, if given a sufficient price incentive... Whether such substitution is feasible or likely depends ultimately on customer attitudes, technology, distance and cost and price incentives.

It is the possibilities of such substitution which set the limits upon a firm's ability to 'give less and charge more'. Accordingly, in determining the outer boundaries of the market we ask a quite simple but fundamental question: If the firm were to 'give less and charge more' would there be, to put the matter colloquially, much of a reaction?

- 7.4 In establishing market boundaries, the Commission seeks to include all those sources of closely substitutable products, to which consumers would turn in the

⁹ *Re Concrete Carters Association (Vic) (1977) 31 FLR 193.*

¹⁰ The Commission identifies the relevant market by determining the smallest area over which a profit maximising monopolist would impose a "small but significant and non-transitory increase in price" (SSNIP), or equivalent exercise of market power. By including all substitution possibilities, the process of market definition identifies all the sources of competition that effectively constrain the price and output decisions of the relevant entities. Market definition is not an end in itself but rather a tool of analysis. The market must be defined only to the extent necessary to determine the effect of the proposed conduct on competition.

¹¹ *Re Queensland Co-op Milling Association Ltd & Defiance Holdings Ltd (1976) ATPR 40-012.*

event that the firm attempted to exercise market power. The Commission looks at both the demand and supply side of the market and defines up to four different dimensions:

- geographic market – which may be local, state, national or international depending on where trade occurs;
- product market – based on whether products are close substitutes for one another;
- functional market – defines at what level the conduct in question occurs, e.g. retail or wholesale; and
- temporal market – what period of time does the analysis apply to? The next two years? The next ten?

7.5 If market boundaries are too narrow so that actual or potential sources of competition are excluded then the proposed conduct will appear to have greater anti-competitive effect than is actually the case. On the other hand, the market may be defined too widely to include products or geographic areas that are not close substitutes. In such circumstances the anti-competitive effects of the proposed conduct will appear to be weaker than they actually are.

Previously stated views of the Commission in respect of air transport sector markets

7.6 The Commission has previously expressed views on markets relevant to air transport in the:

- Determination concerning an alliance agreement between Ansett Australia, Ansett International, Air NZ and Singapore Airlines of 22 July 1998 (A90649 and A90655) (the Ansett alliance determination);
- Determination concerning the Restated Joint Services Agreement (RJSA) between Qantas and BA of 10 May 2000 (A30202) (the Qantas/BA RJSA determination);
- Determination concerning the IATA Passenger Agency Program of 13 November 2002 (A90791) (the IPAP determination); and
- Draft determination concerning the acquisition by Qantas of ordinary shares in Air NZ and cooperative arrangements between Qantas, Air NZ and Air Pacific Limited of 10 April 2003 (A30220, A30221, A30222, A90862 and A90863) (the Qantas/Air NZ draft determination).

7.7 In these determinations the Commission generally concluded that there were three broad markets of relevance to air transport:

- passenger transport;
- freight; and
- sale of air travel.

7.8 Of these three markets, only the markets for passenger transport and sale of air travel are relevant to the analysis of the applications lodged by the Applicant.

Passenger transport

- 7.9 The Commission has consistently stated that the most important dimensions of the passenger transport market are the geographic and product dimensions.

Geographic market

- 7.10 The Commission has previously distinguished between the domestic and international markets primarily on the basis of the different regulatory environments.

Domestic

- 7.11 An important element of the regulatory distinction is cabotage policy which restricts the carriage of passengers between points in Australia to domestic airlines. Government specified ownership restrictions effectively prevent foreign international carriers from operating on Australian domestic routes. Foreign persons, including foreign airlines, are allowed to have up to 100 per cent of equity in an Australian domestic airline, unless this is contrary to the public interest. While a foreign airline is prevented under cabotage from carrying domestic passengers in Australia, it can operate a wholly owned subsidiary in the domestic passenger transport market.
- 7.12 The Commission has previously noted that, while foreign carriers were prevented from operating in the Australian domestic passenger transport market they could have a presence through code sharing, with the Government allowing foreign carriers to code share to all points in Australia on Australian domestic airlines. This policy only relates to international passengers continuing their international voyages beyond their point of entry into Australia. However it does result in domestic flights carrying a mixture of international travelling passengers and domestic passengers. It also encourages linkages between international carriers and domestic carriers meaning that alliances between Australian and foreign carriers on international routes can impact on the performance of the Australian domestic passenger transport market.
- 7.13 Following the failure of Ansett in September 2001 the Government temporarily relaxed cabotage policy as a means of achieving greater balance between supply and demand on trunk routes. United Airlines, for example, was allowed to utilise surplus capacity to carry domestic passengers between Sydney and Melbourne.

International

- 7.14 When examining the international passenger transport market, the Commission has consistently stated that, after taking into account opportunities for indirect travel, a regional approach to market definition is generally the most appropriate. However, this does not preclude the Commission from adopting a different market definition, including a point-to-point market, depending on the circumstances of the conduct at issue.

Product market

- 7.15 In the Qantas/BA RJSA determination, the Commission explored the possibility that there could be separate markets for economy and premium class passengers. After further consideration, in the Qantas/Air NZ draft determination the Commission formed the view that, if there are different product markets for passengers, it is more likely to be based on whether travellers are travelling for the purpose of leisure or business, than on the class of ticket purchased. In the Qantas/Air NZ draft determination the Commission stated that it is increasingly of the view that there are separate markets for business and leisure travellers.

Sale of air travel

- 7.16 While the Commission has generally identified the sale of air travel market as one of the markets relevant to the air transport of passengers, in the IPAP determination it recognised that this market should embrace not only those organisations able to sell tickets directly to the public (airlines and IATA accredited agents), but also licensed agents which are not IATA accredited.

Geographic market

- 7.17 In the past, the Commission has formed the view that the geographic market for the sale of air travel (in both international and domestic trades to consumers located in Australia) has tended to be the whole of Australia, but not outside Australia.
- 7.18 However in the IPAP determination the Commission recognised that with the development of internet web sales sites by both agents and airlines the geographic dimension of the air travel market boundary is becoming increasingly blurred. Visitors to Australia for example can book internal travel in Australia in advance over the internet to access heavily discounted domestic fares. Similarly industry portals being developed such as Zuji are accessible by consumers from any country and provide an ability to purchase travel across a wide range of airlines and international and domestic routes. In effect, the Commission broadened its previously held view of the market to include not only the sale of air travel in Australia but also the sale of travel to and from Australia.

Product market

- 7.19 In the IPAP determination the Commission re-affirmed its belief that the product market in ticket sales includes tickets sold directly by airlines to travellers as well as those sold through indirect channels (for example, travel agents).
- 7.20 The Commission considered that airlines are active retailers in both the domestic and international travel markets and are increasingly promoting sales of their own products both through internet sales and through aggressive press advertising. The Commission has expressed the view that tickets sold by airlines are an important part of the sale of air travel product market.

- 7.21 As indicated above the Commission has previously indicated that it cannot be assumed that a single market exists for both leisure and business passenger transport. A corollary of this view is that there could similarly be separate markets for the sale of air travel to leisure and business travellers. Certainly there are agencies who specialise in corporate travel and comments have been made to the Commission that airlines actively pursue such customers and corporate accounts because of the higher revenue they generate and the repeat business they bring.

Functional market

- 7.22 The Commission is not aware of any changes in the distribution chain for airline tickets. In the absence of comments from the Applicant and interested parties, the Commission will therefore assess the applications on the basis that consumers can purchase tickets from any segment of the distribution system, including retail travel agents, airlines and package tour operators (wholesalers). The Commission continues to see consolidators as an integral part of this distribution system.
- 7.23 It is noted that airlines fill the role of wholesalers to the travel agent industry for air travel as well as retailing air travel in their own right.

Market shares

- 7.24 In the IPAP determination the Commission indicated that it could be expected that in 2002 airlines had around 20 per cent of the retail market for international fares in Australia and travel agents 80 per cent. The domestic sale of air travel market was noted to be structured differently to the international sale of air travel market with a heavier emphasis on direct sales by airlines through call centres and web sites. Industry estimates suggested that in Australia about 50 per cent of domestic air travel sales are made directly through airlines and 50 per cent through agents.

The Applicant's submission on market definition

- 7.25 In its submissions, the Applicant's views on market definition are based on the views expressed by the Commission in the Qantas/BA RJSA determination. In summary, the Applicant considers there are regional markets for air passenger transport, with the relevant regional markets being:
- between Australia and South East Asia;
 - between Australia and Europe;
 - between Australia and New Zealand/Oceania;
 - between Australia and North Asia
 - between Australia and India/Middle East;
 - between Australia and North/South America.¹²

¹² In the Qantas/BA RJSA determination, the Commission also identified a regional market between Australia and Africa which the Applicant has not included in its submission.

7.26 The Applicant notes the Commission's view that the regional market approach is not necessarily the most suitable for analysis of direct routes, such as those to Japan, Singapore, Hong Kong, Indonesia and New Zealand.

7.27 The Applicant also notes that in the Qantas/BA RJSA determination, the Commission suggests a distinction between air passenger transport markets for economy and premium class passengers, although the Applicant does not agree with this view.¹³

Interested parties' submissions on market definition

Australian Federation of Travel Agents

7.28 AFTA submits that the two relevant markets are:

- the provision of passenger airline services to and from Australia; and
- the retailing of passenger air travel both to and from Australia and within.

7.29 AFTA is of the view that the regional approach to market definition adopted by the Commission in the IPAP determination should not apply to the current applications.

Qantas

7.30 In response to the Commission's draft determination, Qantas submitted that:

- there is in practice a high degree of substitutability on the demand side between different fare classes and therefore it is not possible to delineate between 'business' fare classes and 'non-business' fare classes; and
- there is almost perfect supply side substitutability between different classes of airline travel.

7.31 Qantas therefore believes that all classes of fare must be considered to form one product market

The Commission's views on market definition in respect of the current applications for authorisation

Passenger transport

Geographic market

7.32 No information has been provided to the Commission which suggests that it should depart from its view of the geographic markets for passenger transport as expressed in Qantas/BA RJSA determination. While AFTA has suggested that the regional approach should be disregarded for the purposes of assessing the applications, such

¹³ As discussed in paragraph 7.15, the Commission has since moved away from this view and now considers that if there are different product markets for passengers, the distinction is more likely to be based on purpose of travel (leisure or business) rather than the class of ticket purchased.

an approach would disregard variations in the strengths of alliances across different regions and the varying contributions individual regions make to the Australian economy.

Product markets

7.33 As discussed above, the Commission has previously held the view that it cannot be assumed that a single air transport markets exists for both business and leisure travellers. The Commission considers that there can be different demand elasticities for different types of travellers. Demand by a business traveller is relatively price inelastic compared, for example, with demand by leisure travellers.

7.34 In the Qantas/Air NZ draft determination, the Commission noted that it may be argued that airlines have already recognised the distinction between leisure travellers and business travellers in the way that fares and conditions of travel are structured. The typical business traveller requires flexibility, short stay, and short lead booking times. Premium class and full economy fares satisfy all these requirements, but at a relatively fixed price. Leisure travellers typically use discount economy class fares restricted by conditions such as advance purchase, no flexibility and no refunds. These conditions effectively deny access to the business traveller to those lower fares. Even if the business traveller can plan a trip in advance to meet these requirements, minimum stopover conditions will generally rule out that fare.

7.35 The distinction between business travellers and leisure travellers is also becoming evident in the way that airlines structure their operations. For example, the Applicant has launched Express Class in recognition of the business travellers and in a press release of 15 October 2002 announcing the launch stated:

“Specifically the new system of one-way pricing allow more pricing flexibility than ever before as New Zealand’s business travellers can now mix and match fare types and get a ‘combo’ return fare to best match their needs at the start or end of a work trip as the demands of business can be unpredictable.”

7.36 Figures derived from Table 7.1 below show that overseas travel by Australian residents for the purpose of business grew 2.5 per cent between 2001 and 2002 but remained constant as a proportion of all travel at 16.3 per cent.

Table 7.1 International air passenger travel, short term departures by Australian residents for the purpose of business, years 2001 and 2002

| Airline | Purpose of travel | | | |
|-------------------------|-------------------|----------------|------------------|------------------|
| | Business | | All purposes | |
| | 2001 | 2002 | 2001 | 2002 |
| oneworld | | | | |
| Qantas | 246 636 | 271 876 | 1 178 601 | 1 256 891 |
| British Airways | 15 620 | 18 993 | 76 347 | 89 973 |
| Cathay Pacific | 30 007 | 36 573 | 119 770 | 138 073 |
| <i>Total</i> | <i>292 263</i> | <i>327 442</i> | <i>1 374 718</i> | <i>1 484 937</i> |
| Star Alliance | | | | |
| Air NZ | 54 280 | 33 312 | 303 644 | 242 079 |
| Ansett | 10 118 | -- | 68 501 | -- |
| Lauda | 2 115 | 2 335 | 34 332 | 37 507 |
| Singapore Airlines | 68 889 | 70 888 | 393 761 | 417 811 |
| Thai International | 13 729 | 14 001 | 159 707 | 160 014 |
| United Airlines | 18 324 | 15 325 | 109 083 | 74 258 |
| Air Canada | 1 433 | 2 249 | 33 418 | 40 625 |
| <i>Total</i> | <i>168 888</i> | <i>138 110</i> | <i>1 102 446</i> | <i>972 294</i> |
| All airlines | 536 511 | 550 064 | 3 293 034 | 3 369 649 |
| Growth from 2001 | -- | + 2.5 % | -- | + 2.3% |
| % of all travel | 16.3% | 16.3% | -- | -- |

Source: Australian Bureau of Statistics

- 7.37 While the incident of travel remained relatively constant there were significant changes in the shares of business travel achieved by individual airlines. Overall the number of Australian resident business travellers carried by Star Alliance members fell by 18.2 per cent while the number of equivalent passengers carried by the **oneworld** alliance rose by 12.0 per cent. Reflecting these movements, the Star Alliance share of the Australian resident business travel fell from 31.5 per cent to 25.1 per cent. At the same time the **oneworld** share rose from 54.5 per cent to 59.5 per cent.
- 7.38 All **oneworld** carriers experienced significant increases in the number of Australian business travellers they carried between 2001 and 2002 (Qantas plus 10.2 per cent, BA plus 21.6 per cent and Cathay Pacific plus 21.9 per cent). Star Alliance carriers with a multiple Australian airport presence such as Singapore Airlines (plus 2.9 per cent) and Thai International (plus 2.0 per cent) maintained their positions. Star Alliance carriers with less of a presence, Air NZ (minus 38.6 per cent) and United Airlines (minus 16.4 per cent), did not fare as well.
- 7.39 The failure of Ansett Australia has left Star Alliance carriers without an aligned carrier in the Australian domestic passenger transport market. United Airlines indicated in a submission to the Commission during public consultation prior to the release of the Qantas/Air NZ draft determination that it was significantly disadvantaged by the loss of Ansett. The disadvantages included the loss of code share access to seven cities, inferior prorates with Qantas for domestic services compared to other international airlines and problems with access to Qantas domestic inventory. United Airlines stated that it had experienced a significant decline in market share and revenue in several Australia - United States city pairs as a result of losing Ansett's passenger feed.

- 7.40 Given that business travellers would normally be expected to pay higher fares and higher yielding fares the impact of the loss of business custom could be expected to impact on the Star Alliance carriers in proportions greater than reflected by movements in numbers of passengers carried. United Airlines has stated for example that while it succeeded in back filling the seats vacated by lost Ansett connections it did so with lower paying passengers with the average fare for a connecting passenger declining 12 per cent between 1999 and 2002.
- 7.41 An analysis of figures appearing in Table 7.2 below shows that overseas travel by Australian residents to attend conventions grew by 1.2 per cent between 2001 and 2002 but remained constant as a proportion of all travel at 4.0 per cent.

Table 7.2 International air passenger travel, short term departures by Australian residents for the purpose of conventions, years 2001 and 2002

| Airline | Purpose of travel | | | |
|-------------------------|-------------------|----------------|------------------|------------------|
| | Conventions | | All purposes | |
| | 2001 | 2002 | 2001 | 2002 |
| oneworld | | | | |
| Qantas | 57 673 | 70 512 | 1 178 601 | 1 256 891 |
| British Airways | 3 609 | 5 215 | 76 347 | 89 973 |
| Cathay Pacific | 4 076 | 3 917 | 119 770 | 138 073 |
| <i>Total</i> | <i>65 358</i> | <i>79 644</i> | <i>1 374 718</i> | <i>1 484 937</i> |
| Star Alliance | | | | |
| Air NZ | 13 304 | 7 153 | 303 644 | 242 079 |
| Ansett | 2 294 | -- | 68 501 | -- |
| Lauda | 587 | 699 | 34 332 | 37 507 |
| Singapore Airlines | 15 385 | 11 424 | 393 761 | 417 811 |
| Thai International | 4 309 | 4 962 | 159 707 | 160 014 |
| United Airlines | 10 469 | 7 275 | 109 083 | 74 258 |
| Air Canada | 1 354 | 1 763 | 33 418 | 40 625 |
| <i>Total</i> | <i>47 702</i> | <i>33 276</i> | <i>1 102 446</i> | <i>972 294</i> |
| All airlines | 131 691 | 133 313 | 3 293 034 | 3 369 649 |
| Growth from 2001 | -- | + 1.2 % | -- | + 2.3% |
| % of all travel | 4.0% | 4.0% | -- | -- |

Source: Australian Bureau of Statistics

- 7.42 In the same period the number of residents attending conventions carried by oneworld airlines rose by 21.9 per cent while the number of equivalent passengers carried by the Star Alliance fell by 30.2 per cent.
- 7.43 At the airline level, two of the three oneworld carriers operating to Australia increased the number of resident convention travellers they carried between 2001 and 2002 (Qantas plus 22.2 per cent and BA plus 44.5 per cent), while Cathay Pacific experienced a small decrease in such travellers (minus 3.9 per cent).
- 7.44 Most of the major Star Alliance carriers visiting Australia suffered a substantial decrease in Australian resident convention traffic between 2001 and 2002 (Air NZ minus 46.2 per cent, Singapore Airlines minus 25.7 per cent, and United Airlines minus 30.5 per cent). Thai International experienced an increase (plus 15.1 per cent).

7.45 There is a clear difference in the volume of travel undertaken for business purposes compared with the volume of travel undertaken in order to attend a convention. Additionally, there would appear to be a distinction between the demand characteristics of convention delegates and business travellers. This distinction stems from the likelihood that convention delegates have considerable advance notice of their overseas travel requirements whereas corporate travellers are often required to travel at short notice. As a result of this difference, the types of tickets purchased by convention delegates and business travellers are likely to differ. Convention delegates are able to purchase APEX fares which enable overseas travel at a discounted price relative to full fares. In contrast, business travellers are generally not able to purchase APEX fares and thus purchase full fares. Additionally, business travellers are more likely to travel in premium class than convention delegates, who may be required to meet their own travel costs when attending a convention in a personal capacity.

7.46 As a result of the above deliberation, and taking into account factors raised in the Qantas/BA JSA determination such as the effect of loyalty programs, corporate travel contracts and the existence of a highly specialised business travel agency industry, the Commission is increasingly of the view that there may be separate markets for business and leisure travellers in the context of assessing the effect on competition of promotions directed to business travellers. However, in the circumstances at hand, it is not necessary to make such a distinction because the outcome of the current authorisation applications is not dependent on whether a single market, or separate markets, are defined.

7.47 In this context, the Commission does not consider there is a separate market for convention travellers, which only account for around 4% of resident travel, and notes that convention delegates appear to exhibit many of the demand characteristics of leisure travellers, rather than business travellers. That said, the Commission acknowledges that many convention travellers will be travelling at company expense.

Sale of air travel

7.48 No information has been provided to the Commission which suggests that it should depart from its view of the sale of air travel markets as expressed in the IPAP determination. The appropriate market would appear to be for the retailing of passenger air travel both to and from Australia and within Australia. The Commission notes that the broader geographic element of this market, to include air travel to and from Australia, is particularly relevant to its assessment of the current applications, in which the conduct the subject of the applications is likely to affect travellers not only within Australia, but also travellers to and from Australia.

7.49 The Commission notes that the presence of dedicated business travel agencies raises the possibility of a distinct market for the retailing of business passenger air travel.

Convention services

- 7.50 In addition to the above markets relating to air travel, the Commission has identified a further related and relevant area of competition associated with the global supply of convention services by convention organisers - that is, competition between convention organisers in the provision of services to sponsoring organisations or committees and delegates.
- 7.51 The Commission notes the submission from BIC which outlines that currently, most major international conventions and tradeshow events are put out to tender. Professional convention organisers compete against each other with bids to the sponsoring organisation or committee for the right to be appointed as the official convention organiser for the convention or event.
- 7.52 On the basis of the information available to the Commission, it would appear that convention hosts compete with one another on a global basis in the provision of convention services to organisations/delegates. In other words, when the organiser of a large convention is looking for a suitable venue, their search is not limited to venues within their home country, particularly if the convention is likely to involve international delegates. Thus the market for the supply of convention services would appear to be a global market. However, it is not necessary for the Commission to comprehensively define the relevant market(s) because in this instance, market definition will not affect the outcome of the authorisation applications.

8 Commission Evaluation – The future without authorisation

- 8.1 The Commission's evaluation is in accordance with the statutory tests outlined in section 6 of this determination. As required by the test, it is necessary for the Commission to assess and weigh the likely public benefits and detriments flowing from the proposed arrangements.
- 8.2 The Commission also uses the "future with-and-without test" established by the Australian Competition Tribunal to identify and measure the public benefit and anti-competitive detriment generated by the arrangements proposed to be authorised.¹⁴
- 8.3 Under this test, the Commission compares the public benefit and anti-competitive detriment generated by the arrangements in the future if the authorisation is granted with those generated if the authorisation is not granted. This requires the Commission to form a view as to the future state of the relevant markets assuming authorisation is not granted. This view is often referred to as the counterfactual.
- 8.4 The counterfactual provides the benchmark against which anti-competitive detriment and public benefits are assessed. In examining prices to consumers associated with specific conduct, for example, the Commission would expect to compare estimates of prices under the proposed arrangements with prices under the base position (the counterfactual).
- 8.5 It can be seen that the state of the market selected as the counterfactual can be critical in terms of determining net public benefit. In the majority of authorisation cases coming before the Commission, the counterfactual is represented by the status quo. However, this need not necessarily be the case and depends on likely or imminent developments in the markets concerned.
- 8.6 No submissions were received from either the Applicant or interested parties in respect of the likely future situation without authorisation.
- 8.7 In respect of the Corporate Agreement, it appears to the Commission that the future without authorisation is likely to be the status quo. The Commission understands that the Corporate Agreement is yet to be launched globally. In the absence of authorisation, the Commission considers that the Corporate Agreement is unlikely to be launched such that Australian markets are affected. However, the Commission notes that the launch of the Corporate Agreement, in the absence of authorisation, is unlikely to have a significant impact on the relevant Australian markets due to the absence of a Star Alliance member airline operating domestically in Australia.
- 8.8 In respect of the Conventions Program, it appears to the Commission that the future without authorisation is likely to be the status quo. While the Conventions Program may be in operation outside Australia, in the absence of authorisation, it is unlikely that the Conventions Program would be implemented for airlines doing business in Australia or that travellers to or from Australia could obtain discounts on airfares.

¹⁴ See, for example, *Re Australasian Performing Rights Association* (1999) ATPR 41-701.

9 Commission Evaluation – Corporate Agreement

Effect on competition

- 9.1 As discussed at section 6, the Commission must assess the extent to which the proposed arrangements give rise to detriment to the public as a result of any lessening of competition that flows from the proposed arrangements.
- 9.2 In summary, the provisions of the Corporate Agreement which are the subject of the authorisation applications are as follows.

Pricing arrangements

- 9.3 Under the Corporate Agreement, it is intended that Star Alliance members will agree to offer discounts off business and other published fares on some or all of the routes covered by the Star Alliance that are travelled by employees of a corporation. It is also intended that in the case where a corporate customer requests a Star Alliance bid with firm net corporate rates (on some routes), the participating airlines will agree on the fare itself. This arrangement may raise pricing fixing concerns under section 45A(1) of the Act.

Exclusionary provisions

- 9.4 The Corporate Agreement provides for the coordination of bids to corporations. Whilst a bid is outstanding, the Star Alliance members agree not to make independent bids in competition with the joint bid in which they are participating. However, once a joint bid is withdrawn or rejected, the corporation may request and receive individual offers from the Star Alliance members that participated in the joint bid. In this respect, there is a risk that the proposed arrangements are covered by the definition of exclusionary provisions in section 4D of the Act regarding the supply and acquisition of these services.

Views of the Applicant

- 9.5 The Applicant considers that the proposed arrangements will not result in a substantial lessening of competition. The Applicant considers that the arrangements will increase competition in the markets for air passenger transport services in Australia, particularly as they will allow Air NZ and other Star Alliance carriers to provide effective competition against Qantas and BA.
- 9.6 In addition, the Applicant argues that a number of aspects of the proposed arrangements will help safeguard competition in the relevant markets including that:
- the bids will be developed and made on a case by case basis rather than as a standing arrangement between Star Alliance members;
 - the process for making a joint bid will only commence if a corporation consents to receiving a joint bid;
 - contracts between Star Alliance members and corporations will stand for either one year, or, in the case of a multi-year contract, will provide for termination at the end of each year upon 60 days' notice;

- individual Star Alliance members may decide whether or not to participate in a particular joint bid or to develop their own bids; and
- corporations will be able to review decisions about whether to seek a joint bid based on the competitiveness of past bids when compared with bids from non-participating Star Alliance members and airlines or alliances outside Star Alliance.

Commission assessment

Passenger transport market

Domestic

- 9.7 Given the absence of a Star Alliance member competing in the Australian domestic passenger transport market, it is unlikely that the Corporate Agreement will have any direct competitive effect on this segment of the passenger transport market.

International

- 9.8 As discussed in section 7, the failure of Ansett Australia in the domestic passenger transport market impacted heavily upon Star Alliance carriers operating to and from Australia with limited airport presences. The inability of passengers to continue their travel within Australia with a Star Alliance carrier appears to have dissuaded many passengers from travelling to Australia with a Star Alliance carrier, unless that carrier offered direct flights to the passenger's destination city. Consequently, all oneworld carriers who operate to and from Australia have experienced significant increases in their share of the international passenger transport market, particularly with regard to business travellers.
- 9.9 Further, given the relative high yield of business fares, adjustments in the passenger transport market involving business travellers may have a disproportionate impact upon the financial position and competitive ability of airlines.
- 9.10 The Commission is of the view that the Corporate Agreement would appear to provide an opportunity for Star Alliance members to improve their offering to business passengers and consequently improve their competitive position relative to oneworld members in the current passenger transport market environment in which a Star Alliance member does not operate domestically in Australia, particularly in the context of an alliance between Qantas and BA. This issue is examined further in the discussion on public benefits generated by the Corporate Agreement.
- 9.11 However, the Commission is also of the view that the Corporate Agreement has the potential to generate anti-competitive detriment primarily as a result of the requirement that participating airlines must agree on the level of discount to be applied to airfares for corporate travellers. This may limit the level of discounts offered relative to a situation where each airline individually determines its own discounts. That said, the Commission notes that a number of features of the Corporate Agreement are likely to further limit any anti-competitive detriment generated by Corporate Agreement. These features are discussed below.



Pricing arrangements

- 9.12 In the draft determination, the Commission noted that the pricing arrangements contained in the Corporate Agreement are limited to the requirement that participating Star Alliance members provide an agreed discount on business and other published fares. The Commission noted that the discounts are not static, but could vary from bid to bid and that there is no requirement that the actual fares to be discounted are agreed.
- 9.13 The Commission also noted that all Star Alliance members will not necessarily participate in every bid. In the event that two carriers participating in a bid operate on the same route (such as Thai Airways and Singapore Airlines on south-east Asian routes), the Commission noted that the carriers retain the ability to compete on the basis of fares and conditions, and that the proposed arrangements do not involve any revenue sharing between carriers, thus ameliorating any anti-competitive effect.
- 9.14 In response to the draft determination, the Applicant submitted that in the case where a corporate customer requests a Star Alliance bid with firm net corporate rates (on some routes), the participating airlines will agree on the fare itself. While this possibility may increase the anti-competitive effect of the pricing arrangements within the Corporate Agreement relative to that which was identified by the Commission in the draft determination, the Commission notes that the participating airlines would only agree on net fares at the request of a corporate customer. That is, the proposed arrangements will not permit participating airlines to agree on, and advertise, net corporate fares generally to all potential corporate customers. The Commission considers that this increased detriment is marginal and is not likely to alter its conclusion that the Corporate Agreement as a whole generates a net public benefit.

Voluntary participation by carriers

- 9.15 The Commission notes that the proposed arrangements provide for carriers to elect whether or not they wish to participate in a joint bid. The Commission considers that this provision may enable carriers who feel they may be able to offer a more attractive bid separate to the joint bid to compete more effectively. The Commission considers that this provision is likely to have the effect of limiting any detriment flowing from these arrangements. The Commission notes the provision of the Corporate Agreement which prescribes that if a carrier elects not to participate in a joint bid, the other carriers should not attempt to induce its participation.

Voluntary participation by corporate customers

- 9.16 The Commission notes that the proposed arrangements do not require corporate travellers to purchase an airfare under the Corporate Agreement. While corporate customers will face incentives to purchase fares offered under the Corporate Agreement, corporate travellers are free to purchase the best fare available, whether it is a Corporate Agreement fare from a participating carrier or another type of fare from a participating Star Alliance carrier or a fare from a non-participating carrier (whether or not a member of the Star Alliance).

9.17 The Commission considers that without this provision the conduct would have been significantly more anti-competitive. Corporate travellers will be able to purchase the fare that best suits their needs rather than being required to only purchase from a limited range of fares. In addition, the Commission considers that participating carriers are likely to develop fares for the joint bid that are at least as attractive as others on offer in order to attract corporate traffic.

Limited information sharing

9.18 The Applicant submits that the Corporate Agreement includes various provisions to prevent unnecessary information sharing between Star Alliance members and to ensure that only the information necessary to develop and enable the joint bid to be efficiently and promptly communicated to the corporate customer is to be collected. In particular, the Corporate Agreement prescribes that participating carriers should not discuss what they will do individually if the joint bid is not accepted, and that carriers should not engage in any discussion of possible future alterations to any carrier's fares, capacity levels or other sensitive business information.

9.19 The Commission considers that these provisions restricting the nature and extent of information shared between Star Alliance carriers is likely to limit the anti-competitive detriment of any such information sharing

9.20 In this context, the Commission notes Qantas' concerns that the proposed arrangements may enable Star Alliance members to share price information and engage in price fixing, which may facilitate anti-competitive conduct in other areas of their businesses. The Commission notes that any information sharing between competing Star Alliance airlines beyond the scope of this authorisation could be at risk of being in breach of the Act and is not protected from legal action by the Commission or third parties.

Other features of the arrangements

9.21 The Commission notes that the proposed arrangements enable a corporation to determine the carriers (or combination of carriers) from which it wishes to receive bids. The Commission considers that this provision may improve the variety of options available to corporations (or their agents) to seek the most competitive and attractive bid.

9.22 Additionally, the Commission notes that joint bids will only be developed for:

- multinational companies which have travel requirements across the world;
- companies which are based in a particular region; and
- companies which have a principal place of business in Australia (or another country) but which have significant international travel requirements.

9.23 These guidelines as to suitable corporate customers will restrict the applicability of the Corporate Agreement, somewhat limiting further any anti-competitive effect generated by the Corporate Agreement.

Market for the sale of air travel

- 9.24 The Applicant has submitted that the Corporate Agreement will be available through travel agents and other current distribution channels. Currently, the majority of corporations book their air travel through an agency rather than dealing directly with airlines.¹⁵ Industry estimates in 2002 put the annual value of corporate travel business handled by travel agents and airlines at around \$5 billion and of this total, it was estimated that airlines (including Ansett Australia prior to its failure) accounted for 25 per cent of the business and travel agents 75 per cent.¹⁶
- 9.25 In the draft determination, the Commission stated its understanding that following implementation of the Corporate Agreement, it is likely that the travel agency used by a corporation will act as an agent for that corporation in respect of receiving bids from Star Alliance members.
- 9.26 In response to the draft determination, the Applicant submitted that it is likely that the travel agency used by a corporation will act as an agent for that corporation in respect of booking travel on Star Alliance members. A corporation will choose whether to receive a joint bid from the Star Alliance. The role of the travel agent is to book travel on behalf of the corporation.
- 9.27 Consequently, the implementation of the Corporate Agreement is unlikely to impact on existing arrangements between corporations and their travel agencies. More broadly, it would appear that the implementation of the Corporate Agreement is unlikely to impact upon competition in the market for the sale of air travel.
- 9.28 The Commission notes that this situation may change in the event of a Star Alliance member entering the domestic passenger transport market and establishing its own distribution network in Australia.

Conclusion

- 9.29 In conclusion, the Commission is of the view that the Corporate Agreement has the potential to result in some public detriment due to a lessening of competition from the requirement that participating airlines agree on the level of discount to be applied to airfares for corporate travellers and in certain circumstances, participating airlines agreeing on the fare itself. However, the Commission considers that this anti-competitive detriment is likely to be minimal for a number of reasons, including that:
- participation in the joint bid process by Star Alliance airlines is voluntary;
 - while participating airlines are required to agree on the level of discount to be applied, in most circumstances they are still able to compete on the fare itself and any associated terms and conditions;

¹⁵ *Rush to grab Ansett's business clients*, Business Review Weekly, 4-10 April 2002.

¹⁶ *Rush to grab Ansett's business clients*, Business Review Weekly, 4-10 April 2002.

- participating airlines would only agree on the fare itself (on some routes) at the request of a corporate customer; and
- corporate customers are not compelled to purchase the Corporate Agreement fare and may purchase any other fare available.

Public benefits

Views of the Applicant

9.30 The Applicant contends that a number of public benefits will arise from the Corporate Program. These include:

- the introduction of a new product to the market;
- lower airfares for corporate travellers;
- lower costs for corporate travellers through cheaper access to information on fares and incentives, cost savings for sourcing travel arrangements and cost savings for administering travel arrangements;
- cost savings and increased efficiencies for Star Alliance members; and
- benefits to Australian trade and competitiveness.

Commission evaluation

Introduction of a new product

9.31 The Applicant argues that the Corporate Agreement will introduce a new product to corporate travellers and address strong demand among large corporate customers for a centralised solution to their international travel requirements. The Applicant considers that this increase in choice for corporate customers will stimulate competition in the markets incorporating corporate travel to and from Australia.

9.32 In general, the Commission is of the view that the introduction of a new product will only result in a public benefit if the product improves the situation of consumers relative to what it would have been in the absence of the new product.

9.33 The Commission concluded in its Draft Determination that the Corporate Agreement is likely to result in a public benefit to the extent that it provides corporations with an additional choice in respect of selecting an airfare for their corporate travel, and that this additional choice would not likely be available in the absence of the Corporate Agreement.

9.34 The Commission notes Qantas' submission that all major airlines, including the members of the Star Alliance, already compete vigorously in providing discounted fully flexible 'business friendly' fares, and in offering further discounts and rebates to businesses based on their volume of travel expenditure.

9.35 However, the Commission also notes that Star Alliance members can only discount services available on their individual network. The Corporate Agreement will

enable participating Star Alliance members to offer discounts to business travellers on interline fares across their combined network, which in the absence of the Corporate Agreement the airlines would have no incentive to offer. The Commission therefore remains of the view that the Corporate Agreement is likely to result in public benefit by making this new product available to corporate customers.

- 9.36 Additionally, the Commission notes that the availability of discounted published interline fares from Star Alliance carriers may encourage other carriers to seek to discount interline fares. This would introduce a level of competition into the passenger transport market which does not currently exist.

Lower airfares for corporate travellers

- 9.37 The Applicant argues that the implementation of the Corporate Agreement will result in fares and incentives for corporate customers which overall will be more competitive than those that could be offered individually by Star Alliance members. The Applicant contends that Star Alliance carriers will be able to offer corporations a better deal across a range of destinations by operating collectively. An individual airline would not be able to offer the same breadth of destinations at prices competitive with a Star Alliance joint bid.
- 9.38 The Commission agrees that corporate customers are likely to be attracted to a route network broader than that able to be offered by an individual airline. However, on the basis of the information available to the Commission, it is not apparent why the route network available to a corporate customer of a Star Alliance carrier will be broader as a result of that carrier participating in a joint bid under the Corporate Agreement. It would seem that corporate customers of a Star Alliance carrier are able to utilise the route network of the Star Alliance regardless of whether a joint bid is accepted.
- 9.39 In respect of the pricing of routes the subject of a joint bid, the Commission acknowledges that preferential prorates between Star Alliance carriers may enable such carriers to price their products more aggressively than they could do if not a member of a Star Alliance. However, on the basis of the information available to the Commission, it appears that Star Alliance carriers are able to take advantage of preferential prorates regardless of whether the Corporate Agreement is implemented.
- 9.40 The Commission notes that the Applicant has not raised the possibility of the discounted published fares as a public benefit generated by the Corporate Agreement.
- 9.41 The Commission considers that the possibility of discounted interline fares for corporate travel is likely to generate public benefit as such discounts are not currently available. In the absence of the Corporate Agreement, corporate travellers who must use interline services involving fares which are not subject to special pro rate agreements between Star Alliance carriers would not be able to obtain discounts on the IATA airline fares.

9.42 As noted above, the availability of discounted interline fares from Star Alliance carriers may encourage other carriers to discount such fares. This would introduce a level of competition into the passenger transport market which does not currently exist.

9.43 In general, the Commission considers that lower prices for consumers are likely to result in public benefit. Given that corporate travellers requiring interline fares have little choice but to purchase full fares, any discounts on these fares are likely to benefit corporate customers and thus result in a public benefit.

Cost savings for corporate travellers

9.44 The Applicant argues that the implementation of the Corporate Program will lower costs to corporate customers by enabling them to deal with a single carrier rather than a number of carriers, thus reducing the transaction and other costs that a corporate customer would ordinarily incur through dealing with a number of carriers to source and administer travel arrangements.

9.45 As noted in paragraph 9.24, the majority of corporations book their air travel through an agency rather than dealing directly with airlines. Consequently, the implementation of the Corporate Agreement is unlikely to have a direct impact on the transaction costs incurred by a corporation to source and administer travel arrangements.

9.46 The Commission acknowledges, however, that the Corporate Agreement may reduce the transaction costs incurred by a travel agency responsible for booking the travel of a corporation's employees. These potential transaction cost savings may occur as a result of the Corporate Agreement requiring a single carrier to be responsible for each customer account, thus enabling a travel agency to deal with one Star Alliance carrier only when booking travel for corporation, rather than dealing with a number of carriers. The Corporate Agreement may result in indirect cost savings to corporations if the potential transaction costs savings to corporate travel agencies are passed on to their customers.

Cost savings and increased efficiencies for Star Alliance members

9.47 The Applicant argues that the Corporate Agreement will enable participating Star Alliance members to deliver an integrated travel service to corporate customers in an efficient manner. The Applicant contends that in the absence of the Corporate Agreement, an airline could only offer a similarly integrated travel service by entering into a complex set of transactions with other airlines and the associated transaction costs would limit the availability of discounts for customers.

9.48 The Commission acknowledges that the Corporate Agreement may enable Star Alliance carriers to deal with each other in a streamlined manner and thus potentially reduce transaction costs. It appears that the Corporate Agreement provides for these potential transaction cost savings to participating Star Alliance carriers to be passed on to consumers in the form of a discount on published fares.

9.49 In addition to these efficiency arguments, the Commission notes that the Corporate Agreement will redress to some extent the competitive disadvantages experienced

by Star Alliance members relative to oneworld members, particularly in the context of an alliance between Qantas and BA, given the lack of an aligned Star Alliance domestic operator in Australia. Table 7.1 shows that this factor appears to be contributing to a declining Star Alliance share of the passenger transport market with respect to corporate travellers. The Commission agrees with the Applicant's contention that the introduction of the Corporate Agreement constitutes a pro-competitive development in the context of the current passenger transport market environment in which a Star Alliance carrier does not operate domestically in Australia.

Benefits to Australian trade and competitiveness

9.50 The Applicant contends that the proposed arrangements are likely to:

- enhance the attractiveness of Australia as a location for the business operations of multinational and regional corporations;
- improve the ability of corporations already carrying on business in Australia to compete internationally; and
- increase and facilitate the promotion of tourism to Australia generally.

9.51 The Commission would expect that when a corporation is selecting a location to establish its operations, considerations such as taxation requirements, resource availability, access to distribution channels and marketing opportunities would take precedence over considerations relating to corporate travel arrangements. Consequently, the Commission considers that while the Corporate Agreement is likely to enhance the attractiveness of Australia as a location for the business operations of multinational and regional corporations it will only be at a marginal level. All other factors being equal, the Corporate Agreement could contribute to lessening travel cost as a determining issue.

9.52 On the basis of the information available to the Commission, it appears that the Corporate Agreement may improve the ability of corporations already carrying on business in Australia to compete internationally by providing these corporations with cost savings (through discounted airfares) and thus improving the financial resources available to these corporations for competitive purposes.

9.53 The Commission notes the Applicant's argument that the proposed arrangements will increase tourism to Australia generally. This argument would appear to be based on an assumption that corporate travellers utilising the Corporate Agreement may elect to holiday in Australia immediately before or after their business commitments in Australia, or choose to return to Australia for a holiday following a business commitment here. To the extent that this assumption is correct, the Commission acknowledges that tourism may be enhanced however, the Commission is of the view that any such public benefit is likely to be limited and no significant weight will be attached to this claim in the absence of more substantial evidence.

Conclusion

9.54 The Commission considers that public benefits will be generated by the Corporate Agreement including:

- an increase in the range of fares available to corporate travellers;
- an additional level of competition between airlines in the form of discounting of interline fares;
- cost savings to corporate travellers and corporate travel agencies; and
- an increase in the ability of Star Alliance carriers to compete more effectively with oneworld carriers.

Balance of public benefits and anti-competitive detriments

9.55 The Commission must be satisfied that the proposed conduct results in a benefit to the public that outweighs any detriment to the public constituted by any lessening of competition arising from the conduct. There must also be a nexus between the claimed public benefits and the conduct for which authorisation is sought.

9.56 As discussed above, the Commission considers that there is the potential for a small amount of detriment flowing from the effect on competition of the proposed arrangements. However, the Commission is of the view that this anti-competitive detriment will be minimal for several reasons including:

- participation in the joint bid process by Star Alliance airlines is voluntary;
- while participating airlines are required to agree on the level of discount to be applied, they will generally be able to compete on the fare itself and any associated terms and conditions;
- participating airlines will only agree on the fare itself (on some routes) at the request of a corporate customer; and
- corporate customers are not compelled to purchase the Corporate Agreement fare and may purchase any other fare available.

9.57 The Commission considers that the proposed arrangements are likely to result in public benefit, particularly arising from:

- an increase in the range of fares available to corporate travellers;
- a potential additional level of competition between airlines in the form of discounting of interline fares;
- cost savings to corporate travellers and corporate travel agencies; and
- an increase in the ability of Star Alliance carriers to compete more effectively with oneworld carriers.

9.58 In particular, the Commission considers that in the current market environment, in which a Star Alliance carrier does not operate domestically in Australia and the domestic passenger transport market is dominated by a oneworld carrier, any enhancement of competition between airlines, whether through the potential introduction of a new level of competition or through the enhancement of the ability