



Australian
Competition &
Consumer
Commission

Draft Determination

Applications for authorisation

lodged by

Singapore Airlines Limited & Deutsche Lufthansa AG

in respect of

a Joint Venture Framework Agreement

Date: 15 September 2016

Authorisation numbers: A91542 & A91543

Commissioners:

Sims
Rickard
Schaper
Court

Summary

The ACCC proposes to grant authorisation to Singapore Airlines Limited and Deutsche Lufthansa AG to coordinate their operations pursuant to a Joint Venture Framework Agreement.

The ACCC proposes to grant authorisation for five years.

The ACCC will seek submissions in relation to this draft determination before making its final decision.

The applications for authorisation

1. On 20 June 2016, Singapore Airlines Limited and Deutsche Lufthansa AG (the **Applicants**), lodged applications for authorisation A91542 and A91543 with the ACCC. The Applicants and their respective passenger airline subsidiaries are seeking authorisation to coordinate their operations between Germany, Austria, Belgium and Switzerland (the **Lufthansa Home Markets**) and Singapore, Australia, Indonesia and Malaysia (the **Singapore Home Markets**) pursuant to a Joint Venture Framework Agreement (the **JVF Agreement**) and related agreements contemplated by the JV Agreement.
2. In summary, the JV Agreement provides for the following coordinated activities:
 - coordinating pricing, sales, marketing and inventory management for all routes between one of the Lufthansa Home Markets and one of the Singapore Home Markets; and
 - coordinating scheduling and capacity management, and sharing revenue on direct non-stop routes between the Lufthansa and Singapore Home Markets (currently being routes between Singapore and each of Munich, Frankfurt and Zurich, the **'revenue share routes'**).
3. On the revenue share routes the JV Agreement provides for the alignment of incentives through revenue sharing arrangements that result in metal neutrality. That is, on the revenue share routes, the JV Agreement enables Lufthansa and Singapore Airlines to be indifferent as to whether a passenger travels on a Lufthansa or Singapore Airlines operated services.
4. The JV Agreement only extends to services which operate between the Lufthansa Home Markets and the Singapore Home Markets. It does not extend to services within one of the home markets. For example Singapore – Sydney is not included since this route has both its origin and destination in the Singapore Home Markets. Similarly, Munich – London is not included since this route has its origin in a Lufthansa Home Market but no destination in a Singapore Home Market.
5. The Applicants submit that their networks are largely complementary with Singapore Airlines having its hub in Singapore and providing services to South East Asia and Australia, while Lufthansa has its hubs in Europe and provides services largely to European destinations. The Applicants' only overlapping operations are services between Singapore – Frankfurt, and Singapore – Zurich, which in some cases will form a segment of a service to or from Australia.
6. The Applicants submit that through the JV Agreement they will have access to different feeder networks which will result in greater potential to increase network

coverage and connectivity. They further submit that the purpose of the JVF Agreement is to enhance passenger services, facilitate improved capacity utilisation and inventory management and thereby improve their ability to compete with other major carriers.

7. The JVF Agreement does not extend to non-passenger services such as air cargo.
8. In addition to the JVF Agreement, the Applicants will also seek to pursue additional cooperation, where practicable, in relation to codeshare, frequent flyer and harmonisation arrangements. Authorisation is not sought for this additional coordination.
9. The JVF Agreement does not include coordination in relation to services offered pursuant to the codeshare arrangements the Applicants have in place with third parties and will not affect these existing codeshare arrangements. These codeshare agreements are discussed further where relevant below.

The Applicants

Singapore Airlines

10. Singapore Airlines, the flag carrier of Singapore, operates air passenger services across an international network of more than 60 destinations in over 30 countries with a fleet of over 100 aircrafts.
11. Singapore Airlines operates direct services between Singapore and the following Australian cities: Adelaide, Brisbane, Melbourne, Perth and Sydney. Singapore Airlines has also announced the introduction of direct services to Canberra (which will continue to, and return from, Wellington, New Zealand) four times per week from September 2016.¹ From its hub in Singapore, Singapore Airlines operates services to many destinations in Europe.
12. The services offered by Singapore Airlines between Australia and Europe are either:
 - operated wholly by Singapore Airlines (i.e. Singapore Airlines operates the aircraft on both the flight with an origin/destination in Australia and the connecting flight forming part of the service); or
 - operated partly by Singapore Airlines and partly by an airline with which Singapore Airlines has a codeshare agreement including for example, Lufthansa, Air New Zealand (where the codeshare relates to flights to/from New Zealand), or Virgin Australia (where the codeshare relates to services that include a Virgin domestic flight within Australia).
13. SilkAir (Singapore) Private Limited (**SilkAir**), a wholly owned subsidiary of Singapore Airlines, is also included in the JVF Agreement. SilkAir is the regional wing of the Singapore Airlines Group. It positions itself as a premium, short-to-medium haul regional carrier. SilkAir operates more than 350 weekly flights to 49 destinations in 13 countries from its hub in Singapore.

¹ *Capital Express' Service to Connect Singapore, Canberra and Wellington* (20 January 2016), http://www.singaporeair.com/en_UK/au/media-centre/press-release/article/?q=en_UK/2016/January-March/20Jan2016-1428/ Accessed: 1 August 2016.

Deutsche Lufthansa

14. Lufthansa is the parent company and largest single operating company in the Lufthansa Group. Apart from Lufthansa Passenger Airlines (which is the passenger airline business of Lufthansa), the Lufthansa Group's passenger airline service includes Austrian Airlines AG (**Austrian Airlines**), Swiss International Airlines Ltd (**Swiss International**) and low-cost airline Germanwings GmbH (**Germanwings**). Austrian Airlines and Swiss International are included in the JV Agreement, but Germanwings is not.
15. Lufthansa Passenger Airlines is the largest airline in Germany. It operates from the two biggest German hubs in Frankfurt and Munich and also operates long-haul flights from Dusseldorf. Lufthansa Passenger Airlines operates a global network of 235 destinations in 78 countries with a fleet of more than 400 aircraft.
16. Lufthansa does not operate any aircraft on a flight with an origin or destination in Australia. Therefore, services offered by Lufthansa between Australia and Europe are never entirely operated by Lufthansa. Rather, Lufthansa offers flights to Australia marketed under codeshare arrangements (including itineraries entirely operated by codeshare partners Thai Airways and United Airlines and itineraries partly operated by Lufthansa). Pursuant to a codeshare agreement with Singapore Airlines, Lufthansa codeshares on direct Singapore Airlines routes between Australia and Singapore. However, these codeshare flights are not marketed by Lufthansa on a standalone basis. They are only marketed as part of an Australia – Frankfurt itinerary.
17. Swiss International is the national airline of Switzerland and services 106 destinations in 49 countries from its hubs in Zurich and Geneva. Austrian Airlines is Austria's largest carrier and operates a global network of around 130 destinations from its hub in Vienna.

Star Alliance

18. Both Lufthansa and Singapore Airlines are part of the Star Alliance which coordinates customer service initiatives and harmonisation of passenger and baggage policies. The Star Alliance has over 25 member airlines. The Star Alliance's Corporate Plus, Conventions Plus and Meetings Plus programs which cover arrangements between Star Alliance members to jointly offer discounted fares, discounts on published fares and rebates to corporate customers and conference organisers under a single contract was authorised by the ACCC in 2012 until August 2020.²

Consultation

19. The ACCC tests the claims made by an applicant in support of its application for authorisation through an open and transparent public consultation process.
20. The ACCC sought submissions from a range of potentially interested parties including major competitors, suppliers, customers, relevant industry associations or peak bodies, consumer groups, state and federal government and relevant regulatory bodies.

² Determination: A91300-A91306, Air New Zealand on behalf of members of the Star Alliance in respect of Star Alliance's Corporate Plus, Conventions Plus and Meetings Plus Programs – 25 July 2012.

21. The ACCC did not receive any submissions.

Assessment

22. The ACCC's assessment of the JVF Agreement is carried out in accordance with the relevant net public benefit tests³ contained in the *Competition and Consumer Act 2010* (the **CCA**). In broad terms, the ACCC may grant authorisation if it is satisfied that the likely benefit to the public from the JVF Agreement would outweigh the likely detriment to the public, including from any lessening of competition.

Relevant areas of competition

23. The ACCC considers that the relevant areas of competition are international air passenger transport services, notably services between Australia and Europe (including the UK).
24. Within this area of competition, the ACCC has examined the likely effect of the JVF Agreement on competition and rivalry on particular routes (and route segments) where necessary. In particular, routes between Australia and the Lufthansa Home Markets.
25. The ACCC notes that most direct air transport services between Australia and the Lufthansa Home Markets are on routes transitioning through hubs in either Asia or the Middle East. In turn, this means there are many routes and combination of route segments between Australia and the Lufthansa Home Markets that can be chosen by consumers of air passenger transport services.
26. The ACCC recognises that people travel for different reasons and can have substantially different demand characteristics. In particular, differing characteristics of leisure and business passengers may suggest that each group could be assessed as separate parts of a broader market. In considering these applications for authorisation, the ACCC considers that the assessment of public benefits and detriments in this matter is not significantly affected by whether business and leisure services are considered together or separately.

Future with and without

27. To assist in its assessment of the JVF Agreement against the authorisation tests, the ACCC compares the benefits and detriments likely to arise in the future with the conduct for which authorisation is sought against those in the future without the conduct the subject of the authorisation.

28. The ACCC considers that without the JVF Agreement for which authorisation is sought:
- Singapore Airlines and Lufthansa would be likely to continue to operate their present networks of flights;
 - Lufthansa would continue its existing operations from the Lufthansa Home Markets and would be unlikely to commence standalone flights to Australia;
 - Lufthansa would continue to codeshare on some Singapore Airline routes between Singapore and Australia; and

³ Subsections 90(5A), 90(5B), 90(6), 90(7), 90(8).

- Lufthansa and Singapore's existing codeshare agreements with other airlines would continue.

Public benefit

29. The CCA does not define what constitutes a public benefit and the ACCC adopts a broad approach. This is consistent with the Tribunal which has stated that the term should be given its widest possible meaning, and includes:

...anything of value to the community generally, any contribution to the aims pursued by society including as one of its principal elements ... the achievement of the economic goals of efficiency and progress.⁴

30. The ACCC considers that the public benefits of the JVF Agreement fall within the following broad categories:

- enhanced products and services;
- operational and other efficiencies;
- increased competition in international air passenger transport markets; and
- stimulation of tourism.

31. The ACCC's assessment of the likely public benefits from the JVF Agreement is as follows.

Enhanced products and services

32. The ACCC recognises that, absent coordination, two airlines offering complementary services do not have an incentive to take into account the effect of their product and service decisions on demand for the other airline's products and services. The consequence can include less convenient connections for passengers, less attractive customer reward programs and/or lower levels of provision of ground services such as airport lounges and check-in services.

33. The ACCC considers that the Applicants are likely to have an incentive under the JVF Agreement to optimise their joint service offering and that this is likely to result in public benefits. In particular, the JVF Agreement has the potential to confer public benefits through better scheduling of complementary services, better access to value added services (reward schemes and airport lounges) and coordinated offers to corporate account holders.

34. The ACCC also considers that the JVF Agreement will provide a greater likelihood of new services, up-gauging of capacity and increased frequency of services due to the Applicants combined passenger feeds arising from their complementary networks.

Operational and other efficiencies

35. In its consideration of similar airline alliances the ACCC has previously accepted that improved operating efficiencies and/or avoidance of duplicated fixed costs through alliances are likely to result in a public benefit. However, the ACCC has

⁴ *Queensland Co-operative Milling Association Ltd* (1976) ATPR 40-012 at 17,242; cited with approval in *Re 7-Eleven Stores* (1994) ATPR 41-357 at 42,677.

generally not placed a significant weight on this as a public benefit absent strong evidence about how such savings will be achieved.

36. In this case, the Applicants submit that through increased passenger numbers the JVF Agreement allows the Applicants greater opportunity to access efficiencies through:

- better load factors and scale effects in operations as fixed costs are allocated to more flights and spread over more passengers;
- efficiency benefits from synergies in marketing; and
- revenue sharing eliminating double mark ups which occur when each airline applies a margin to its leg of the journey involving flights operated by both airlines.

37. In principle, the ACCC considers that the JVF Agreement is likely to facilitate some public benefits through:

- the realisation of efficiencies associated with network growth, improved load factors, more efficient and effective marketing; and
- more efficient (cost reflective) pricing of services to the extent that the price and revenue coordination contemplated under the JVF Agreement results in each airline factoring in the impact of the margins they apply to their own fares on the other airline's profits and, hence, incentive to sell seats.

38. The ACCC considers that efficiencies are a public benefit in and of themselves. However, the ACCC gives greater weight to the realisation of efficiencies where they are likely to be passed through to consumers in the form of lower fares or better services.

39. The ACCC considers that the likelihood of efficiencies achieved by the JVF Agreement being passed through to passengers will depend on competitive conditions year to year, but accepts there is likely to be some pass through of realised cost savings and efficiencies in the form of lower fares or better services.

Increased competition in international air passenger transport services markets

40. The ACCC considers that airline alliances can stimulate competitive responses among rivals where the alliance enhances the alliance partners' products and results in lower fares (to the extent that cost savings and other efficiencies are passed through to customers).

41. The ACCC notes that the joint venture's product and service offering is greater than either airline could have offered alone. The joint venture is able to leverage this integrated network, through joint sales and marketing initiatives, to attract passengers who otherwise might not have flown with either Lufthansa or Singapore Airlines.

42. The ACCC considers that the enhanced product and service offering under the JVF Agreement - including new services, up-gauging of capacity and increases in frequency of services, improved lounge access and greater loyalty program benefits - is likely to trigger a competitive response from competing airlines. This is likely to result in a public benefit.

Tourism benefits

43. As the ACCC has noted in previous assessments of airline alliances, there are a wide range of factors that influence tourism demand and expenditure including general purchasing power in source countries; the relative cost of other destinations; the total cost of visiting Australia; and the perceived quality of Australia as a destination. Notwithstanding this, the ACCC has recognised the potential for airline alliances to increase tourism demand and expenditure.
44. In this case, the ACCC considers that the JVF Agreement has the potential to stimulate tourism in Australia through increased passenger traffic as a result of enhanced products and services and, potentially, lower fares to the extent that, on balance, the JVF Agreement promotes rather than lessens competition and the Applicants pass through cost savings and efficiency gains to customers.
45. The ACCC considers that the extent of the tourism benefits realised under the JVF Agreement will be highly (positively) correlated with the additional traffic to Australia stimulated by the JVF Agreement. In this respect, while the Applicants have not provided strong evidence that the JVF Agreement will materially increase traffic to Australia the ACCC accepts that, on balance, the JVF Agreement has the potential to generate some additional traffic. On this basis, the ACCC considers that the JVF Agreement has the potential to generate some, limited, tourism-related public benefits.
46. The ACCC considers that the extent of the tourism benefits realised under the JVF Agreement will be highly (positively) correlated with the additional traffic to Australia stimulated by the JVF Agreement. The Applicants have not provided evidence that the JVF Agreement will materially increase overall passenger traffic to Australia. The ACCC accepts that, on balance, the JVF Agreement has the potential to generate some additional traffic. On this basis, the ACCC considers that the JVF Agreement has the potential to generate limited tourism-related public benefits.

Public detriment

47. The CCA does not define what constitutes a public detriment and the ACCC adopts a broad approach. This is consistent with the Tribunal which has defined it as:
- “...any impairment to the community generally, any harm or damage to the aims pursued by the society including as one of its principal elements the achievement of the goal of economic efficiency.”⁵
48. The ACCC notes that Lufthansa does not directly operate flights on any routes into or out of Australia. Based on the available information, the ACCC considers that it is unlikely Lufthansa would be likely to commence operating services to Australia over the timeframe for which authorisation is sought (five years).
49. In terms of indirect flights to Australia, the Applicants currently only operate overlapping services on two routes, Singapore – Frankfurt and Singapore – Zurich, which in some cases will form a segment of a service to or from Australia. The ACCC notes that there are many other options available to travellers between Australia and Frankfurt and Australia and Zurich, including services with a comparable travel time to that offered by the Applicants by Etihad Airways, Emirates, Cathay Pacific, Qatar Airways and Thai Airways.

⁵ *Re 7-Eleven Stores* (1994) ATPR 41-357 at 42,683.

50. While Lufthansa does not directly operate flights on routes to or from Australia, it does market services between Europe and Australia pursuant to its codeshare agreements with Singapore Airlines, Thai Airways and United Airways. Absent the JVF Agreement, Lufthansa may be more likely to also consider other options for providing flights between Europe and Australia such as through existing and potentially new codeshare agreements with other airlines. Therefore, there is potentially some loss of competitive rivalry for air passenger transport services on some routes between Australia and Europe as a result of the JVF Agreement. However, given that Lufthansa does not have a significant presence on these routes – and the competitive discipline imposed by other international airlines on these routes – the ACCC considers that any reduction in competition resulting from the JVF Agreement is likely to be very limited.
51. On this basis, the ACCC considers that the JVF Agreement is likely to result in little, if any, public detriment.

Balance of public benefit and detriment

52. In general, the ACCC may grant authorisation if it is satisfied that, in all the circumstances, the JVF Agreement is likely to result in a public benefit, and that public benefit will outweigh any likely public detriment, including any lessening of competition.
53. The ACCC considers that the JVF Agreement would, or would be likely to, result in public benefits, primarily in the form of:
- enhanced products and services;
 - operational and other efficiencies; and
 - increased competition in international air passenger transport markets.
54. The ACCC considers that the JVF Agreement is likely to result in little, if any, public detriment.
55. Therefore, for the reasons outlined in this draft determination the ACCC is satisfied that the JVF Agreement is likely to result in a public benefit that would outweigh the likely public detriment, including the detriment constituted by any lessening of competition that would be likely to result. Accordingly, the ACCC proposes to grant authorisation.

Length of authorisation

56. The CCA allows the ACCC to grant authorisation for a limited period of time.⁶ This enables the ACCC to be in a position to be satisfied that the likely public benefits will outweigh the detriment for the period of authorisation. It also enables the ACCC to review the authorisation, and the public benefits and detriments that have resulted, after an appropriate period.
57. In this instance, the ACCC proposes to grant authorisation for five years.

⁶ Subsection 91(1)

Draft determination

The applications

58. Application A91542 was made using Form A and A91543 using Form B of Schedule 1 of the Competition and Consumer Regulations 2010. The applications were made under subsection 88(1) and (1A) of the CCA.
59. Authorisation is sought by Singapore Airlines and Lufthansa and their respective passenger airline subsidiaries to coordinate their operations between Germany, Austria, Belgium and Switzerland (the **Lufthansa Home Markets**) and Singapore, Australia, Indonesia and Malaysia (the **Singapore Home Markets**), pursuant to a Joint Venture Framework Agreement (the **JVF Agreement**) and related agreements contemplated by the JVf Agreement.
60. Authorisation is sought as the JVf Agreement may contain a cartel provision or may have the purpose or effect of substantially lessening competition or be an exclusionary provision within the meaning of section 45 of the CCA.
61. Subsection 90A(1) of the CCA requires that before determining an application for authorisation the ACCC shall prepare a draft determination.

The net public benefit test

62. For the reasons outlined in this draft determination, the ACCC is satisfied, pursuant to sections 90(5A), 90(5B), 90(6) and 90(7) of the CCA, that in all the circumstances the JVf Agreement for which authorisation is sought is likely to result in a public benefit that would outweigh any likely detriment to the public constituted by any lessening of competition arising from the JVf Agreement.
63. The ACCC is satisfied, pursuant to section 90(8), that the JVf Agreement for which authorisation is sought is likely to result in such a benefit to the public that the JVf Agreement should be allowed to take place.

Conduct which the ACCC proposes to authorise

64. The ACCC proposes to grant authorisation A91542 and A91543 to Singapore Airlines and Lufthansa to the conduct described at paragraph 59.
65. The ACCC proposes to grant authorisations A91542 and A91543 for five years.
66. This draft determination is made on 15 September 2016.

Next steps

67. The ACCC now seeks submissions in response to this draft determination. In addition, consistent with section 90A of the CCA, the Applicants or an interested party may request that the ACCC hold a conference to discuss the draft determination.