

3 August 2012

Dr Richard Chadwick
General Manager, Adjudication
Enforcement and Compliance Division
Australian Competition and Consumer Commission
GPO Box 3131
Canberra ACT 2601

Dear Dr Chadwick

Qantas Airways Limited & Jetstar Airways Pty Ltd – Authorisation – A91314 & A91315

Thank you for providing Virgin Australia with the opportunity to comment on the application for authorisation by Qantas and Jetstar Airways in respect of the Jetstar Pan-Asia Strategy (**Application**).

Virgin Australia generally supports airline alliance proposals where there is a clear commercial rationale which will deliver benefits to consumers (with evidence supporting these benefits) and where there is no material adverse impact on competition.

Virgin Australia is concerned that, given the broad and uncertain nature of the Application, it is not possible to satisfactorily assess the competitive effects, or to adequately weigh the public benefits and detriments, associated with the proposed conduct.

Integration of Jetstar LCC operations and the proposed conduct

It appears the essence of the conduct proposed in the Application is to establish an integrated Jetstar operation which will encompass the provision of domestic and international air passenger services under the Jetstar brand, including between Australia and destinations in Asia.

The scope of the proposed authorisation as currently stated in the Application and, in particular, how that is related to and required in order to establish an integrated Jetstar LCC network, is unclear. Authorisation is being sought to operate as a single, fully integrated organisation by fully coordinating airline and associated operations and activities in the Asian region (ie, coordination through joint network and scheduling, sales and marketing, pricing and inventory, product distribution, frequent flyer and loyalty programs, IT, purchasing and procurement, and customer service activities).

Authorisation is being sought, as described in paragraph 5.1, to apply between:

- Each and all of Qantas, Jetstar Airways, Jetstar Asia, Jetstar Pacific, Jetstar Japan and Jetstar Hong Kong;
- each Jetstar joint venture and its local partner airline shareholder (where they have overlapping or potentially overlapping services), namely:
 - Jetstar Japan and JAL;
 - Jetstar Pacific and Vietnam Airlines; and
 - Jetstar Hong Kong and China Eastern Airlines.

- a Jetstar joint venture (including future unspecified joint ventures), its local airline shareholder and any other airline in the Jetstar Group (including Jetstar Airways) to the extent they overlap or potentially overlap.

The Application describes the proposed conduct in only general terms and does not provide any details on how it will be implemented or on the practical relationship between the various existing and future parties, with and without the authorisation. This makes it difficult to assess and comment upon the likely impact of authorisation of the Application. Further detail on the proposed conduct is necessary in order to assess the Application.

The scope of authorisation sought is unnecessarily broad and potentially uncertain

The scope of the authorisation is very broad and would appear to go beyond what is necessary to achieve the commercial case as argued. Qantas/Jetstar is seeking what appears to be an open-ended authorisation covering any Jetstar-branded operations together with coordination with FSA members, including any future Jetstar joint ventures, in respect of any air passenger services between Australia and Asia operated by these entities.

In particular:

- The Application states (at paragraph 5.6) that “*under the JVCA the parties propose to operate as a single, fully integrated organisation coordinating their operations and activities in the Asian region*”. These parties include each airline and joint venture described above, as well as future unspecified parties. Despite this, the Application states (at 5.19) that coordination will not take place between certain specified entities who are, nevertheless, parties to the agreement. It also states that strict ring fencing protocols have been implemented to ensure that there is no actual or potential coordination between any of these specified airlines, e.g. between Qantas and JAL.
- It is difficult to see how the Ring Fencing Protocol provided at Appendix E would sufficiently prevent such coordination occurring. Further, if this coordination is to be carved out from the scope of authorisation, it appears unnecessary for the Applicants to seek such a broad authorisation between so many parties. For example, it is unclear why Qantas Airways is a party to the proposed conduct and what role it would play in joint pricing and scheduling, for example with the Jetstar joint ventures. This is particularly so as it is a competitor, or potential competitor, to the FSA partners of the Jetstar joint ventures. If granted, authorisation should not be broader than what is necessary in order to achieve the stated commercial objectives.
- It is unclear why the integration of the relevant local partner FSAs, being JAL, Vietnam Airlines and China Eastern Airlines (particularly in respect of overlapping services with Jetstar Airways) is necessary to achieving the commercial objectives of the proposal, or what benefit this would bring for customers. The FSA partners of the existing Jetstar LCCs currently operate flights between Asia and Australia which compete, or potentially compete, with services operated by the Jetstar Group. Qantas/Jetstar is effectively seeking authorisation to fully cooperate (including by jointly making decisions in respect of scheduling, pricing and marketing) with its FSA competitors on unspecified actual or potentially overlapping services. This appears to go beyond the stated commercial rationale of the Jetstar Pan-Asia Strategy. Such a level of coordination between competitors on routes would likely result in an adverse effect on competition.
- The proposal contemplates the addition of future, unspecified Jetstar joint venture partner airlines as parties to the agreement for which authorisation is being sought. Virgin Australia considers that, if granted, authorisation of the proposed conduct as currently stated in the Application, has the potential to operate in an ambiguous and uncontrolled manner.

Specifically, it is difficult to see how a competition assessment, and a weighing of likely public benefit and detriment, can be conducted where the identity of the parties and the potential competitive overlap cannot be identified at the time of the Application. The Application states (at paragraph 4.35) that *“the Applicants will provide the ACCC with full details of any Future Jetstar Joint venture that becomes a party to the JVCA that is the subject of this application for authorisation”*. Such notification would not alleviate these concerns. Virgin Australia considers that authorisation should not be granted in circumstances when the scope of and the parties to the conduct cannot be identified and the effect of an authorisation cannot be adequately assessed.

Assessment of competitive effects

It is unclear from the Application the areas of actual and potential overlap between:

- each existing Jetstar joint venture and its local partner FSA (ie, JAL, Vietnam Airlines and China Eastern). Virgin Australia notes that section 5.1 of the Application states that authorisation is only sought for overlapping or potentially overlapping services with the FSAs; and
- each of Qantas, Jetstar Airways and Jetstar Asia and the above airlines. Virgin Australia notes that the Application seeks authorisation in respect of coordination between the Jetstar Group and the local partner FSAs (including any future relevant local partner FSAs) to the extent they overlap or potentially overlap.

Potential competitive overlap is particularly unclear given that the services of Jetstar Hong Kong and Jetstar Japan are unknown at this stage. Further, it is impossible to identify all the areas of actual and potential overlap between the services of the existing parties and potential future parties.

Virgin Australia considers that additional information is required before any assessment of the competitive effects of the Application can be made. In particular, the Application states (at paragraphs 5.17-18) that regulatory approval is needed because *“there is a risk that at least one of Qantas or Jetstar Airways is a potential competitor to any Existing Jetstar Joint Venture or any Future Jetstar Joint Venture or that at least one Existing Jetstar Joint Venture or Future Jetstar Joint Venture is a potential competitor to another Existing Joint Venture or Future Joint Venture”*. Despite this, the Applicants maintain that no anti-competitive detriment will result from the proposed conduct. The Application identifies some airlines between which there are currently no overlaps but does not provide any detail. Virgin Australia considers that further information is required about the extent of existing overlapping services and the scope of potential competition between the parties. We note that the Application is silent as to competitive overlap between Jetstar Pacific, Vietnam Airlines and the other parties.

Public Benefits

Virgin Australia notes that from a review of the Application and supporting submission, it is unclear how the proposed conduct will result in the claimed public benefits. In particular, it is unclear why the breadth of cooperation proposed is necessary in order to achieve benefits such as cost savings, an enhanced consumer experience and an expanded network. It appears that there is no clear link between the identified benefits and the conduct, as described in the Application. Further, the Application does not appear to include any evidentiary support for the claimed public benefits. For example, it is unclear how the proposed conduct will increase tourism and employment in Australia. Virgin Australia considers that further evidence is required in order to properly assess the claimed public benefits.

In particular, increased competition and innovation has been listed as a public benefit that will arise from the proposed conduct. It is unclear whether this is as a result of, or despite, the proposed cooperation between the Jetstar joint ventures (and Jetstar Airways) and the relevant FSAs.

Given the current market position of the Qantas/Jetstar Group, it is difficult to see how an increase in its competitive position could result in meaningful and durable public benefits. In particular, we note that in 2011, Qantas/Jetstar had, overwhelmingly, the largest share of passenger traffic to and from Australia. It carried 26% of international passenger traffic. Its nearest rival, Singapore Airlines, carried 9% of international passenger traffic.¹ Similarly, according to 2011 DIMIA embarkation /disembarkation data:

1. the Qantas/Jetstar Group carried 76% of passengers between Australia and Japan and when the other proposed parties to the authorisation are added, they collectively carried over 92% of passengers.
2. the Qantas/Jetstar Group carried 16.53% of passengers between Australia and Vietnam and when the other proposed parties to the authorisation are added, they collectively carried over 91% of passengers.
3. The Qantas/Jetstar Group carried 30.51% of passengers between Australia and Singapore and when the other proposed parties to the authorisation are added, they collectively carried over 32% of passengers.
4. the Qantas/Jetstar Group carried 28% of passengers between Australia and Hong Kong and 12.54% of passengers between Australia and China and when the other proposed parties to the authorisation are added, they collectively carried over 30% of passengers to China.²

Given Qantas/Jetstar's current market position, it is unlikely that any strengthening of its ability to compete would have pro-competitive benefits. Rather, there may be the potential for this to increase barriers to entry and, ultimately, to reduce customer choice.

Term of authorisation

The Application is for a term of 10 years. Virgin Australia considers that, if granted, authorisation should not be granted for such a long period. This is particularly so given the very broad terms of the authorisation including between such a large number of parties. As market and competitive dynamics can change rapidly, particularly in the Asian aviation market, it is appropriate that the competitive effects and public benefits of the alliance be tested after a shorter period of implementation than that proposed.

Other comments

Virgin Australia notes that the Application draws some parallels with the underlying purpose of authorised conduct engaged in by resources companies to supply export markets.³ The Application does not refer to any particular decisions, however Virgin Australia has taken this to refer to the applications for authorisation lodged by BHP Billiton and other related companies in respect of agreements relating to the extraction, blending and sale of iron ore from Western Australia.⁴ It is difficult to see how these decisions relate at all to the present Application, given that those

¹ BITRE, Statistical Report: International airline activity 2011, p 12.

² DIMIA Data (Overseas Arrivals and Departures) – May 2012 Ref: Q20110080

³ Application [8.8].

⁴ See, applications for authorisation A40091-A40095 lodged by BHP Billiton Minerals Pty Ltd (2004), and applications for authorisation A90981-A90983, lodged by BHP Billiton Ore Pty Ltd (2005).



authorisations were granted in respect of supply to export markets only. The present Application contemplates coordination on routes outside Australia, but also has the potential to impact on routes connecting to, and within Australia.

Please contact us if you would like to discuss any of the issues raised in this letter.

Yours faithfully

A handwritten signature in black ink, appearing to read "Adam Thatcher".

Adam Thatcher

General Counsel / Company Secretary