

STRATEGIC

18 August 2010

Mr Michael Bird
Executive Director
International Air Services Commission
GPO Box 630
Canberra ACT 2601

Dear Mr Bird *Mike*

Application for Allocation of Capacity on the Indonesia Route

On 28 July 2010, Strategic Airlines ("Strategic") applied to the Commission for an additional allocation of 1716 seats each way, each week on the Indonesia route. In response to your letter of 9 August informing Strategic that the capacity sought by Australian airlines exceeds the capacity available for allocation, and inviting Strategic to address the criteria in paragraph 5 of the Minister's Policy Statement, we request that the Commission considers the submission below.

Background

Decision [2009] IASC 222 varying Determination [2008] IASC 101 transferred to Strategic the allocation of 408 seats of capacity per week previously made to Ozjet Airlines on the Indonesia route. With approval for 60 additional seats each week via the spillover provisions, Strategic has been able to provide three services per week between Perth and Denpasar on its 156-seat Airbus A320. The aircraft is configured with 144 economy seats and 12 business class seats.

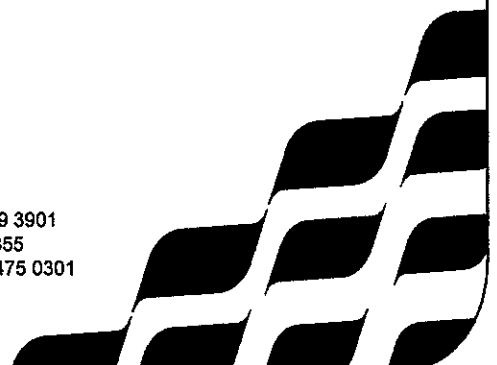
Although still in its infancy, the market has received Strategic extremely well, as evidenced by passenger load factors on all Strategic flights. We believe that the reasons below justify our request that the allocation sought by Strategic be awarded in full.

Competition Benefits

Strategic commenced operations over the Perth-Denpasar market on 12 June 2010 with the launch of sales occurring on 16 March 2010. Immediate associations were formed with reputable Bali market wholesalers, travel agencies and marketing firms to complement our methods of sales distribution (i.e. traditional reservations centre supported by internet booking engines), and tailored a product with a schedule directed towards a broad consumer base.

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The effect was both immediate and pervasive. With a limited schedule (a maximum of three frequencies per week), Strategic achieved extraordinary sales and by operational launch, had well over 6000 customers booked (advanced seat sales) on our services.

Strategic employs a wide range of fare initiatives specific to both the wholesale and retail markets. We choose not to enforce "sales blackout" periods regardless of the time of year, and testimonials from the travelling public bear witness to the quality of the service. Our first completed month of services (July 2010) exceeded all expectations with a load factor in excess of 82%. Strategic anticipates that it will have sold tickets to, (and in part uplifted), more than 20,000 customers by early October.

The Perth-Denpasar market as a whole has experienced exceptional growth, particularly in the last two years. In the twelve months to May 2010, over 600,000 passengers were uplifted over the route - a growth of 96% over the preceding 12 month period.

Annual traffic from all mainland Australian ports to/from Denpasar has also witnessed a remarkable expansion in passenger numbers;

2006/7	428,313
2007/8	588,187
2008/9	825,039
2009/10	1,242,615 (11 months data annualised)

The growth in passenger traffic can be attributed both to the expansion of competition and the subsequent increase in services from Australian capital cities.

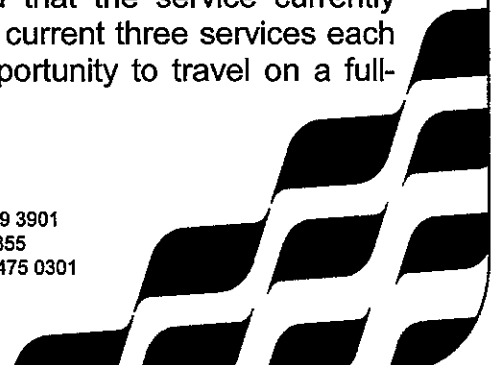
The market dynamic has, in our opinion, also shifted. Whilst Bali is most decidedly an attractive destination for tourists, we perceive a growing element of support in the level of business travel, and remarkably, tickets transacted and issued well inside normal booking parameters; "on-day/next-day" reservations to an international destination were once uncommon. In our experience, that is certainly no longer the case.

Moreover, general market growth shows no signs of abatement. We would simply contend that an increase in east coast frequencies is likely to mirror the Perth experience - incremental growth in traffic with an emphasis on repeat travel to a destination within reasonable access, irrespective of the departure port.

Accordingly, the increased capacity sought by Strategic will drive increased demand for travel to Bali, and augur well for competition across all Australian gateway ports. If the capacity sought by Strategic is received in its entirety, Strategic will be able to commence an additional 11 return services each week. It is planned that the service currently operated between Perth and Denpasar will increase from the current three services each week, to a daily service. This will allow passengers the opportunity to travel on a full-

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service Australian airline every day of the week in the high-demand market of Perth. Notwithstanding the desire to stagger the introduction of these new services, it is anticipated that all of these additional services ex Perth will be offered by 31 March 2011, and operational by 30 June 2011.

It is expected that if Strategic receives the allocation requested, the remaining capacity will be dedicated to the provision of direct services from Brisbane and Melbourne to Denpasar, as early as 30 June 2011, but prior to 31 October 2011. These new services will provide much needed travel options for passengers out of these gateway ports, and will again introduce a full-service Australian carrier to the route where there is currently none operating.

Other Benefits

Tourism

By offering a full-service product in the form of the Airbus A320 aircraft, Strategic will help to ensure that the opportunity for inbound tourism from Indonesia is maximised. The absence of this product offering from any other Australian carrier servicing the Bali market has forced passengers wishing to visit Australia via Denpasar to use a low-cost service, or travel with a foreign airline – both being options that are often unpalatable for passengers in this market.

Further, for tourists visiting the region, a holiday to Australia will follow on from a holiday in Bali. For many of those passengers, there is a preference to fly business class only. By being able to offer an increased schedule, Strategic will help to ensure that there is no deterrent for these passengers transiting through to Australia who seek a business class offering, and whose preference is to fly with an Australian airline.

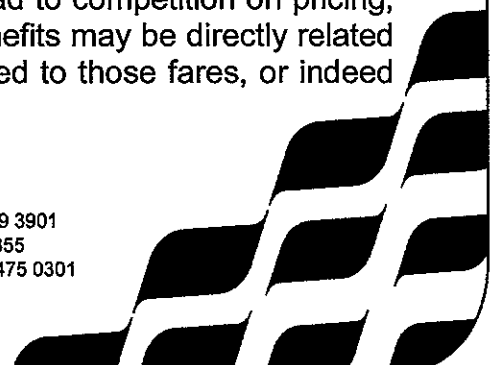
Consumer

It is a given that consumers are the primary beneficiaries of increased competition on any air route - choice of carriers will always help to create attractive options for holiday-makers. Without the requested increased capacity, Strategic is severely constrained as a viable option for travellers wishing to fly on specific days of the week from Perth, and cannot currently offer any services to and from other gateway ports. If on any given day, a consumer has the option to fly with one of three Australian Airlines out of one or more gateway ports, barriers to travel are diminished.

Importantly, the presence of three airlines will undoubtedly lead to competition on pricing, which will in turn deliver benefits to the consumer. These benefits may be directly related to fares, the conditions of travel (flexible or otherwise) attached to those fares, or indeed

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the standard of airline service delivery. Strategic has proven to be extremely competitive on pricing with its current (limited) schedule, and our market objectives together with the expectations of our passengers, will only be enhanced with the desired increase in frequency.

Moreover, consumer choice increases significantly if amongst Australian airlines, there is also the option to travel either 'low-cost' or 'full-service', and the choice of travelling economy or business class. This product differentiation obviously opens up options that will appeal to a wider range of consumers.

Trade Benefits

The trade benefits that will be derived from Strategic's increased presence on the Indonesia route are clear. Strategic has a corporate history in contract charter and logistics, with extensive experience in freight and cargo movements. This experience will allow users of air freight services in Australia to have access to the expertise that comes with over 20 years specialising in this part of the aviation industry.

Notwithstanding this, the increase in air freight options through additional flights to Indonesia each week on Strategic's A320, Australian importers and exporters will have access to markedly more competitive freight prices, stimulating multiple industry sectors and the economy at large.

Industry Structure

The Australian aviation industry will be stronger for the presence of Strategic. The opportunity for Strategic to grow both its revenue and customer base will result in the development of another viable player in the aviation market in Australia. It is expected that Indonesia (Bali) will play a pivotal role in the growth of Strategic as a business, as public support thus far has been overwhelming. Further, increased frequency will only serve to support the reputation that Australian carriers have for both quality and service.

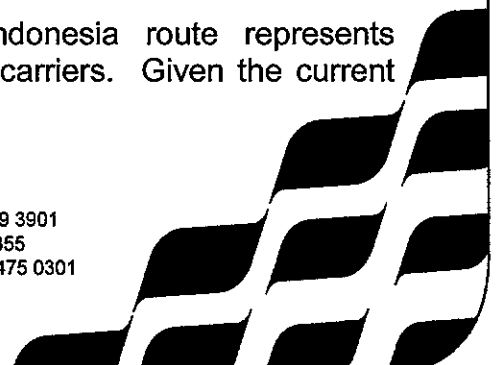
Conclusion

While there is little doubt that Strategic Airlines could well be regarded as the new entrant within this sector, there is also little doubt that the competition benefits, enhanced tourism offering, consumer choice and trade benefits that are created by Strategic's presence are clearly an asset to this sector's industry structure. Strategic Airlines' proven ability to grow the aviation market segment in question provides benefits to both consumers and the nation's trade alike.

At present, Strategic's allocation of capacity on the Indonesia route represents approximately 4% of the capacity available to all Australian carriers. Given the current

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allocation of seats among incumbent operators, Strategic believes that its request is both fair and equitable, particularly given our full-service offering and the provision of a business class to this market, which are both currently lacking in the offerings provided by those Australian incumbents.

Sincerely



Damien Vasta
Head of Commercial
Strategic Aviation Group Pty Ltd

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