

Qantas Airways Limited (Qantas) and China Eastern Airlines Corporation Limited (China Eastern) – application for authorization – A91470 & A91471 (the Application)

Air China (CA) welcomes the opportunity to comment on the Application and, in particular, the ACCC's draft determination, published on 24 March 2015 (the Draft Determination).

CA's position

CA does not have a position as to whether the Application would result, or be likely to result, in a public benefit which outweighs the likely public detriment constituted by any lessening of competition as required by the *Competition and Consumer Act 2010 (Cth)* (the Act). CA considers that integrated alliances between airlines can bring significant benefits to passengers, to cargo customers and to airlines by creating synergies and efficiencies, enabling improved services and stimulating passenger demand which leads to increased tourism demand, benefiting tourism industries.

The purpose of this submission

In this submission, CA seeks to:

- (1) provide the ACCC with an understanding of CA's operations, in particular in relation to services to and from Australia;
- (2) describe the growth of Chinese outbound tourism;
- (3) make submissions on the Draft Determination in relation the China/Australia market or markets; and
- (4) to correct some statements in the Draft Determination referring to CA.

Air China

CA is one of China's largest airlines offering scheduled passenger and cargo services. Its corporate office and main operations base is in Beijing (Beijing Capital International Airport) but it has flight operations and a significant network across China. It is also a member of the Star Alliance.

CA is listed on the Hong Kong and London stock exchanges. CA's main shareholders are the China National Aviation Holding Company and China National Aviation Corporation (Group) Limited, both state-owned enterprises. They together own 53.37% of the shares in CA.

As at the end of February 2015, CA operated 326 routes to 160 cities in 33 countries, utilizing a fleet of 366 aircrafts.

Air China's operations in Australia

CA has been operating on routes between China and Australia for over 30 years and currently operates three routes, namely:

- Beijing/Shanghai/Melbourne;
- Beijing/Sydney (since December 2007);
- Shanghai/Sydney (since July 2014).

CA also used to operate Beijing/Shanghai/Sydney on an Airbus 330-200 with normally 5 weekly flights in the winter season and 4 weekly flights in the summer season. In July 2014, CA stopped this route and started operate two separate flights between Beijing/Sydney and Shanghai/Sydney. CA also increased its frequencies on Beijing/Sydney.

Similarly, CA will replace its current Beijing/Shanghai/Melbourne route by two direct flights from Beijing and Shanghai to Melbourne in June 2015. The table below summarizes CA’s current operations on Australia/China routes, and its short term plans. **[REDACTED – COMMERCIAL IN CONFIDENCE]**

Route	Aircraft	Current frequencies		Planned future frequencies	
		2014 W	2015 S	[REDACTED]	[REDACTED]
Beijing-Sydney	Airbus 330-200	Once daily	5 per week	[REDACTED]	[REDACTED]
Shanghai-Sydney	Airbus 330-200	4 per week	3 per week	[REDACTED]	[REDACTED]
Beijing-Shanghai-Melbourne	Airbus 330-200	5 per week	5 per week (29 Mar – 31 May)	[REDACTED]	[REDACTED]
Beijing-Melbourne (starting June 2015)	Airbus 330-200	N/A	4 per week	[REDACTED]	[REDACTED]
Shanghai-Melbourne (starting June 2015)	Airbus 330-200	N/A	4 per week	[REDACTED]	[REDACTED]

[REDACTED – COMMERCIAL IN CONFIDENCE]

Growth of outbound Chinese tourism

CA believes that the Application must be assessed having regard to the significant growth recently experienced in China's outbound tourism (Chinese tourists travelling abroad). This growth, of at least 18% year on year, is evidenced in the following table.¹

Year	Number of Outbound Tourists	Growth Compared to Previous Year
2010	57,386,500	
2011	70,250,000	12,863,500
2012	83,182,700	12,932,700
2013	98,185,200	15,002,500

The UNWTO predicts that China will generate 100 million outbound tourists worldwide by 2020.² This means that in just five years, the number of Chinese outbound tourists will have at least doubled. This significant growth is anticipated to include Chinese tourists travelling to Australia (and New Zealand). Chinese tourists accounted for 709,000 arrivals in Australia in the year of 2013.³ Research undertaken by Australian tourism authorities has stated that China is the largest single contributor to both the growth of inbound arrivals and inbound expenditure. In terms of visitor numbers, for the period 2012–13 to 2022–23, China is expected to contribute about 24% to the total growth. Further, about 40% of inbound Australian tourism expenditure will be sourced from Chinese tourists.⁴

This growth has been driving (and will continue to drive) a significant increase in aircraft capacity acquired by Chinese airlines and the construction of scores of new airports, including in second and third-tier Chinese cities.

Market Definition

The ACCC is aware that a detailed econometric analysis has been of assistance in assessments of previous proposed airline joint arrangements and identification of the market or markets likely to be affected. Much information to undertake such analysis is not available to CA at this stage.

¹ Statistics from China National Tourism Administration. <http://www.cnta.gov.cn/>

² <http://pub.unwto.org/WebRoot/Store/Shops/Infoshop/Products/1189/1189-1.pdf>

Please also find a UNWTO report in China outbound tourism market which can be purchased online: <http://asiapacific.unwto.org/publication/chinese-outbound-travel-market-special-insight-image-europe-destination>

³ Tourism Australia: *China Market Profile*, May 2014.

⁴ Tourism Research Australia, *Tourism Forecasts*, Autumn, 2014.

Nevertheless, CA is still well placed to form a view that the analysis should focus on competition on routes between China and Australia rather than on specific city pairs.

Flights to Australia originate from one of four major China-based gateways (Beijing, Shanghai, Guangzhou and Hong Kong), as well as increasingly from second tier cities. Alternatively, Chinese travelers fly to Australia from locations within China to a major gateway outside China (Singapore, Kuala Lumpur, etc). The vast majority of Chinese citizens do not have access to direct flights and must first fly to one of these gateways before an onward journey to an Australian destination. As a result, there is fierce competition within China between these gateways to attract these customers, not to mention competition from other hubs such as Singapore.

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From an inbound perspective (for Australian tourists travelling to China), tourists are likely to visit more than one city in China. A typical tour would include at the very least Beijing, Shanghai, Xi'an and Hong Kong. Australian tourists are indifferent as to where they start and end their journey.

Thus, from CA's experience, the market is characterized by competition between the major gateways. Prices applied on routes between one gateway and Australia are constrained by prices on routes between other gateways and Australia.

Air China's response in case of a price increase on Shanghai/Sydney

In its Draft Determination, the ACCC states that *“it is unlikely that Air China, the only other airline to operate direct flights on the route [Shanghai/Sydney], with significantly fewer frequencies and declining capacity (on a route which is growing), will provide a sufficient constraint to Qantas and China Eastern in the event that they decided to reduce or limit growth in capacity. Given its existing capacity on the route, any increase in capacity by Air China would have to be significant to constrain Qantas and China Eastern. The ACCC considers that any competitive response by Air China is unlikely to be sufficient to make a unilateral reduction or limitation in growth of capacity unprofitable for Qantas and China Eastern. Further, it may be in Air China's interest to raise its airfares to some extent in response to any increase in price/reduced capacity by Qantas and China Eastern”* (see paragraph 205 of the Draft Determination).

Further, the ACCC contents that it has *“also considered whether the alliance could increase the risk of coordinated conduct between [Qantas and China Eastern] and other carriers operating services on relevant routes. For example, the high level of concentration on the Sydney-Shanghai route arguably creates a strong incentive for [Qantas and China Eastern] and Air China to coordinate their conduct on this route, for example, through a common strategy to limit growth in capacity”* (see paragraph 233 of the Draft Determination).

CA never intended to decrease its capacity on Shanghai/Sydney. It has been operating the same aircraft (Airbus 330-200) with the same frequencies (5 weekly flights in the winter season and 4 weekly flights in the summer season) on Beijing/Shanghai/Sydney from 2010 to 2014 before it

stopped flying to Sydney via Shanghai. CA only slightly adjusted the frequencies occasionally in response to unexpected changes such as weather conditions. CA believes that its capacity on Shanghai/Sydney remained stable during that period of time. Instead of capacity decrease, CA was in fact trying to expand its overall capacity on Australian/China routes and offering a more competitive product by flying directly from Beijing or Shanghai to Sydney, instead of flying from Beijing via Shanghai. CA's apparent decrease in the share of total capacity could simply be because it did not expand as quickly as other airlines on this particular route.

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This being said, CA has the ability to increase capacity. It already has the necessary traffic rights and it has sufficient aircrafts and can convert existing slots at Shanghai's Pudong Airport to increase frequencies to Sydney. CA will have the incentive to increase capacity in response to an increase in fares, or if Qantas/China Eastern were to decrease capacity.

CA rejects the inference that it would have the incentive to engage in any form of collusion (even tacitly) with Qantas and China Eastern. More importantly, it would be unable to do so. Such an inference fails to have regard to the dynamics of competition in China. Tacit collusion is only possible when the market shares of the members of the oligopoly are symmetric. This is not the case here as the ACCC has noted it in Draft Determination: CA's market share on Shanghai/Sydney is much lower than Qantas/China Eastern's. CA therefore has a significant incentive to grow market share in the event Qantas/China Eastern were to increase prices/decrease capacity. In any event, CA does not believe that price increases are possible as passengers are able to switch to flights departing from other gateways.

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Annex 1: [REDACTED – COMMERCIAL IN CONFIDENCE]