



Australian Government

Department of Infrastructure and Regional Development

Dr Richard Chadwick
General Manager, Adjudication
Australian Competition and Consumer Commission
23 Marcus Clarke Street
CANBERRA ACT 2601

Dear Dr Chadwick,

Virgin Australia and Etihad Airways Limited application for revocation and substitution of authorisations A91217 & A91248

Thank you for your letter of 13 August 2015. The Department of Infrastructure and Regional Development (the Department) welcomes the opportunity to provide a submission to the ACCC on the proposed alliance between Virgin Australia and Etihad Airways (Etihad).

The Department recognises it is a matter for the ACCC to determine the relative merits of arguments presented by the applicants on the public benefits and the effect on competition of the proposed alliance. However, to assist the ACCC in coming to a determination, this submission will provide contextual information on the relevant aviation markets, the air service arrangements which underpin them and the Australian Government's aviation policy.

Air services arrangements between Australia and the United Arab Emirates (UAE)

The Department notes there are no economic regulatory barriers preventing Australian or United Arab Emirates (UAE) airlines from increasing capacity in the Australia-UAE market. The *Agreement between the Government of Australia and the Government of the United Arab Emirates relating to Air Services*, done at Dubai on 8 September 2002, [2005] ATS 8, supplemented by the Memorandum of Understanding between aeronautical authorities signed in Jeddah on 11 December 2012 (together the arrangements) outlines the capacity entitlements of air services between the two countries. These air services arrangements currently allow designated airlines of the UAE to operate 154 services per week to major gateways and an unlimited amount to non-gateway airports. Australian carriers can also operate a total of 154 services per week (98 to Dubai, 49 to Abu Dhabi and 7 to Sharjah) between Australian Gateway Points and the UAE, using any type of aircraft. Airlines of both countries are able to serve any intermediate points and all beyond points. Of this allocation, UAE airlines operated 123 services and Australian airlines only 17 during the Northern Summer schedule of 2015.

The Memorandum of Understanding (MOU) between Australia and the UAE provides for designated airlines to conduct code share operations. Specifically, paragraph 19 states that, 'In operating or offering the agreed services on any segment or segments of the specified routes, any designated airline of each Contracting Party may enter

into code sharing arrangements, as marketing and/or operating airline, with any other airline(s)'.

Paragraph 18 of the MOU permits any designated airline of Australia fifth freedom rights to any point beyond the UAE. Accordingly, Australian airlines can operate to the UAE and beyond without entering into a code share arrangement or alliance. It is then a commercial decision for the individual airlines of each country to determine whether to utilise these rights by providing services.

The alliance between Virgin Australia and Etihad is consistent with the authority granted under paragraph 18 and 19 of the arrangements.

Status of the Market

Services operated by Virgin Australia comprise a very small portion of the Australia-UAE market, operating only 3 of the 140 weekly services between Australia and the UAE. The most recent data available for Virgin Australia indicates that in the 2014-15 financial year it carried 2.1 per cent of the total number of passengers discharged in the United Arab Emirates, including passengers who connected to a further overseas destination.¹ Of the total share of uplift passengers from Australia for UAE airlines, only 4.9 per cent of Emirates and 5.3 per cent of Etihad passengers nominate the UAE as their final destination, indicating the importance of the UAE as a 'hub' destination.²

As a result, the primary markets relevant for the purposes of this reauthorisation application are the operation of commercial air services between Australia and the United Kingdom, and between Australia and other destinations in the European Union (EU). According to 2015 passenger card data collected by the Department of Immigration and Border Protection (DIBP) approximately 28.7 per cent of passengers on Emirates flights from Australia cite the UK as their final destination. Other European destinations such as Italy (8.5 per cent), Germany (6.4 per cent) and France (5.9 per cent) also benefit from onward flights operated by Emirates. The origin-destination pattern of Emirates is mirrored by Etihad flights to and from Australia, with 23.9 per cent of passengers leaving or heading to the UK (plus an additional 10.4 per cent to and from Ireland). Virgin Australia carries only 2.5 per cent of passengers who nominate the UK/EU as their final destination.³

There are strong competitive forces in these markets. The 'hub' capacity provided by Middle Eastern airlines is subject to competition from several other major mid-point carriers operating in the Australia-Europe market, including major North and South-East Asian carriers such as Singapore Airlines (12.1 per cent of market share to the UK and 11.6 per cent to the EU) and Cathay Pacific Airways (7 per cent and 5.7 per cent respectively). The data suggests that there are a number of competitors servicing the Australia-UK/EU market which are capable of adding to or altering their services to respond to demand.

Qantas and Emirates remain the dominant carriers on routes from Australia to the UAE and onward to the UK and EU. Emirates carried 28.6 per cent of passengers to the EU to Qantas' 14.7 per cent, and also grew its share of UK passengers to 26.2 per

¹ Bureau of Infrastructure, Transport and Regional Economics, 'International Airline Activity Annual Publications: 2014'.

² Department of Immigration and Border Protection, 'Australian Passenger Card Data,' data supplied by Bureau of Infrastructure, Transport and Regional Economics 21 August 2015.

³ Ibid.

cent ahead of Qantas, which declined slightly to 17 per cent share.⁴ Qatar Airways was a new entrant to the market in 2010 and has been able to grow its share of the total international market served from Australia to 1.2 per cent, suggesting that competition will continue to grow on these routes.⁵

Australian Government Aviation Policy

The Australian Government's aviation policy is focussed on helping the aviation industry grow in an environment that is safe, competitive and productive. This includes providing improved opportunities for Australian carriers to access international markets and increasing competition and choice for Australian and foreign travellers on international routes to and from Australia.

In addition to the provision of own aircraft services, the international aviation marketplace benefits significantly from the ability of airlines to enter into commercial alliances and co-operative arrangements. This is particularly the case for airlines based in geographic regions which are not a natural 'hub' for airline services, such as Australia. As a result, a key Australian objective in negotiating air services arrangements is to ensure Australian airlines are provided the maximum possible flexibility to pursue commercial alliances.

The proposed reauthorisation of Virgin Australia and Etihad is, in the Department's view, consistent with the overarching objectives of the Australian Government's aviation policy. In our view, the alliance has benefited Australian consumers by enabling Virgin Australia to offer its customers better access to Virgin Australia's integrated 'virtual network', which is underpinned by commercial relationships such as the Etihad alliance.

Australian international airlines have historically been characterised by low profit margins, notwithstanding a recent turnaround in reported profits as a result of reduced fuel prices and efficiency measures. Noting Virgin Australia's low market share on these routes, we believe that Virgin Australia's ability to compete effectively with Qantas and Emirates would be enhanced if the alliance is reauthorised.

Thank you again for inviting the Department to provide a submission. I can be contacted on 02 6274 7739 should you wish to discuss this matter further or require any additional information.

Yours sincerely



Stephen Borthwick
General Manager
Aviation Industry Policy
Aviation & Airports Division

10 September 2015

⁴ Ibid.

⁵ Ibid.