Submission on the application for authorisation of a Tasman networks agreement (Qantas & Air New Zealand)

Wellington International Airport

15 May 2006

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INTRODUCTION

1 This submission is presented by Wellington International Airport Limited (*WIAL*) and relates to an application by Qantas Airways Limited (*Qantas*) and Air New Zealand Limited (*Air NZ*) for authorisation of a Tasman Networks Agreement (*TNA*).

WIAL'S INTEREST IN THESE PROCEEDINGS

2 The main end-users of WIAL's facilities - Australian and New Zealand people travelling on the Tasman – are particularly vulnerable to the removal of competition between the two main airlines on Tasman routes. Like many groups in Australia and New Zealand, we have no desire to oppose a proposal put by our major airline customers. However, this proposal will directly affect our travelling customers, the vast majority of whom are Australians travelling to New Zealand or New Zealanders travelling to Australia. Indeed, we fear that with the TNA in place, the number of travelling customers will diminish significantly.

3 WIAL has consistently opposed Air NZ's and Qantas' sustained efforts to collude, described as the "Alliance". WIAL took an active role in opposing the Alliance, including engaging in substantive proceedings in both the New Zealand Commerce Commission and, subsequently, the High Court of New Zealand.

4 The outcome of course was that the New Zealand High Court substantially affirmed the Commerce Commission's view that the Alliance was a highly anti-competitive arrangement giving rise to substantial detriments for affected markets. In Australia, the ACCC rejected the application, but the Australia Competition Tribunal took the opposite view in October 2004. As discussed below, the evidence since that decision is that the Tribunal was overly optimistic in it is assessment of possible competition constraints on any Qantas/Air New Zealand collusion.

5 The current proposal is presented as limited compared to the Alliance. However, the TNA presents issues of comparable significance for the travelling public. So WIAL's position is essentially unchanged.

6 WIAL elaborates below both by reference to the specific questions raised by the ACCC in its letter dated 19 April 2006 and with additional comment of particular relevance to the issues at hand. WIAL would of course welcome any opportunity to speak directly to these points. In that regard, please feel free at any time to contact Simon Draper, Chief Executive on +64 4 385 5141.

SUMMARY OF POSITION

7 Like other businesses in the Wellington Region, Wellington Airport has a direct interest in a sustainably prosperous travel industry on the Tasman. Our revenues are directly related to the number of people travelling to and from Wellington (not the number of aircraft landing at the airport). Our interests are aligned with other travel oriented businesses and our revenue structure encourages us to shoulder some of the burden of promoting travel. We receive no benefit whatsoever from an airline operating an empty aircraft. Nor would we suffer any detriment if, under the proposed arrangement, the volume of passengers were the same as the counter-factual scenarios (trans Tasman markets without an arrangement between Qantas and Air New Zealand). We simply do not believe that this will be the case.

8 We have invested heavily in the objective of sustainable travel growth, including joint marketing programs with some airlines and tourism authorities. Some of our efforts are publicly known and some are not. We would continue to invest in growth oriented strategies in the absence of a "code-share" or anti-competitive arrangement. However, it is our experience that without healthy competition between airlines, investment in destination marketing is a very blunt instrument.

9 Naturally, Wellington Airport supports airlines in their objective to pursue a return on their investment. We also accept that individual airlines in a competitive market are entitled to make commercial decisions on schedules and fares, and that in some cases those decisions may reduce their own supply or raise their own prices. It is likely that if the current application is not approved, individual airlines will decide to make changes in some Tasman markets. Indeed, that has already been happening over the past few years. We expand further on possible outcomes in the section of this submission on counter-factuals.

10 That said, Wellington Airport recognises that some arrangements between airlines may have benefits that outweigh any disadvantages through reduction in competition. For example, there are numerous code-shares that have no impact on competition – they are branding extensions on a route that an airline would otherwise not serve. There are also some arrangements that on the face of it diminish competition, but are authorised for other reasons. We have never participated in deliberations over Qantas' Joint Service Agreement with British Airways on the Kangaroo route. But, as an example, there seem to be plausible reasons why the ACCC would authorise such an arrangement on a route that has a number of other players with comparable competitive strength and presence. This will probably remain the case for as long as the Kangaroo route is a one

stop service to London with a number of airlines based in well placed hubs that actively exercise traffic rights between Australia and the UK.

11 The reason for Wellington Airport's objection to the current application before the ACCC is that it does not fit into any of the above circumstances. The current application is for two airlines that dominate the relevant markets to jointly set schedules, supply, prices and several other matters, as well as share the revenues from their joint enterprise in pre-determined fashion. Our principal concern is about market structures that will be in place for some time and how those structures will affect future decision making. We naturally have reservations about some of the announced schedule changes (particularly as they relate to Wellington), but we are equally concerned about future decisions that would take place under the TNA.

12 The 'code-share' proposal should be evaluated for its impact on long term market structures. Behaviour in the market will be dictated by the market structures that are approved by the Commission, not by the declared best intentions of the proponents putting forward the proposal today. That behaviour will not be mitigated by the best of relationships or attempts to secure promises and commitments. Even undertakings that are monitored by the Commission are a poor second to a well functioning market.

13 In our view, the outcome of decision making under the proposed arrangement will significantly disadvantage travellers compared to the decision making in a competitive environment where the most efficient producer with the best strategy fills gaps left by other players. That will flow on to numerous businesses and regional economies, including our own.

14 We expect that prices will rise and that seats in lower fare categories will become harder to secure, particularly at peak times. We expect reductions in capacity and higher prices to lead to a significant reduction in travellers on the Tasman.

15 We foresee no public benefits sufficient to outweigh those detriments.

16 We do not accept that there are no or few viable alternatives for the applicants.

WHAT ARE THE REASONS FOR THE PROPOSAL?

17 The Applicants say they continue to face "unabated challenges of a global aviation industry" where passengers expect cheaper fares due to low cost carriers, and that network airlines must lower their costs. They also say that the international regulatory regime precludes consolidation by merger.

Of course, none of those factors is unique to the 2 major carriers servicing the Tasman.

18 But the applicants claim that the Tasman is an "intensely competitive market", where they face the competitive strategies of Emirates (marginal cost) and Pacific Blue (low cost point to point). That competition has meant, according to the applicants:

- significant surplus capacity (5,200 seats a day);
- the applicants must secure cost reductions, increase load factors and improve revenues.

19 The applicants say the TNA will:

- remove surplus capacity with no impact on low fares;
- access "unique efficiency gains";
- comprise a "natural and necessary response" by network carriers to a competitive market;
- allow for a number of service enhancements.

20 WIAL believes a robust public process is needed to test these claims, and commends the ACCC for the way it is handling this application. Some obvious questions are:

- If capacity reductions are necessary, can't capacity be reduced unilaterally by one or both of the applicants?
- Why are the efficiency gains unique to the TNA proposal?
- Why is schedule spreading unique to the TNA?
- Don't both applicants have substantial advantages over their rivals on the Tasman - reputation, national carrier status, domestic feeder network, special government protections - Qantas (ownership restrictions) and Air NZ (financial bail out)?
- Why is collusion a natural response to a competitive market?
- What competitive strategies have the applicants considered but rejected?

- Are those service enhancements really inefficient add-ons that a competitive market would not sustain?

- Given the importance of connectivity to network airlines, won't collusion leak into other markets - e.g. other international routes, domestic routes?

- In what the applicants assert is an "intensely competitive" market with marginal-cost players, how is it that trans Tasman fares have been so readily increased since the time of the Australian Competition Tribunal decision? Why has there been no entry of new players in response?

- Why is it that the applicants are only now seeking to respond to low cost carriers, who have been around for a long time?

- What specifically are the international regulatory regimes that prevent merger? It was the New Zealand Commerce Commission and High Court that prevented the applicants last time, bearing in mind that the ACCC's decision was overturned by the ACT.

- Don't many industries, especially those with high fixed costs, have firms that operate at marginal cost?

- Don't many industries have start up firms which operate on a lower cost base than incumbents with legacy costs?

- What is so unique about the aviation industry?

- If major aircraft manufacturers or fuel companies were proposing to collude on production levels and price (with the stated aim of improving efficiency), would the applicants support that action?

HOW SHOULD THE MARKETS BE DEFINED?

21 WIAL submits that when considering the TNA it is important to approach the market definition question afresh, and ask what is the market analysis that best brings to light the competition effects of the proposal?

Previous approaches to market definition

22 Market definition is particularly difficult in a network industry, where a slavish adherence to substitutability criteria would result in an unworkable number of narrow markets. For this reason, judgment is required to select the market most appropriate for the application or proposal being considered.

23 This was the approach taken by the ACCC to the issue of geographic market definition when analysing the previously proposed comprehensive Qantas/Air New Zealand Alliance. At paragraph 10.12 of its determination the ACCC stated:

> *When examining international air transport passenger markets, 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.*

24 The New Zealand Commerce Commission adopted a similar framework, emphasising the central issue was identifying the market definitions most appropriate for the particular transaction or proposal, which is a matter of judgment. The New Zealand Commerce Commission stated at paragraph 240 of *Decision 511*:

> *...there is authority to support the approach of individual city pair routes as being the correct geographic markets in airline cases. The reasoning behind this is that travellers, in most instances, have little flexibility in terms of their origination and destination. The Commission considers that, in principle, such an approach is correct, but for the purposes of competition analysis in this case, it is more appropriate to aggregate city pairs into geographic groups, consisting of groups of city pairs that will be impacted similarly by the proposed Alliance.*

25 The geographic aspect of market definition was not contested in front of the Australian Competition Tribunal and New Zealand High Court, and so the Tribunal and Court made no comment on this issue.

An aggregate market definition will obscure the competition effects

26 WIAL submits the market definitions used to analyse the previous proposed Qantas/Air NZ equity transaction and comprehensive Alliance are different from the market definitions that most usefully facilitate a competition analysis of the TNA.

27 In particular, an aggregated Tasman market is no longer appropriate. Aggregating at the Tasman level was an acceptable and necessary compromise when analysing a proposal on the scale of the comprehensive Alliance. But the detail and the differential impacts of the TNA mean a less aggregated market definition is needed if the competition effects are to be properly considered.

28 "The Tasman" in fact currently represents 25 different direct city-pairs. WIAL does not suggest that there are 25 distinct markets, but there are certainly a number of markets. As noted above, the issue is one of judgment, with the objective being market definitions that best facilitate an analysis of the competition effects of the TNA. **Schedule 1** sets out the airlines serving the main city pairs and the frequency of their services.

29 WIAL submits that, after a prolonged opportunity to observe the actions of Emirates and Pacific Blue, there are at least three clusters of routes:

29.1 Routes on which a number of other airlines represent an offer comparable those of the applicants. These would include Auckland-Brisbane, Christchurch-Brisbane and Christchurch-Sydney. These routes are characterised by frequency of services by other players that makes those services relevant to the combined Qantas-Air NZ schedule.

29.2 Routes on which there is some competition (a daily service by another player), but that competitive offer pales compared to the schedule offered by the two applicants. This would include Auckland-Sydney, Auckland-Melbourne and Christchurch-Sydney. For example, on the Sydney-Auckland route, the applicants currently offer 71 services per week out a total of 85 services. Emirates offers only 7. Aerolineas Argentinas and Lan Chile offer another 7 between them (but Lan Chile code-shares with Qantas).

29.3 Routes on which there is no comparable offer or a very limited offer from other airlines when compared to Qantas and Air New Zealand. These would include all routes in and out of Wellington, Christchurch-Melbourne, and all services from regional ports in NZ (Queenstown, Dunedin, Palmerston North and Hamilton) and other ports in Australia (Cairns, Adelaide, Perth and Gold Coast).

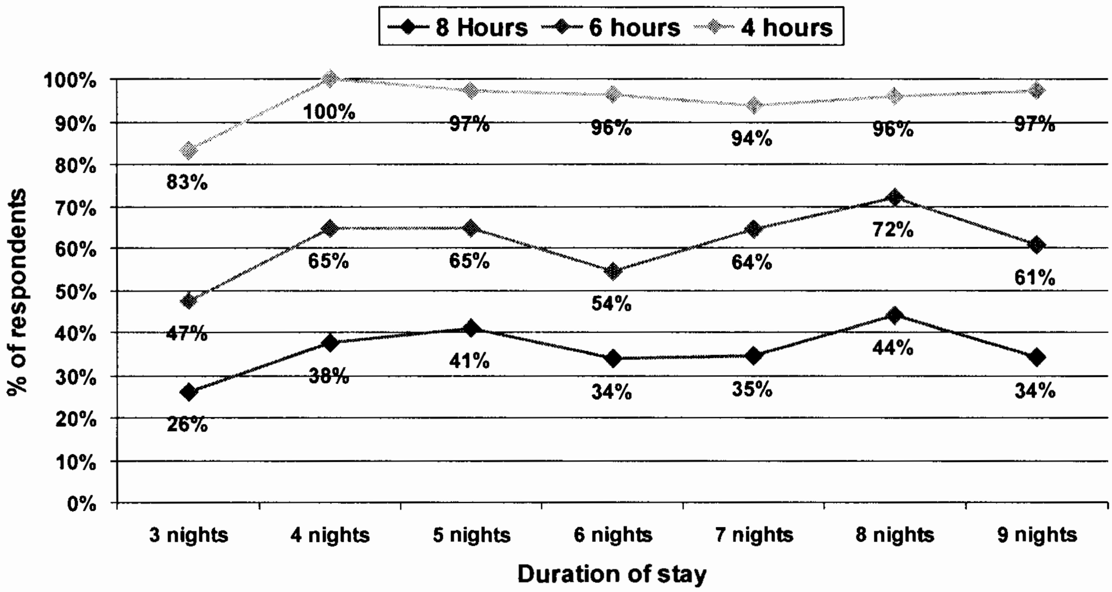
30 These clusters have distinct characteristics, and are impacted differently by the proposed TNA. Despite the minimal competition on many routes, the applicants seek to collude on all routes.

31 The ACCC's investigation may reveal the competitive impacts in Australia are best examined by making a different distinction. The general point, however, is that an aggregated Tasman market will obscure rather than facilitate an analysis of the competition effects of the TNA.

Short haul markets have a distinct competition dynamic

32 In 2004, AC Neilsen conducted customer research on behalf of Tourism New Zealand. It showed that travellers on short stay holidays (those already sensitive to price) are also highly sensitive to travel time and travel

convenience. The graph below shows the percentage of respondents who would take a short holiday of a particular duration, based on the hours required to travel to the destination.



33 This simply confirms what airlines have always known: the number of stops in an itinerary affects market share and potentially yield. It also confirms the philosophy of low cost carriers like Jetstar - stimulate markets with direct services at affordable prices.

34 The Tasman markets are short haul and highly sensitive to convenience and the need to change flights. They are markedly more sensitive to connections than long haul markets such as the Kangaroo Route where the time consumed by a connection or transfer is relatively insignificant compared to the total trip duration and period of travel.

35 For most travellers on the Tasman, a direct service is highly valued and there is very limited or zero substitution with connections via other city-pairs. This is particularly so for leisure travellers on tight itineraries and business people on short trips. Some business people travel across the Tasman just for the day.

36 An analysis based on a single aggregated Tasman market will not properly recognise this fundamental feature of trans Tasman travel, and not properly consider the significant competition impacts of the TNA.

37 In any case, there is no potential for taking connecting flights on the New Zealand side other than through Qantas and Air NZ. On the Australian side, Virgin Blue can offer domestic connections, but suffers considerably on trans Tasman route diversity and frequency.

The Wellington market

38 WIAL is most aware of the market for travel to and from Wellington. This is a distinct market (or markets), with clear differences from other trans Tasman markets. It is a short haul market that requires convenient direct services. While some passengers fly the Tasman via Auckland, they can only do so if they are very inconvenienced by several hours and if they fly on Air NZ or Qantas on the domestic sector (which adds to their cost unless they also fly on Qantas or Air NZ on the Tasman). Insofar as people fly via Auckland, it is due to lack of competition in Wellington.

39 It is very unlikely that any other airline will enter the Wellington market. Emirates has repeatedly said that it will not do so, which has been borne out by its actions. Pacific Blue has not grown its fleet significantly, it has not entered domestic routes and its approach to the Tasman is now very limited compared to the applicants. In Wellington, it serves one route three times per week. Indeed, WIAL has spent a great deal of time over a long period working with Pacific Blue to promote and increase its services from Wellington. Out of that experience, we are well aware of the difficulties that Pacific Blue faces in doing so.

40 It has already become clear that seats and services will be withdrawn diminishing the availability of affordable seats in the Wellington market. When seats have been withdrawn in recent past, volumes of passengers have fallen.

41 If the TNA goes ahead, WIAL expects average prices to increase substantially. In addition to no real competitive tension holding down headline prices, the reduction in the number of seats offered will force more customers into higher priced seats, especially during peak periods.

HOW HAS THE TRANS-TASMAN MARKET CHANGED SINCE OCTOBER 2004?

42 This is the vital question, particularly in the Australian context where the Australian Competition Tribunal in 2004 placed significant confidence in predictions of growing competitive constraints on any Qantas/Air NZ collusion. As demonstrated below, this confidence in fact was misplaced. Despite rises in trans Tasman fares since the decision, the evidence is that Pacific Blue and 5th Freedom couriers have been, and will continue to be, of limited competition significance.

Air NZ

43 Despite Qantas continuing to operate comprehensive services on the Tasman, Air NZ's own competitive position has improved markedly. In that regard, it is useful to reflect on the underlying commercial objectives articulated in support of the original Alliance. Those were many and varied

but, at least in the initial stages of the regulatory processes, the airlines' rhetoric focussed heavily on Air NZ's perilous commercial position and in particular its vulnerability to being sent into a "death spiral" by Qantas.[1] A "failing company" argument all but in name.

44 Indeed, at that time, Air NZ's position was marginal. Fortunately for Air NZ – but unfortunately for the argument supporting the need for market collusion – things improved quickly and dramatically. Of course, the "death spiral" forecast becomes less tenable with each incremental improvement in Air NZ's financial position.

45 It is apparent to any observer that those improvements were secured the "old fashioned way" – through strong management and innovation, not collusion. Recent notable commercial initiatives have included:

45.1 Launch of the quasi-LCC "Express" product first on New Zealand domestic routes and then subsequently on the Tasman;

45.2 Substantial additional fleet investment particularly in 777 and 787 aircraft types.;

45.3 Overhaul of the long-haul product in particular to bring its Business Class service to the forefront of the market and to establish the new "Premium Economy" class;

45.4 Launch of new international routes establishing connections with destinations such as San Francisco, Shanghai and Delhi;

45.5 Commitment to fly the (genuinely) competitive Hong Kong-London route, therefore being the only airline in the world to offer a seamless round-the-world service.

45.6 Rationalisation of its engineering operations; and

45.7 Rationalisation of various ancillary services, such as aircraft cleaning.

45.8 Growth of market share on various Tasman routes.

45.9 New marketing initiatives in Australia for the first time since the demise of Ansett.

46 These are not the activities of an airline in terminal decline. Any similar arguments should be treated with caution this time around.

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[1] See "Updated Executive Summary" dated 17 March 2003 restating and updating the key arguments put to both the Commerce Commission and ACCC, page 10.

Qantas

47 Of course, there has never been any suggestion that Qantas should require competition shelter to secure its survival. Quite apart from its robust financial position, Qantas enjoys ongoing Governmental relief through the particular configuration of international air rights in and out of Australia – such as on the key "Kangaroo route" and the Pacific route.

48 Rather, this proposal will have the effect, and we assume the purpose, of encouraging Qantas to "close down" competition on the Tasman (and on New Zealand domestic routes). WIAL submits the effective $40m payment from Air NZ to Qantas needs to be seen in this context also.

49 Over the period since the ACT's decision in 2004, Qantas launched Jetstar and has entered the trans Tasman market. By all accounts, Jetstar has been a great success.

Pacific Blue

50 The commercial impact of Jetstar's activities on Virgin Blue has clearly flowed through to its Pacific Blue operations in New Zealand.

51 The New Zealand Commerce Commission had been (rightly) sceptical as to the competitive constraint likely to be exerted by Pacific Blue if the Alliance were to proceed. In relation to the Tasman market, the Commission concluded that:

51.1 Virgin Blue was unlikely to enter to a sufficient extent to constrain the Alliance for at least two years from that time; and

51.2 Instead, Virgin Blue was likely to enter in a measured way as it received delivery of more of its B737-800 aircraft and depending on demand and the response it faced from the incumbents (*see paragraphs 747 and 751 of Decision 511*).

52 It was also noted that the establishment of Virgin Blue in Australia was greatly assisted by the collapse of Ansett and that it was unlikely that its growth in the Tasman and domestic New Zealand markets would receive a similar boost, so that its expansion would be slower (*paragraph 531 of Decision 511*).

53 By contrast, in Australia, the Tribunal was (prematurely) bullish. Claiming to have access to more up to date data than that available to the ACCC in its rejection of the Alliance, the Tribunal found that:

53.1 Virgin Blue appeared to be in a strong position to enter quickly or expand on any trans-Tasman city-pair route (*ACT Determination, [2004] AcompT 9 (12 October 2004), para 318*);

53.2 Virgin Blue had built up a 9% market share of the aggregated main trans-Tasman routes within a very short time (since beginning in early 2004)(*para 299*);

53.3 Virgin Blue had three aircraft in domestic operation in Australia in Pacific Blue livery which were capable of being deployed across the Tasman within two months and was therefore readily able to add another 42 weekly return flights across the Tasman (*para 315*);

53.4 As there were no natural or strategic barriers to its long-run expansion, Virgin Blue was in a position to expand its current market share (*para 324*);

53.5 Virgin Blue would not withdraw from the trans-Tasman markets, which it considered to be an extension of the Australian domestic market (*para 325*); and

53.6 Virgin Blue intended to begin domestic New Zealand services from December 2004, suggested that it might enter the trans-Tasman Auckland routes to enable connectivity with its domestic services (*para 325*).

54 Time has proved the Tribunal wrong. Pacific Blue has been a shadow of the competitive constraint expected by the Tribunal. In particular Pacific Blue:

54.1 Has not entered the New Zealand domestic market and has never appeared close to doing so;

54.2 Operates only 28 services per week each way across the Tasman (across six of the possible 25 routes). This is the equivalent of two aircraft.

54.3 Has withdrawn from the Sydney-Wellington route completely, remaining only on the Wellington-Brisbane route three times per week;

54.4 Operates only three routes out of Christchurch (its home base), not all of which have been trouble free;

54.5 Operates only two routes from Auckland with limited frequency;

54.6 focused much of its energy and resources on routes between Australia and the Pacific Islands;

54.7 failed to enter new parts of the market or grow its fleet or presence; and

54.8 remains somewhat pinned-down by the commencement of Jetstar in the Australian domestic market.

5th Freedom

55 Meanwhile, in terms of competition from "5th Freedom" carriers, Thai Airways, Malaysian Airlines and Polynesian Airlines have all stopped flying the Tasman.

56 It is worth noting that there is nothing to stop the applicants code-sharing with fifth freedom carriers. For example, Qantas already code-shares with Lan Chile (one of the 'competitors' flying SYD-AKLvv that operates only four times per week).

57 All fifth freedom carriers suffer from limited awareness of their trans Tasman offer. For example, most potential customers would only know that they can fly Royal Brunei between Auckland and Brisbane (three times per week) if they went into a travel agent (and then one with a relationship with Royal Brunei). In a short-haul market dominated by internet bookings, the fifth freedom carriers are severely disadvantaged.

58 Emirates has been cited as the main destroyer of "yield" in the trans Tasman market. Air NZ has even gone so far as to claim that it has been unlawfully "dumping" capacity on the trans Tasman market. True it does provide services on the following routes:

58.1 Auckland-Sydney (once per day, compared to 10 per day by Qantas and Air New Zealand)

58.2 Auckland-Brisbane (once per day, compared to 4 per day by Qantas and Air New Zealand)

58.3 Auckland-Melbourne (once per day, compared to 4 per day by Qantas and Air New Zealand)

58.4 Christchurch-Sydney (once per day, compared to 4 per day by Qantas and Air New Zealand)

59 Emirates' "FSA" improved service offering will clearly have a competitive appeal. But Emirates' will always been confined to a niche of time elastic travellers, which represents a small minority in short-haul markets like the Tasman. Its effectiveness overall as a competitive constraint is structurally limited by:

59.1 Comparative infrequency of service;

59.2 Service to only 4 out of 25 city pairs;

59.3 Lack of domestic connections in either Australia or New Zealand, which limits its market only to those in the cities it serves;

59.4 Lack of presence as a trans Tasman player (that is, regular travellers on the Tasman are less likely to be members of its loyalty program or to check prices on the Emirates website).

59.5 Relative inconvenience of flight times; and

59.6 Lack of presence out of most centres.

60 The applicants have argued that fifth freedom carriers operate at a marginal cost. Perhaps so. It is also the case that, despite the best intentions of some airlines, the Tasman is not a core market and their long term commitment to the market is also marginal. For most, the Tasman is a convenient add-on that is subject to other drivers of route decisions.

WHAT IS YOUR VIEW OF THE CURRENT STATE OF COMPETITION MORE GENERALLY AND ON PARTICULAR ROUTES?

61 Generally, competition between Air NZ and Qantas on the Tasman is relatively keen and remains overwhelmingly the most significant dynamic in the trans Tasman markets. They dominate in terms of brand presence, service frequency, network coverage, domestic connections and loyalty programme membership.

Overview

62 A summary of routes and frequencies is provided in **Schedule 1**. This has been constructed from simple public information provided by the airlines on their websites. There are some small disparities between this information and that provided by the applicants in their submission, but none that changes the key message. The table clarifies that although there may be eight airlines operating across the Tasman:

62.1 All the fifth freedom carriers except Emirates operate on only one route, and only a few times per week.

62.2 No route has eight carriers.

62.3 Most routes have only 2 or 3 carriers. Some have only one carrier.

62.4 There are major disparities between the frequencies and capacity offered by the applicants and those offered by other airlines (including Emirates and Pacific Blue).

62.5 Where there are more than three players on a route, the balance tends be made up of fifth freedom operators with limited frequency and presence.

63 For services in and out of Wellington, competition is very limited. It is entirely constituted by Air NZ and Qantas, except for a single service to Brisbane by Pacific Blue (3 times weekly). In Auckland and Christchurch competition is still severely limited with the possible exception of two routes (AKL-BNE and CHC-BNE) and possibly a third (CHC-SYD).

64 Air NZ claims that competition is so fierce that it is has precipitated some kind of crisis of over-capacity. This is not the case. Load factors on trans Tasman sectors are in fact comparable with those on many commercially viable routes all over the world. This is discussed in detail below.

65 The relatively benign competitive conditions (certainly as compared with the airlines' claims) can also be illustrated by reference to market prices. They have been increasing significantly over the past year.

Qantas and Air NZ are dominant in Tasman markets

66 The applicants point to a decline in total market share from over 90% to slightly less than 80% (although it is not clear to us whether this includes Freedom and Jetstar). Our calculation from BTRE data for the full year to June 2005 (when competition was said to be fierce) is that the two airlines had 81% of passengers. This data was not available to the ACT at the time of its decision. The combined market share now appears to be relatively stable and will of course depend on the actions of the applicants.

67 Only a market player with extreme expectations of market share would describe a market share of anywhere between 75% and 85% as anything other than dominant. We note that in data provided to the ACCC in relation to the JSA for the Kangaroo Route, the two applicants on that occasion (Qantas and British Airways) had a combined market share of 44% between the UK and Australia. Quite a difference to the combined market share of the current applicants. To accept that 81% market share is acceptable for an anti-competitive arrangement may place the ACCC in a difficult position in future deliberations in other industries.

68 The applicants are keen to focus on capacity shares on various routes, rather than market shares. This can be highly misleading as other airlines, particularly fifth freedom carriers, operate with particularly low load factors. That is, their impact in the market seems well below their capacity share.

69 That phenomenon also highlights the limits to the competitive role of fifth freedom carriers. The applicants say that players such as Emirates are price

leaders with a marginal cost model, yet they have very low load factors. This demonstrates a number of points:

69.1 Fifth freedom carrier schedules are determined by long-haul imperatives. Their participation in the trans Tasman market is also determined by long-haul imperatives, which makes them fragile participants.

69.2 Fifth freedom carriers cannot offer the frequency or route diversity required for short haul markets such as the Tasman.

69.3 Fifth freedom carriers have no access or very limited access to domestic connections on both sides of the Tasman. This means they can serve only the cities in which they directly operate.

69.4 Market awareness of the trans Tasman operations of Fifth Freedom carriers is very limited.

69.5 Participation in loyalty programs of fifth freedom carriers is limited.

Competition and Excess Capacity

70 The applicants say that load factors have fallen which shows problem with over-capacity. They quote numbers of empty seats and empty aircraft (equivalents) to suggest the same point. In fact, empty seats need to be considered in the context of total seats. The FY2005 year data (the most recent full year publicly available) provides some interesting comparisons on international routes in and out of Australia. This was a twelve month period during which the applicants put to the Australian Competition Tribunal that competition was fierce and would continue to be so. Since that time, there have been withdrawals from the Tasman by some airlines. The relevant load factor figures are as follows:

Trans Tasman – Seats Occupied

Qantas	77%
Air New Zealand	72%

Other International – Seats Occupied (to/from Australia)

Qantas - average	76%
All international airlines	70%
Singapore Airlines	76%

Cathay	72%

71 The Tasman load factors for the applicants seem to be very similar to load factors of other reputable airlines on other international routes. There just doesn't seem to be any crisis of over-capacity on the Tasman.

72 Only a market player with extreme expectations of load factor could suggest that the applicants' Trans Tasman load factors are at such an unacceptable level that an anti-competitive arrangement should be authorised. Figures published by Air New Zealand themselves suggest that they consider a seat load factor of 74% on the Tasman to be reasonable.

73 In part, any decline in load factor is the result of actions by the applicants themselves. For example in 2004 when routes out of Christchurch were colourfully being described as a "bloodbath", Air New Zealand made a decision to shift a great deal of capacity from other markets to trans Tasman routes out of Christchurch.

74 There appears to be a natural range of load factors, and that range is reflected in the recent load factors of the applicants on the Tasman routes. Too low and capacity is withdrawn. Too high and customers are turned away on a regularity that is unacceptable to airlines operating a market. And of course, to operate a schedule across a season means that there may be periods when demand is below the average. When competitive dynamics are withdrawn, that range of load factors may change as it becomes more acceptable to discourage or turn away travel.

75 But the Commission should not be swayed by the idea, put by the applicants, that they cannot adjust capacity unilaterally for fear of losing network coverage. For airlines like the applicants with a variety of aircraft types operating the Tasman, it is possible and practicable to reduce capacity by changing aircraft types during periods of seasonal low demand. On routes already dominated by narrow bodied aircraft (such as those from Wellington), airlines often adjust capacity by making changes to schedules within seasons and adding or withdrawing services on days of particularly slow demand (eg: Saturday afternoon). That is, it is quite possible to unilaterally adjust capacity without losing network coverage and it is done regularly by the applicants.

76 It would also be incorrect to accept that demand is fixed and that supply needs to be adjusted to demand. In fact, demand is a function of supply, fare levels and marketing (as Virgin and Jetstar have shown in Australia). This is particularly so for the "marginal passenger". When seats are added at affordable prices on an airline with market presence, the market grows. When they are taken away demand can fall commensurately. Locally,

Wellington has experienced that over the past year. When Virgin Blue left the Sydney-Wellington route, seats fell by 22% in the year to March 2006. Passengers fell by exactly that proportion over the same period. During that year, seats grew dramatically on routes to Brisbane and the Gold Coast, and passengers grew with them.

77 This suggests that the "marginal passenger" is constrained in many markets. We fear that this will again become the norm.

78 An examination of the "before" and "after" schedules put forward by the proponents suggests a very dramatic reduction in seats in many cases. Some adjustments are required to the 'current schedules' to reflect public information and known changes to aircraft types. On routes to Wellington the reduction is 12% overall between the two airlines, and on some routes Air New Zealand will simply withdraw from flying. For Auckland the reduction of Air New Zealand and Qantas seats seems to be 14%. At Christchurch (where Pacific Blue is based and does most of its trans Tasman routes) we estimate that seats will increase by around 2% overall (principally on the Melbourne and Brisbane routes). Apart from anything else, these disparities suggest that there is more than one market.

Prices

79 The Australian Competition Tribunal said that cost savings would go initially to Qantas and its shareholders, but that they are "capable of being passed through in the form of a potential lowering of fares, or a delay in increasing fares." Which is to say, anything is possible. The question is what is probable.

80 We can perhaps put it no better than it is explained by Tourism New Zealand in a moment of thoughtful candour. Tourism New Zealand (the Government tourism agency) is not an organisation given to commenting publicly on matters of public affairs, but the following appeared in its publication "Regional Rap May 2006":

> *The industry is currently considering the impact of Air New Zealand and Qantas code-share arrangements. This will decrease the number of weekly trans Tasman flights operated by the two airlines from 242 to 219, a decrease of approximately 10%. With both carriers signalling an increase in load factors* ***it appears inevitable that airfares will increase and that few seats will be available at peak demand periods****. (emphasis added)*

81 In short, average fares will increase dramatically as seats are reduced and inventory becomes jointly managed to maximise yield per ASK in a less competitive market. It is also likely that advertised fare levels in each category will increase significantly above those under any of the counter-

factual scenarios. That is, the airlines will enjoy an increase not only in yield per ASK (through higher load factors) but also an increase in yield per revenue passenger kilometres (RPK) through higher average fares.

82 Based on fares that prevailed in the past on the Tasman, prices could increase not just significantly but dramatically. There have been periods when travellers faced paying 50% - 100% more than they do today.

83 Wellington Airport is unable to determine what the applicants say will actually happen to prices because sections of their proposals on prices have been withheld.

84 However, we are confident of two outcomes:

84.1 Fares within each category will over time be set at much higher levels than if one of the counter-factual scenarios applied. The minimal competition from other players will be insufficient to prevent this happening.

84.2 The availability of fares in more affordable categories will reduce markedly particularly over peak periods of travel, pushing people into higher and higher fares.

WHAT IS YOUR VIEW ON BARRIERS TO ENTRY AND EXPANSION?

Previous statements

85 In its consideration of the previous, more comprehensive Alliance the New Zealand Commerce Commission, in October 2003, identified two significant barriers to a potential Tasman market entrant - being the impact of the airlines' combined loyalty programme and the potential response of the incumbents to any newcomer. The Commission was satisfied however that there was no evidence that a new entrant would have any difficulty obtaining suitable landing slots from which to fly Tasman sectors.

86 With regard to the combined loyalty programme, the Commission found that the deterrent effect would be less pronounced on the Tasman than in the New Zealand main trunk because of the lower proportion of business travellers (31% as against 56%). It did note however that the greatest impact on the Tasman would occur on the Wellington to Sydney route where 39% of travellers have business purposes.

87 Incumbent response to a new entrant on the Tasman was seen as a formidable barrier. The Commission found that the Alliance would give a greater ability to recoup losses arising from strategic over-capacity than the airlines acting independently would have.

88 The New Zealand High Court doubted that either frequent flyer programmes or incumbent response should properly be categorised as barriers to entry so much as "limitations on expansion". It observed that:

> *A feature of Australasian airline markets has been the inability of new entrants to consolidate their position. With the sole exception of Virgin Blue, new entrants over recent years have failed to build significant market share and have exited in the short to medium term. This suggests there are forces at work which may not be fully understood and which affect the ability of an entrant to achieve sustained entry.*

89 By contrast, in Australia the Tribunal in October 2004 focused on Pacific Blue's own claim that it would be in a strong position to enter and expand on any trans-Tasman city links (para 318); although it also recognised (para 324) that the surplus capacity on certain trans-Tasman routes may delay Pacific Blue's plans for entry and expansion on those routes. More specifically, the Tribunal found (para 327) that there are no significant barriers to entry or expansion on trans-Tasman routes facing Pacific Blue, or indeed, for that matter, Emirates. In particular, the Tribunal noted that claims that there were structural barriers – including loyalty programmes – were unsupported by the facts.

90 The Tribunal observed that Virgin Blue had established a significant Australian presence, having captured around 30% of the domestic Australian market in less than 3 years. While acknowledging that the Tasman had generally been more competitive than the Australian domestic market, the Tribunal was clearly influenced by the prospect of further entry and expansion by Pacific Blue.

Market experience since the last proposal

91 The passage of a further 18 months since the Tribunal's decision has demonstrated the danger in extrapolating Australian domestic experience on to trans-Tasman routes; and, more particularly, across the Tasman. The fact is that Virgin/Pacific Blue simply does not have the same omnipresence in New Zealand as in Australia. There are few flights available; they operate at limited frequencies; and they are to relatively few destinations. Brand recognition serves little purpose if not matched by actual availability.

92 That availability continues to be constrained by the same "forces" as the New Zealand High Court recognised. More importantly, that limited availability of flights will continue unless and until Pacific Blue develops the confidence, and is incentivised, to expand its operations at the New Zealand end.

93 But, none of that will happen in an environment when the two incumbent airlines have been officially sanctioned to combine their resources against it. The applicants' declared rationale for the TNA, of course, is to respond to the competitive challenge from Pacific Blue (and Emirates). Threat of incumbent response already constitutes a substantial limitation on Pacific Blue's expansion, especially at the New Zealand end. Both Qantas and Air NZ have systematically disciplined the market in recent years, signalling to the market that any expansion will be met with increased capacity. Market participants know the threat of incumbent response is real and not theoretical, and complaints have been made to the competition regulators on both sides of the Tasman. Allowing a combined response from Qantas and Air NZ would be fatal to any prospect of expansion by Pacific Blue or others.

94 The applicants' main point on barriers to entry is that there is little to stop other airlines entering new routes and "cherry picking", and that this was a view taken by the Australian Competition Tribunal.

95 At the time, the Australian Competition Tribunal was relying on only a short period of participation in the market by Pacific Blue and Emirates. It was encouraged to believe that "the worst is yet to come" in terms of competition. It has often been said that competition must be viewed as a process rather than a snapshot. We now have two years of actual observations to show that the picture provided to the Tribunal was quite wrong.

96 Emirates is constrained by being a long-haul player with long-haul equipment. It relies on having aircraft on the ground in Australia and has simply not found opportunities to expand. In fact, where it entered a new route, it did so by withdrawing from another. It is most unlikely to make a decision on flying to Australia from Dubai based on an opportunity for more trans Tasman flying.

97 Similarly, all the 2004 predictions of Pacific Blue becoming a major player on the Tasman and domestically in New Zealand have proven to be dramatically over-stated. In fact, they were just wrong. In particular, there has been no shift of aircraft from the Australian domestic market to the Tasman, as predicted. Pacific Blue is a subsidiary of Virgin Blue. It has the equivalent of two aircraft operating on the Tasman. It has another aircraft but it operates on other international routes between Australia and the Pacific Islands. It has become clear that participation on various Tasman routes is subject to aircraft availability, and even demand from Pacific Island routes can constrain growth on the Tasman. For example, when Pacific Blue withdraw from the Sydney-Wellington route, it was in large part explained by the desire to enter the Auckland market, but the inability to do so unless aircraft were taken from another part of the market.

98 Constraints on Pacific Blue's participation on Tasman routes extends not only to Pacific Island routes, but also to Australian domestic routes. Virgin's ability to pull aircraft out of domestic operations is highly constrained by the entry of Jetstar in the Australian domestic market. Jetstar was established specifically in response to Virgin Blue. It would be highly unlikely that Virgin would withdraw from parts of the hard won and core domestic market in the face of a growing, successful and well resourced Jetstar. It is equally unlikely that they would take initiatives to grow their fleet with a period of recent share price instability, in order to expand in a trans Tasman market already dominated by Qantas and Air New Zealand (and will be even more dominated if authorisation is given).

99 In short, Pacific Blue is a welcome player on the Tasman, but it has its hands full elsewhere.

100 The suggestion by the applicants that other airlines can "cherry pick" should be rejected. The two applicants have a large combined fleet at their disposal comprising 747-400s, 747-300s, 777s, 767-300s, 737-800s, 737-400s and A320s. They operate on all routes with dominant shares in all markets. They are able to incrementally intensify or reduce their market presence at will and to swap equipment. By contrast, the other players have a limited number of aircraft and equipment types. They operate only on selected markets. They publish schedules and cannot flick from one route to the other at will.

101 It has even been put by Auckland Airport that this code-share will increase competition by opening up landing slots. The applicants themselves say that there is no barrier to entry arising from landing slots.

WOULD EMIRATES, PACIFIC BLUE AND OTHER CARRIERS CONSTRAIN PRICE, CAPACITY AND SCHEDULING DECISIONS?

102 For the reasons already stated above, no - except perhaps on very select routes and then the constraint will be partial, at best. This is borne out by the fact that the airlines have already openly acknowledged that they *will* withdraw capacity. They have also raised prices regularly over the past year. In doing so, they obviously feel no constraint.

WHAT IS THE COUNTERFACTUAL?

103 As mentioned elsewhere in this submission, Wellington Airport accepts that if the application is not authorised, Qantas and Air New Zealand may individually make immediate decisions about current prices and supply on some routes based on their own strategy and assessment of potential route profitability, network and brand. However, the likely medium term counter-factual is more important and possibly more complicated. It may bring significant benefits to consumers that would not otherwise emerge.

104 The applicants have consistently claimed that, without authorisation, the consequences will be dire and that there are no alternatives. But Qantas and Air New Zealand are highly professional and successful companies. They are extremely unlikely to simply allow their businesses to be damaged if the authorisation is not granted. Like most businesses they will adapt, and in large part have already started to do so, albeit that a competitive malaise must surely develop between the parties when arrangements such as the Alliance and the code-share are being developed and negotiated over a prolonged period (at least the last four years).

105 Until now, a great deal of effort within the two airlines has been focused on an arrangement between them. However, if the authorisation is not granted it is likely that their efforts will individually turn to other strategies. Indeed, when the Qantas-Air New Zealand Alliance was rejected by the NZ High Court, Qantas' CEO Geoff Dixon was quoted as proclaiming it "dead". It is very unlikely that at that point, Qantas and Air NZ did not consider a range of alternatives that they are yet to pursue. The current application is but one of those options.

106 Wellington Airport claims no special access to the internal deliberations or views of Qantas, Air NZ or other airlines. However, from observing other markets, including the Australian domestic airline market and the Tasman itself, some of the following possibilities (or combinations of them) may emerge:

Arrangements with other airlines

106.1 Air NZ in particular has argued that it needs an arrangement on the Tasman with an Australian airline. The issue with the current application is that the proposed arrangement is with the other major competitor, Qantas. It is possible that Air NZ could pursue an arrangement with another airline without the negative consequences of the current proposal.

106.2 In the case of Virgin Blue, an arrangement with Air NZ could be even more extensive than the TNA in that, in addition to the various Tasman markets, it could involve the domestic networks of Virgin (in

Australia) and Air NZ (in NZ). It is worth noting that there are changes in control at a parent company level that may allow such proposals to be revisited, even if they have been dismissed in the past.

Further development of lower cost product and brands by each airline

106.3 In other airline markets, including the Australian domestic market, there has been an acceptance that competition and lower fare environments will be a permanent feature of short haul routes. That is, those markets have been transformed by airlines offering high frequency, high convenience, affordable prices and a product to meet every part of the market. This is certainly the case in Europe and it is increasingly the case in other regions. Airlines of this type have a specific strategy of low costs and stimulating new markets through affordable fares, direct services and new routes.

106.4 In Australia, there was a major shift with the entry of Virgin and then Jetstar. Although customer acceptance of Jetstar has been mixed on some Qantas routes, it was a very positive initiative, well executed and has proven highly successful. Few would like to see Jetstar and Virgin disappear from the Australian domestic scene. At the same time, Qantas remains a highly valued airline for a large body of travellers. The Australian domestic market has demonstrated a demand for a variety of products and airline models.

106.5 On Tasman routes, the transformation is far from complete, although there have been some halting moves toward new short haul models:

- Air NZ started Freedom in 1996 in the face of competition from Kiwi Air. Freedom has been a positive force in many ways, but has not developed to the extent of other low cost leisure carriers and struggled to get brand presence in Australia. Freedom has largely been integrated back into Air NZ.

- Virgin was welcomed onto some trans Tasman markets in 2004, based in Christchurch. However, after more than two years, they have entered the market in a reasonably limited way. It remains a relatively small player compared to its presence in Australian domestic markets and compared to the applicants on the Tasman.

- Air NZ introduced Tasman express fares in late 2003 and Qantas did the same, but this reflected a reaction on fares rather than a permanent shift in underlying costs.

- Air NZ has been taking steps to address its costs and in some cases this has required some hard decisions. They would no doubt argue that this application is part of that process. But transformations to low cost environments are not achieved through anti-competitive arrangements.

- Jetstar entered the Christchurch market in December 2005 and was very welcome. Jetstar has made it quite clear that, for the time being, it will only serve Christchurch. This is different to the experience of low cost carriers in other markets, including Australian domestic markets where Jetstar and Virgin have opened up routes previously unavailable to consumers. In the absence of the TNA, Jetstar might be expected to enter more markets (which may explain some of the enthusiasm for the TNA by at least one of the applicants).

106.6 However, there is unlikely to be a full and permanent shift to new models for short haul travel on the Tasman while the two major players pursue an arrangement between themselves. That is, we will see a fuller transformation and diversification of product when Qantas and Air NZ are liberated from any sense of competitive inactivity.

Unilateral Actions to Improve Performance on the Tasman Markets

106.7 It is open to airlines to take unilateral actions in accordance with their own assessment of the potential passenger markets. If the judgement of those who would withdraw capacity or put up prices is correct, their competitors will probably do the same. If not, then the arguments put for the authorisation are flawed and it should not proceed.

106.8 We note that the applicants have ruled out unilateral action as their network may be considered inferior and that their passengers would "spill" to the other applicant or other competitors. This is no different to any other market. However, this suggests that the other airline would not commensurately reduce capacity and therefore that their judgement of the market is different. In other markets, this would be considered the right result.

106.9 As we have noted elsewhere, the applicants have a number of measures available to them to add or reduce capacity without withdrawing from routes or diminishing their network coverage.

Proposals for more limited arrangements between Qantas and Air NZ

107 It is also possible that the applicants will continue to focus on an arrangement between them, but of a more limited nature. This may include a small number of routes where there is some level of genuine competition. There are no such routes out of Wellington, and even in larger markets like Auckland, not all routes would qualify. If that were the alternative pursued, some very precise controls would be required to avoid diminution of competition in other markets, and any authorisations would need to have regular sunset clauses to revisit the markets in question (rather than periods of five years as sought by the applicants).

WHAT ARE THE DETRIMENTS?

108 The key detriments flow from the fact that Qantas/Air NZ collusion on trans-Tasman routes will result in higher prices and fewer passengers. Most directly, this means Australian and New Zealand consumers will lose. Travellers will pay more than they have to, and more than they do now, and more than they would under other scenarios in the counterfactual. Further, some travel will no longer occur, significantly detracting from consumer welfare.

109 There will be secondary impacts in related markets in Australia as well as New Zealand. Most obviously, those markets for the provision of other services to Trans Tasman travellers and those firms which rely upon air carriage of perishable and other goods.

110 In addition, the idea of sharing revenue (but retaining independent responsibility for reducing costs) would seem to incentivise sub-optimal gaming such that both airlines will be looking to ensure that the other airline incurs the expense of carrying its passengers. This particular aspect of the proposed TNA is highly distortionary and therefore likely to give rise to significant additional detriment.

111 It is also likely that service levels will diminish. The declared intention of the applicants is to spread schedules and increase the number of direct routes to new destinations. However, it goes against experience that less competition leads to better service and more options. Usually the opposite is observed.

112 In particular, it seems unlikely that under the proposal Jetstar will enter new routes to regional centres, as Freedom has done on the Tasman for many years and Jetstar has done in Australia. The TNA dramatically decreases the likelihood that new regional routes will emerge (that would otherwise benefit consumers in those areas).

113 There are longer term detriments also. Both Australian and New Zealand governments have emphasised the importance of an open economy, export-led growth and "connectedness" with a rapidly globalising world. Within that context, both governments have recently re-energised the Closer Economic Relationship between Australia and New Zealand. New Zealand is a significant destination for Australian exports and foreign investment.

114 On the weekend of 6-7 May 2006, a forum of businesses and unions was conducted in Auckland to promote increased harmonisation between Australia & New Zealand. One of the strong themes to come out of that forum was that Australia and New Zealand need to work more closely to promote the economic potential of businesses in those two countries. It is not our understanding that this was intended to mean that Australian and New Zealand businesses should form anti-competitive arrangements or adopt a protectionist approach against companies from other parts of the world.

115 Instead, we understood the message from that forum to mean that Australian and New Zealand businesses should be in a position to participate and invest as much as possible in each other's markets, without artificial constraints and costs of doing business.

116 We support that goal. However, we have a concern that the arrangement proposed by the applicants will in part diminish the effectiveness of efforts to promote cross-border business and trade. In particular, we fear that it will drive up the costs of doing business by increasing costs of travel and air freight significantly and reduce the ease with which business people will be able to operate across Australian and New Zealand markets.

117 The arrangement itself appears to be contrary to the original policy intentions to liberalise aviation markets between the two countries.

118 This proposed collusion makes it harder for Australia and New Zealand to move in the direction identified by their governments as being in the long term interests of both countries.

WHAT IS THE COLLATERAL DAMAGE FOR OTHER MARKETS?

119 The applicants identify affected markets as comprising only:

119.1 air passenger services between Australia and New Zealand (the Tasman routes);

119.2 Tasman air freight services.

120 Management of the Tasman Network is to be undertaken by a Committee (comprising 3 members appointed by each applicant) the functions of which include - but are not limited to - the following activities:

120.1 setting strategic objectives for the Tasman Network, including as to scheduling, pricing, passenger processing, code sharing, frequent flyer programmes, lounge and check-in facilities at airports included in the Tasman Networks, co-ordinating in-flight product standards and marketing plans;

120.2 ensuring optimisation of the Tasman Network schedule;

120.3 ensuring coordination between each of the applicants with respect to the above activities; and

120.4 assuming responsibility for decisions that have a material impact on the base revenue including aircraft type and configuration changes and all capacity additions, reductions and deployments.

121 While those activities relate specifically to the trans-Tasman operations of the applicants there is an obvious competition risk here - namely, that there will be "leakage" of that co-operation into other markets.

122 Connectivity is said to be of vital importance to all airlines, but especially network carriers. Involvement in the scheduling and pricing, and knowledge of the loading and profitability, of all Qantas trans-Tasman flights must give Air New Zealand unique insight into Qantas' operations at the point where those passengers arrive in New Zealand. While Air New Zealand and Qantas may notionally "compete" with each other for those passengers who seek to fly on to other New Zealand designations, they will do so with a substantial information advantage over other carriers - such as Origin Pacific - who might also seek their custom.

123 Similarly in Australia, Qantas will have a unique advantage over other Australian carriers competing for arrivals from New Zealand.

124 Even with complete purity of purpose on everyone's part, the applicants will be significantly advantaged within their respective domestic markets by the scheduling, operational and financial information that flows to them from the TNA. But, of course, the applicants will not be incentivised to compete too vigorously against each other in those markets excluded from the TNA. For Air New Zealand in particular, having a benign rival "contesting" its home markets may be much more comfortable than having an hostile one. Qantas, for is part, may be hesitant to attack the profitable main trunk route within New Zealand if it would harm its TNA partner to the extent that the TNA were put at risk.

125 Put bluntly, the real price of combining on the Tasman to drive off Pacific Blue and Emirates, may well be forbearance within each other's home markets.

126 Such forbearance of course does not require overt collusion or understanding - simply each applicant acting in what it perceives to be its own self interest, but that incentive to forebear would not be present without the TNA.

WILL PUBLIC BENEFITS FLOW?

127 In short, no. The purpose of the application is not to generate public benefit - it is airline profit. There is nothing wrong with airlines making a profit in a competitive market, but the airlines claim they wish to avoid the waste of excess capacity and seek an extraordinary remedy. The lack of evidence for the excess capacity claim is discussed above. Even on its own terms, however, this simply means restricting supply and so effectively raising price. Indeed, joint setting of prices would be authorised. This will cut travellers out of the market - consumer and business travellers alike. That harm will be structural and therefore permanent.

128 The co-ordinated scheduling can only bring benefits at the margin as there is limited scope for increased frequency. In any case, there is no reason to expect that these scheduling changes will remain indefinitely .

129 The proponents argue that one of the great benefits of the TNA is that there will be less wingtip to wingtip flying and more spreading of schedules. Given a choice between genuine competition on one hand and a promise of coordinated schedule spreading (with collusion on prices) on the other, most people would opt for competition.

130 The proponents also argue that customers will get more choice through being able to book seats on each other's flights. Customers can already do that by going to the website of the airline of their choice.

DIFFERENCES BETWEEN AUSTRALIA AND NEW ZEALAND

131 The TNA is subject to 10 conditions precedent, including authorisation by the New Zealand Minister of Transport, or her delegate, under sections 88 and 89 of the New Zealand Civil Aviation Act. Section 91 of that Act provides that nothing in sections 27 to 29 of the New Zealand Commerce Act shall apply to the negotiation or provisions of an arrangement so authorised.

132 Crucially, however, authorisation by the New Zealand Minister - even if given - may not oust competition concerns in New Zealand - or exposure of the TNA to the Commerce Act.

Minister's powers are limited

132.1 The New Zealand Minister can only authorise provisions under the Civil Aviation Act in so far as they relate to the fixing of tariffs, or the fixing of capacity, or any combination thereof. Some aspects of the TNA, e.g. revenue sharing - go way beyond that.

Minister must use powers for proper purpose

132.2 Collusive capacity and cost reduction are not relevant purposes under the Civil Aviation Act, and the New Zealand Minister cannot use her exemption powers to endorse these purposes.

Exclusion is limited

132.3 The effect of authorisation under the Civil Aviation Act is only to exclude sections 27 to 29. The airlines' conduct will remain exposed to sections 36 and 36A of the Commerce Act. While these sections generally relate to unilateral conduct by a person having a substantial degree of market power, the term "person" includes an association of persons. Although conduct authorised under the Commerce Act is excluded from the application of section 36 and/or section 36A, arrangements authorised by the Minister under the Civil Aviation Act would remain exposed.

Minister's authorisation may be revoked at any time

132.4 Authorisation under the Civil Aviation Act may be revoked at any time by the New Zealand Minister, without any of the procedural protections of the Trade Practices Act and Commerce Act. Further, there is no saving provision for conduct previously authorised but no longer.

133 Clearly, the ACCC has expertise in the Australian Trade Practices Act and its application and there are broad similarities with the New Zealand Commerce Act. But, as the recent report of the Australian Productivity

Commission identified, substantial differences do exist between the two competition regimes.

134 For example, there are now significant differences between the wording of section 45 of the Trade Practices Act – in respect of which authorisation is being sought – and section 29 of the Commerce Act.

Any authorisation must be tagged

135 The ACCC must act to enhance the welfare of Australians, not New Zealanders. A striking illustration of this difference is the respective objects of the two Acts. The object of the Trade Practices Act, and the primary function of the ACCC, is to enhance the welfare of Australians through the promotion of competition. The benefits it must have regard to are the benefits to Australians – not the benefits to New Zealanders or trans-Tasman comity.

136 Conversely, the Commerce Act, and the New Zealand Commerce Commission, are there to promote competition for the long-term benefit of consumers within New Zealand. The benefits they must look for are the benefits to New Zealanders.

137 Any determination by ACCC must be circumscribed by those fundamental limitations. As should the applicants' ability to rely on the ACCC's determination were the ACCC to authorise the TNA. To protect against a confusion that was evident in some of the public commentary in the previous process, it will assist if the ACCC clearly states it has considered the competition impacts on the Australian public but not the New Zealand public.

SCHEDULE 1

Trans-Tasman City Pairs - Weekly Frequencies by Airline (Auckland, Christchurch and Wellington only)

Auckland	Services/wk
AKL - SYD vv	5 airlines
Emirates	7
Pacific Blue	no service
Lan Chile	4
Aerolineas Arg.	3
Total Competition	14
Air NZ	34
Qantas	37
Total Code Share	71
Total Services	**85**
AKL - BNE vv	6 airlines
Emirates	7
Pacific Blue	6
Garuda	2
Royal Brunei	3
Total Competition	18
Air NZ	18
Qantas	10
Total Code Share	28
Total Services	**46**
AKL - MEL vv	3 airlines
Emirates	7
Pacific Blue	no service
Total Competition	7
Air NZ	14
Qantas	14
Total Code Share	28
Total Services	**35**
AKL - OOL vv	2 airlines
Emirates	no service
Pacific Blue	2
Total Competition	2
Air NZ (Freedom)	6
Qantas	0
Total Code Share	6
Total Services	**8**

Christchurch	Services/wk
CHC - SYD vv	4 airlines
Emirates	7
Pacific Blue	5
Total Competition	12
Air NZ	14
Qantas/Jetstar	14
Total Code Share	28
Total Services	**40**
CHC - BNE vv	3 airlines
Emirates	no service
Pacific Blue	8
Total Competition	8
Air NZ	8
Qantas/Jetstar	7
Total Code Share	15
Total Services	**23**
CHC - MEL vv	3 airlines
Emirates	no service
Pacific Blue	4
Total Competition	4
Air NZ	8
Qantas/Jetstar	7
Total Code Share	15
Total Services	**19**
CHC-OOL vv	2 airlines
Emirates	no service
Pacific Blue	no service
Total Competition	0
Air NZ (Freedom)	3
Qantas/Jetstar	2
Total Code Share	5
Total Services	**5**

Wellington	Services/wk
WLG-SYD vv	2 airlines
Emirates	no service
Pacific Blue	no service
Total Competition	0
Air NZ	12
Qantas	14
Total Code Share	26
Total Services	**26**
WLG-BNE vv	3 airlines
Emirates	no service
Pacific Blue	3
Total Competition	3
Air NZ	6
Qantas	3
Total Code Share	9
Total Services	**12**
WLG-MEL vv	2 airlines
Emirates	no service
Pacific Blue	no service
Total Competition	0
Air NZ	7
Qantas	7
Total Code Share	14
Total Services	**14**
WLG-OOL vv	1 airline
Emirates	no service
Pacific Blue	no service
Total Competition	0
Air NZ (Freedom)	2
Qantas	0
Total Code Share	2
Total Services	**2**

AKL-ADL vv	2 airlines
Emirates	no service
Pacific Blue	no service
Total Competition	0
Air NZ	3
Qantas	3
Total Code Share	6
Total Services	**6**

CHC-ADL vv	-
Emirates	no service
Pacific Blue	no service
Total Competition	0
Air NZ	0
Qantas	0
Total Code Share	0
Total Services	**0**

WLG-ADL vv	-
Emirates	no service
Pacific Blue	no service
Total Competition	0
Air NZ	0
Qantas	0
Total Code Share	0
Total Services	**0**

AKL-PER vv	1 airline
Emirates	no service
Pacific Blue	no service
Total Competition	0
Air NZ	6
Qantas	0
Total Code Share	6
Total Services	**6**

CHC-PER vv	-
Emirates	no service
Pacific Blue	no service
Total Competition	0
Air NZ	0
Qantas	0
Total Code Share	0
Total Services	**0**

WLG-PER vv	-
Emirates	no service
Pacific Blue	no service
Total Competition	0
Air NZ	0
Qantas	0
Total Code Share	0
Total Services	**0**

AKL-CNS vv	1 airline
Emirates	no service
Pacific Blue	no service
Total Competition	0
Air NZ	3
Qantas	0
Total Code Share	3
Total Services	**3**

CHC-CNS vv	-
Emirates	no service
Pacific Blue	no service
Total Competition	0
Air NZ	0
Qantas	0
Total Code Share	0
Total Services	**0**

WLG-CNS vv	-
Emirates	no service
Pacific Blue	no service
Total Competition	0
Air NZ	0
Qantas	0
Total Code Share	0
Total Services	**0**

Note 1: Thai Airways pulled off Tasman since last Alliance proposal

Note 2: City pairs with Hamilton, Palmerston and Dunedin not counted (zero competition)

Note 3: Queenstown not included - only QF and NZ services

Note 4: 15 routes above. Routes to NZ regional cities account for balance of 25 trans Tasman routes

Key:

SYD	Sydney
BNE	Brisbane
MEL	Melbourne
OOL	Gold Coast
ADL	Adelaide
PER	Perth
CNS	Cairns
AKL	Auckland
CHC	Christchurch
WLG	Wellington