



Australian Government

Department of Infrastructure and Regional Development

File Reference: 15/2107

Dr Richard Chadwick
General Manager
Adjudication Branch
Australian Competition and Consumer Commission
By Email

Dear Dr Chadwick

Proposed Joint Coordination Agreement between Qantas Airways Ltd and China Eastern Airlines Corporation Ltd applications for authorisation

I refer to the draft determination of the ACCC issued on 24 March 2015 proposing to deny authorisation of the proposed coordination agreement between Qantas Airways Ltd (Qantas) and China Eastern Airlines Corporation Ltd (China Eastern). The Department of Infrastructure and Regional Development (the Department) appreciates the opportunity to provide a further submission on the proposed agreement.

It is the view of the Department that, on balance, the proposed agreement is a positive for the Australian economy and is consistent with the Australian Government's aviation policy settings.

As outlined in our previous submission, the agreement would benefit Australian consumers by improving coordination of schedules and frequencies; sharing frequent flyer benefits between the two airlines; and allowing Qantas to offer its customers better access to destinations within China by reducing connection times for onwards flights from Shanghai. It would also result in added benefits by boosting Australia's tourism industry through increasing the ability for both airlines to market and sell tickets to Australian destinations.

The Department notes that the ACCC recognises that 'the primary area of competition for the purpose of assessing the Proposed Conduct is international air passenger transport services between Australia and China' and that it is 'appropriate to examine the likely effects of the proposed alliance on competition and rivalry on particular routes where necessary'. The Department suggests the draft determination is too narrowly focused on the Sydney-Shanghai route rather than the operations of the wider Australia-China market.

While the Department notes the evidence to suggest the Sydney-Shanghai route comprises relatively strong 'point to point' traffic, the commercial reality is that in any given market a hub airline will have significant market share on routes to and from that hub. This should not in itself prevent the formation of immunised alliances with other carriers when consumer benefits can be showed to outweigh competitive impacts.

The Department also contends the ACCC has overstated the impacts on the Sydney-Shanghai route, particularly when considered in the context of the existing competition on the route and the availability of one-stop services in the broader Australia-China market.

Air China is a direct competitor for Qantas and China Eastern on the Sydney-Shanghai route. Whilst its market share on the route has fallen from 23 per cent in 2010 to 17 per cent in 2014, the Department believes it is inappropriate to estimate Air China's competitive response entirely within a historical vacuum. If Qantas and China Eastern were to reduce or limit capacity on the Sydney-Shanghai route in an effort to increase yield and profitability, there are few barriers to Air China increasing their capacity if such a commercial opportunity emerged.

There is also substantial scope for competitive response from indirect services. A large number of airlines offer one-stop services between Sydney and Shanghai, including China Southern, Cathay Pacific, Singapore Airlines and Malaysian Airlines. These one-stop services are frequent, comparable to direct services in terms of product and price (or even cheaper in some cases) and, as the ACCC has indicated in its draft determination, the difference in travel time can be as little as one hour and forty minutes. While indirect flights only account for around 12 to 15 per cent of passenger traffic passengers, it would be reasonable to expect a greater proportion of passengers (particularly more price-sensitive leisure travellers) would elect to travel on indirect services should Qantas and China Eastern increase fare prices under the proposed agreement.

The Department expects that, together, the competitive pressures on both direct and indirect services would be sufficient to limit anti-competitive conduct on the Sydney-Shanghai route.

Additionally, the Department does not agree with the ACCC's implicit assertion in paragraph 232 of the draft determination that additional competition in the Sydney-Shanghai route may be hampered by capacity entitlements under the air service arrangements. The draft determination notes the recently negotiated air service arrangements provide a further 11,000 seats of additional capacity to October 2016 but suggests the Civil Aviation Administration of China will allocate this additional capacity to more underserved routes between Australia and China (i.e. not to the Sydney-Shanghai route). The implicit assertion is that there will be insufficient capacity to allocate to China Eastern, Air China or another Chinese airline to provide sufficient competition on the Sydney-Shanghai route.

The Australian Government's policy is to prioritise bilateral air service arrangements to ensure there is sufficient aviation capacity to meet future demand. Should Chinese carriers approach their capacity limits, the Government would review the air service arrangement to ensure consistency with this policy. It is also important to note the updated air service arrangements provide an additional 33,500 seats of capacity between Australian gateway airports and Chinese locations outside of Shanghai, Guangzhou and Beijing, further increasing opportunities for Chinese carriers to service Australian gateways from a variety of destinations.

In summary, the Department sees no reason to deny the proposed coordination agreement. The benefits that will flow to Australia's aviation industry, Australian consumers, the Australian tourism industry, and the Australian economy as a whole are exactly the benefits the Australian Government's aviation policy approach is designed to support.

The Department would be happy to discuss the contents of this submission with the ACCC as necessary.

Yours sincerely

A handwritten signature in black ink that reads "Stephen Borthwick". The signature is written in a cursive style with a prominent flourish at the end.

Stephen Borthwick
General Manager
Aviation Industry Policy Branch
8 April 2015