



Australian Government

International Air Services Commission

DETERMINATIONS

Determinations: [2009] IASC 131 and [2009] IASC 132
The Route: Fiji
The Applicants: Virgin Blue International Airlines Pty Ltd
(ACN 125 580 823) (V Australia) and
Qantas Airways Limited
(ACN 009 661 901) (Qantas)
Public Register File: IASC/APP/200926

1 The applications

1.1 On 12 August 2009, V Australia applied for an allocation of 1,267 seats of capacity per week on the Fiji route. The airline proposes to operate daily 361-seat B777-300ER services between points in Australia and Fiji. A total of 2,527 seats is required for these operations. The further 1,260 seats needed to operate the services in addition to the allocation sought are proposed to be obtained by a transfer of that capacity from Pacific Blue Australia. (Concurrently with V Australia's application for capacity, Pacific Blue Australia applied to transfer 1,260 seats of capacity per week to V Australia). The capacity proposed to be transferred would be made available by the cessation of daily B737-800 services operated by Pacific Blue Australia between Sydney and Nadi. These services would end at the time of commencement of V Australia's services. V Australia sought a five year determination. The capacity is proposed to be fully utilised from December 2009.

1.2 In response to V Australia's application, the Commission published a notice on 13 August 2009 inviting other applications for the capacity sought by V Australia. In response to this notice, on 20 August 2009 Qantas submitted its intention to apply for capacity on the Fiji route. As the proposed application from Qantas was expected to create competing applications for available capacity, the Commission wrote on 25 August 2009 to Qantas and V Australia inviting them to address the paragraph 5 criteria in the Minister's policy statement in support of their respective applications.

1.3 In light of the advice from Qantas that it proposed to compete for capacity sought by V Australia, V Australia requested that the application by Pacific Blue Australia to transfer capacity to V Australia not be dealt with by the Commission, pending the outcome of the contested case. On 30 October 2009, in responding to the Commission's draft determinations in this case of 20 October, the Virgin Group sought the reactivation of the transfer application if the allocations proposed in the draft determinations were confirmed in the Commission's final determinations. A further application was also made to transfer a further 360 seats per week from Pacific Blue Australia to V Australia. Those transfer applications are the subject of separate Commission decisions.

1.4 On 27 August 2009, Qantas lodged an application for an allocation of 1,491 seats of capacity per week. The capacity sought was made up of remaining shelf capacity not sought by V Australia (493 seats per week) and a portion (998 of 1,267 seats per week) of the capacity allocation applied for by V Australia. Qantas advised that Jetstar, its wholly-owned subsidiary, planned to commence daily services between Sydney and Nadi with one-class A321-231 aircraft configured with 213 seats. The services are planned to commence from April 2010. Qantas requested an allocation on the basis that the capacity may be utilised by Qantas or its wholly-owned subsidiaries, including in joint services between them.

1.5 On 7 September 2009, both Qantas and V Australia responded to the Commission's request to address the paragraph 5 criteria. These supporting submissions are summarised in Section 5 below. The V Australia submission included a confidential attachment. The confidentiality issues were matters of a commercial nature and other possibly sensitive issues. A further confidential submission from V Australia was received on 22 September 2009 on similar themes.

1.6 Following receipt of the paragraph 5 responses from V Australia and Qantas, the Commission published a notice on 9 September 2009 inviting submissions about the two applications. One submission dated 21 September was received from Mr Navin Raj supporting the V Australia application. The submission stated that only Air Pacific operates on the route with Qantas code sharing. This means there is little competition, no choice and delays because the Air Pacific aircraft are old. Competition is needed to reduce air fares.

1.7 All public material supplied by the applicants is filed on the Register of Public Documents. Commercial-in-confidence material provided by the applicants is filed on the Commission's Confidential Register.

2 Current services

2.1 The Fiji route is served by:

2.2 Air Pacific, a designated airline of Fiji, which operates services between Sydney, Melbourne, Brisbane and Coolangatta and Nadi. The number of flights operated varies across the scheduling period, with the total number of seats operated varying between 5,000 and 5,689 per week. For the great majority of the period, the number of seats operated is in the lower to middle part of this range. Additional capacity is generally provided during seasonal peak times. A typical weekly operation by Air Pacific is :

- Seven B747-400 services between Nadi and Sydney;
- Six B737 services between Nadi and Brisbane, with generally five of the six operated by B737-800 series aircraft with the other flown by a B737-700 series aircraft. One service operates via Coolangatta There is also a once weekly (sometimes twice-weekly) B767-300 service;
- Four B767-300 services per week between Nadi and Melbourne; and

- One B737-800 service weekly between Nadi and Coolangatta (in addition to the service extending to Brisbane).

2.3 Qantas code shares on all of Air Pacific's services on a free-sale basis and owns a 46% stake in Air Pacific. As a marketing carrier, Qantas requires no capacity allocation from the Commission to participate in these services.

2.4 Pacific Blue Australia operates seven B737-800 passenger services weekly between Brisbane and Nadi, seven B737-800 services per week between Sydney and Nadi and twice weekly B737-800 services between Melbourne and Nadi. These services account for the exercise of 2,880 seats of capacity per week. The airline holds unused a further 360 seats of capacity per week. Pacific Blue Australia also operates twice per week between Adelaide and Nadi but seating capacity on this sector is not limited under the air services arrangements.

3 Provisions of relevant air services arrangements

3.1 The air services arrangements between Australia and Fiji permit multiple designation of airlines. The designated airlines of Australia may determine the frequency of service and aircraft type subject to capacity entitlements totalling 5,000 seats per week on the specified routes to or from Sydney, Melbourne, Brisbane and/or Perth. The designated airlines of Fiji may operate up to a total of 6,000 seats per week. Passenger operations are unrestricted to or from points in Australia other than Sydney, Melbourne, Brisbane and Perth.

3.2 The Commission has previously allocated a total of 3,240 seats per week to Pacific Blue Australia. The Register of Available Capacity shows that 1,760 seats per week remain available for allocation to Australian airlines for services to or from Sydney, Melbourne, Brisbane and/or Perth. Pacific Blue Australia also holds an allocation of unlimited capacity for operations to and from other Australian points.

3.3 The airlines of either Contracting Party may enter into co-operative marketing arrangements, such as code sharing, whether as the operating or marketing airline, with an airline(s) of the same or the other Contracting Party. Capacity offered by a marketing airline is not counted against the capacity entitlements of the Contracting Party designating that airline.

4 Characteristics of the Australia – Fiji route

4.1 As the following table shows, in the year ending July 2009, traffic on the Australia – Fiji route totalled just more than 616,000 passenger movements. Traffic growth over the previous year was a modest 0.9% compared with the long term growth rate for the route, but this was a solid result in view of the global financial crisis which saw passenger travel decline on many routes around the world. Growth in passenger numbers in the July 2008 year over the preceding year was a very strong 12.5%. The average annual growth rate from 2006 to 2009 was 4.1%.

4.2 Of the total movements, 84.2% of passengers travelling on the route had a destination of Australia or Fiji, or about 5,000 passengers each way each week. The great

majority of these passengers (502,000 for the July 2009 year) flew on direct services, with less than 17,000 flying via intermediate points. The remaining 15.8% of passengers carried on the route (just under 100,000) were destined for countries beyond Fiji or Australia (such as New Zealand or the United States).

Australia - Fiji air passenger market

Years ended July						Compound annual growth rate	
	2005	2006	2007	2008	2009	06-09	
Direct (Annual % change)	428,125	449,610 5.0%	434,272 -3.4%	494,495 13.9%	501,871 1.5%	81.5%	3.7%
Indirect (Annual % change)	18,550	16,433 -11.4%	16,766 2.0%	17,350 3.5%	16,858 -2.8%	2.7%	0.9%
Through (Annual % change)	77,655	79,586 2.5%	91,461 14.9%	98,697 7.9%	97,318 -1.4%	15.8%	6.9%
Total Market (Annual % change)	524,329	545,629 4.1%	542,498 -0.6%	610,542 12.5%	616,046 0.9%	100.0%	4.1%

Source and note: Data in this table has been derived from information supplied by the Australian Bureau of Statistics. Figures may not add to totals due to rounding.

4.3 Australian residents dominate travel numbers on the route, comprising about 88% of traffic with an origin/destination of Australia or Fiji. This proportion has risen dramatically over the past decade, with Australian resident traveller numbers more than tripling since 2000, while visitor numbers from Fiji to Australia have grown very slowly. In the year to July 2009, on average nearly 4,400 Australia residents travelled each way each week, while there were just over 600 visitors to Australia each week originating from Fiji.

4.4 Nearly 80% of Australian residents travel for holidays, with about 10% visiting relatives. Nearly 8% travel for business or conventions. The much smaller Fiji visitor market is made up mainly of those visiting relatives or for holiday. About 20% of visitors from Fiji are travelling for business or conventions.

5 Summary of applicants' claims against the paragraph 5 criteria

5.1 The claims of V Australia and Qantas against the paragraph 5 criteria are set out below.

Introduction

Virgin Blue Group

5.2 The Virgin Blue Group noted that Qantas had sought an allocation of 1,491 seats per week comprising a proportion of the capacity sought by V Australia and the balance of the shelf capacity not sought by V Australia. If Qantas' application was successful, this

would leave 269 seats per week available for future allocation. V Australia believed the public interest would be best served by the Commission authorising V Australia's proposal.

5.3 The airline provided background to its claims against the paragraph 5 criteria. It noted that, since March 2000, Qantas has participated in the market exclusively as a marketing carrier on services operated by Air Pacific. This followed changes to the air services arrangements which meant that Qantas no longer required an allocation of capacity to participate as a marketing airline.

5.4 The Virgin Blue Group entered the route in August 2004 with services operated by Pacific Blue Australia. That airline now operates 16 B737-800 services per week from Sydney, Brisbane and Melbourne and a further two B737-800 flights weekly from Adelaide. The services proposed by V Australia illustrate the Group's continuing investment in and commitment to the Fiji market.

Qantas

5.5 Qantas provided introductory information about the Australia – Fiji passenger market from ABS data, as well as summarising Jetstar's plans for the route. Fiji is Australia's 12th largest route in origin/destination terms, with 510,000 passengers travelling between the two countries in the year to June 2009. Most travellers fly direct between the two countries, with New Zealand the principal intermediate country for the few passengers journeying indirectly. Australian resident traffic dominates the route, with only 12% of passengers being visitors to Australia. Most Australian resident passengers travel for holidays (78%), with 10% visiting friends and relatives (VFR). Only four per cent travel for business. In the much smaller Fiji visitor market, VFR is the larger segment (33%), with holiday 21% and business 16%.

5.6 Qantas said that market shares on the route in the year to June 2009 were Air Pacific 46%, Pacific Blue 34% and Qantas 20%.

5.7 Jetstar's proposed daily Sydney – Nadi A31-200 services are scheduled to commence from 5 April 2010. Sydney is the largest market for residents and visitors. Same-day connecting services would be offered to passengers travelling to/from Melbourne and Perth. Qantas plans to code share on Jetstar's services.

Competition benefits

Virgin Blue Group

5.8 The Virgin Blue Group noted that there has been no impediment to Qantas operating its own aircraft services on the Fiji route, either before or after the entry of Pacific Blue Australia. It has been a matter of Qantas' commercial and strategic judgement that it has chosen to participate only as a marketing carrier on Air Pacific's services. However, this does not lessen Qantas' competitive impact in the market. The presence of Qantas and Pacific Blue Australia's entry in 2004 means that Australian carriers are able to compete effectively with one another and with carriers of foreign countries on this route.

5.9 V Australia's entry would maintain the competitive pressure brought by Pacific Blue Australia which has resulted in lower air fares. V Australia would also bring new competition in the premium market and a significantly increased air freight capability. The low unit cost of the B777-300ER will enable V Australia to offer fares at lower levels than those currently in the market.

5.10 Pacific Blue Australia has increased its capacity by 27% since its first full year of service, while Qantas has maintained virtually the same capacity despite inherent advantages in the Australian market and scope to flexibly manage its capacity through the free-sale nature of its code share agreement with Air Pacific. However, the Air Pacific/Qantas partnership operates a combined total of 62% of route capacity, compared with 38% for Pacific Blue Australia. Air Pacific/Qantas would still hold 54% of all capacity if V Australia's application was successful. Should the Qantas application be successful, the market share of Qantas/Air Pacific would rise, but with the majority of capacity still operated by Air Pacific aircraft.

5.11 Pacific Blue Australia had lowered tariffs, stimulated significant demand increases and improved consumer choice and welfare benefits by operating in competition with the incumbent partnership. The Pacific Blue Australia Group estimated that the Fijian economy had benefitted by FJD41 million since the start of services by Pacific Blue Australia. This included the creation of about 40,000 new jobs. V Australia would bring a new competitive dimension and product innovation, particularly in the premium market.

Qantas

5.12 Qantas summarised the capacity operated on the route, noting that the main competitors are Air Pacific, Pacific Blue and Qantas (through its free-sale code share with Air Pacific). Air New Zealand is the most significant third-country carrier, operating 11 flights per week between Nadi and Auckland, Wellington and Christchurch. These connect with Air New Zealand's trans-Tasman services.

5.13 Qantas said that Pacific Blue Australia is the only Australian carrier holding an allocation of capacity on the Fiji route and it has 65% of the total Australian entitlements. If V Australia was allocated the capacity it has sought, the Virgin Blue Group would hold 90% of Australian capacity rights. If Jetstar entered the market, it would be utilising less than 30% of these rights, and mean there was a second Australian carrier operating its own aircraft on the route, bringing direct competition for Pacific Blue Australia. Qantas suggested that there was little possibility of negotiations for additional capacity entitlements in the foreseeable future. If Jetstar was not allocated the capacity sought on this occasion, it would mean it was unlikely the airline could enter the route to the extent needed to be competitive.

5.14 Qantas said the entry of Jetstar with daily flights would provide considerable competition as Jetstar would have to battle two established incumbents in order to gain market share. Qantas stated that Pacific Blue Australia's market share had grown from about 25% to 34% in the two years since the year ending June 2007. This trend could continue following Pacific Blue Australia's recent addition of services from Melbourne and Adelaide. The proposed entry of V Australia could also be expected to result in further market share gains.

5.15 Qantas explained that it had lost 28% of its market share since its code share relationship with Air Pacific was changed from a block-space to a free-sale arrangement. Air Pacific's market share has risen to 46% through a combination of the changed code share arrangements, increased capacity and advertising and promotion.

5.16 This environment provides the incentive for Jetstar's entry and, as an Australian carrier in a market with predominately Australian resident traffic, can utilise its domestic network and well-know brand to compete on the Fiji route. Jetstar has 140 combined international and domestic departures daily from Sydney. Qantas quoted outbound traffic forecasts for the Fiji route which average 1.6% per annum to 2012/13 and then 5% per annum to 2017/18.

5.17 Qantas said that Jetstar seeks to operate capacity on leisure routes which are sensitive to price stimulation, like Fiji. Jetstar has successfully launched services on comparable international routes, such as Thailand and Vietnam, resulting in double average passenger growth rates on those routes. The competitive responses by incumbents to fare stimulation by Jetstar has often resulted in traffic growth for incumbents.

5.18 Qantas stated that to compete successfully against Air Pacific and Pacific Blue, which operate nine and seven services per week respectively between Sydney and Nadi, it is essential for Jetstar to receive sufficient capacity to operate a marketable frequency on the route; in this case a daily service being the minimum required. Qantas noted that Jetstar had entered other routes with less than a daily service, but this had been to replace or complement Qantas flying or on sectors where there has been no more than one direct competitor.

5.19 Qantas said that Jetstar would offer considerable price competition in the Australia - Fiji market. Jetstar's business model is predicated on price leadership from a low cost base. About 10% of Jetstar's passengers since the start of its international services have been first-time flyers.

5.20 Jetstar's proposal would result in seven additional frequencies per week being operated between Sydney and Nadi, in contrast to V Australia's proposal which would involve no increase in frequencies. Jetstar would offer attractive Sydney departure and arrival times.

5.21 Jetstar would offer product differentiation. It provides a one-class product while giving consumers the option to purchase additional services such as meals, entertainment and extra leg room seats. Jetstar also offers lower fares for passengers with carry-on baggage only and the cabin bag weight allowance of 10 kilograms is higher than V Australia, Pacific Blue Australia and Air Pacific. Jetstar also offers customers the ability to purchase fares of change bookings via mobile phone. Jetstar was voted the Best Low Cost Airline in Australia and New Zealand in the 2009 *SkyTrax Awards*.

5.22 Qantas said that the few business passengers on the route can take advantage of the options available to upgrade their travel experience on Jetstar flights. This may be advantageous on short haul flights to Fiji, whereas passengers may not be prepared to pay for features offered on V Australia flights such as lie flat beds on a four hour flight.

5.23 Qantas proposes to code share on Jetstar's services while continuing to code share with Air Pacific. However, Jetstar would provide independent and direct competition to all operating carriers on the Fiji route. Qantas noted that its continuation as a shareholder with Air Pacific is under review, but expects to maintain its commercial arrangements, such as the free-sale code share agreement, for the long term.

Other benefits

Tourism benefits

Virgin Blue Group

5.24 The Virgin Blue Group pointed to the limited potential for tourism development from Fiji, with its small population and low disposable incomes. However, the number of Fijian visitors to Australia had risen by 14% since Pacific Blue Australia's entry to the market. The operational and product offerings provided by the B777-300ER would open up new tourism markets by encouraging foreign visitors to Fiji to travel on to Australia and V Australia plans to operate beyond Fiji to other international destinations.

Qantas

5.25 Qantas noted that the number of visitors travelling to Australia is low compared with Australian residents travelling to Fiji but that Jetstar could stimulate additional visits because most inbound traffic is for leisure purposes and therefore price sensitive. Qantas noted that similar international leisure routes where Jetstar operated, such as Vietnam and Thailand, had seen higher than average growth in visitor numbers.

5.26 Qantas said that Jetstar would promote the Sydney – Nadi services via network-wide and route specific campaigns. Jetstar offers a range of pre-set and customised holiday packages to visitors.

5.27 Jetstar has an extensive domestic network which would facilitate visitor travel beyond the Australian gateway. Also, passengers travelling between Nadi and the United States will be able to connect with Qantas' code share services from Nadi to Los Angeles flown by Air Pacific.

Consumer benefits

Virgin Blue Group

5.28 The Virgin Blue Group stated that consumers had benefitted from the improved frequency and schedule choice associated with its entry into the Fiji market. V Australia's entry would expand consumer choice further, particularly in the premium market segment.

5.29 Annual traffic on the Fiji route had risen by 36% from the year ending August 2004 (prior to Pacific Blue Australia's entry) to the twelve months to June 2009. Pacific Blue Australia had been responsible for all of the growth in the market, with the combined Air Pacific/Qantas carriage declining slightly over that period. Further statistical detail was provided of the growth of traffic on city pairs served by Pacific Blue Australia, including in a series of charts attached to the submission.

5.30 The Virgin Blue Group also offers connections for domestic transfer passengers and for those travelling beyond Australia, particularly to New Zealand and the United States. Additional connections will be available soon as services commence to Thailand and South Africa.

5.31 The Group has made a demonstrable contribution to the introduction of competitive pricing as well as product development on the Fiji route. The Group has also shown and ongoing commitment to capacity growth.

Qantas

5.32 Qantas said that Jetstar would offer Australian residents a range of benefits, including customisation of travel experience through a range of product options both pre-paid and onboard; competitively priced holiday packages; sustainably competitive fares; access to the Qantas Frequent Flyer program; and an extensive domestic network.

5.33 Jetstar would give Australian consumers greater choice of carrier as there are currently only two carriers on the route. The departure and arrival times of Jetstar's flights were at attractive times. Connections at Sydney for passengers travelling to Perth and Melbourne would be more convenient than V Australia's services (if it operated on the same schedule as Pacific Blue Australia currently does). Qantas again summarised the product offerings available on Jetstar's A321 aircraft, and other planned options being web check-in and self-tagged baggage check-in.

5.34 Qantas outlined the fully-inclusive packages that would be available to families and couples. Several destinations within the Fiji island group would be available. Consumers would also have options such as hotels, tours and activities. Hotel transfers were being considered and consumers could hire a car Jetstar's car hire partners Avis or Budget.

5.35 Qantas said that Jetstar's packages to Bali, a comparable destination to Fiji, were generally equal to or cheaper than the Virgin Blue equivalent. Jetstar's packages also provided more options.

5.36 As mentioned earlier in its submission, Qantas referred to Jetstar's approach to fare setting, its higher carry-on baggage allowances and access to the Qantas Frequent Flyer program.

5.37 Jetstar has an extensive distribution network spanning all industry channels in Australia. The airline would promote Fiji heavily in the Australian market through a variety of channels. This is expected to stimulate demand for travel between Australia and Fiji.

5.38 In terms of efficiencies, Qantas said that Jetstar's business model is predicated on a low cost base and this has enabled Jetstar to compete in markets which are not viable for Qantas. Options available to customers, such as self-check kiosks, save passengers time by reducing queues. The A321-200 aircraft has the best seat per kilometre operating costs in its class. This will also contribute to Jetstar's ability to offer lower fares. Qantas again referred to the awards won by Jetstar.

5.39 Qantas said that Jetstar's entry would see incumbent carriers becoming more innovative in their fare and product offerings. It instanced responses by incumbents on the Thailand and Bali routes.

5.40 Only a small proportion of passengers on the Fiji route travel to for from the United States, but these passengers could connect with Air Pacific services to the United States, on which Qantas code shares.

Trade benefits

Virgin Blue Group

5.41 The introduction of B777-300ER aircraft will bring important trade benefits. The aircraft has an extensive freight capability through carriage of pallets and containers. Air Pacific is the only carrier currently with significant air freight capability in the Fiji market. Daily services operated by V Australia would provide Australian exporters and importers with competitive choice and scope to trans-ship product to wider markets on a regular and reliable basis.

Qantas

5.42 Qantas said that there is a sizeable air freight market made up mainly of textiles and fresh produce, as well as express cargo and international mail. Jetstar could carry on each service about 500 kilograms of freight, depending on passenger loads and season of operation. Connections to other international and domestic points are available.

Industry structure

Virgin Blue Group

5.43 The proposed operations would be an important part of the expansion of V Australia's operate network. This will generate increased operational efficiency in use of aircraft and crews and increase profitability. This would have benefits for the Australian industry. The expanded services are consistent with decisions taken by successive Australian Government's to facilitate the role of the Virgin Blue Group in developing the Australian aviation industry.

Qantas

5.44 Qantas considered that Jetstar's expansion would ensure its aircraft were efficiently utilised and provide additional employment for Australian crews. Jetstar's entry would encourage long term competition, equipping Australian carriers to compete effectively with foreign airlines and encouraging future investment and skills development.

6 The draft determination and submissions in response

6.1 The Commission issued draft determinations on 20 October 2009 proposing to allocate 907 seats per week to V Australia and 852 seats per week to Qantas for a period

of five years. Submissions in response to the draft determinations were received on 30 October from Qantas and the Virgin Blue Group. These are summarised as follows:

Virgin Blue Group

6.2 The Virgin Group welcomed the proposed allocation of 907 seats per week to V Australia. It said that, in the event this allocation was confirmed, its concurrent application for the transfer of 1,260 seats from Pacific Blue Australia to V Australia was confirmed. V Australia proposed to commence daily services within the time frame proposed in the draft determination. A further application was made to transfer an additional 360 seats from Pacific Blue Australia to V Australia.

6.3 A further submission was received on 4 November 2009 from the Virgin Blue Group, confirming plans for V Australia to operate on the Fiji route and that the operation of services by V Australia was an important part of the Group's long term strategy for Fiji. This submission was made in response to comments in the Qantas letter of 30 October (below).

Qantas

6.4 While welcoming the proposed allocation of a portion of capacity for Jetstar's use, Qantas responded to a number aspects of the draft determinations. Qantas considered that the grant of the equivalent of four A321 services per week was not sufficient to enable Jetstar to compete effectively. The originally proposed allocation of 1,491 seats, enabling the operation of daily A321 services, was required to operate a marketable and competitive frequency on the route. Qantas noted that Pacific Blue Australia had mostly operated at least five services per week on the Sydney – Nadi sector with daily flights for the past two scheduling seasons. This illustrated the important of frequency to the leisure segment of the market, especially in comparable markets for which Fiji competes for Australian leisure traffic, such as Bali. Qantas also considered that Jetstar required daily services to compete effectively with the established incumbents, Pacific Blue Australia and Air Pacific which operated a combined total of 40 frequencies per week between Australia and Fiji.

6.5 Qantas reiterated the position in its original submission that Jetstar serves other international leisure destinations with less than daily services only on sectors which complement Qantas' flying, or which have limited competition. Qantas said that the Fiji route did not fit into either of these categories, with Qantas having an indirect presence through the code share with Air Pacific. Qantas also said the viability of four services per week was questionable because of the less efficient crew and equipment utilisation compared with daily flights.

6.6 Qantas speculated that V Australia could vacate the Fiji route when conditions improve on other routes suited to B777-300ER operations. This could enable Pacific Blue Australia to operate 23 weekly B737-800 services to Fiji, providing a capacity and frequency advantage that would make Jetstar's four weekly services unsustainable.

6.7 Qantas considered that, although the Commission had discounted the amount of capacity available to Qantas through the code share, it had not given sufficient recognition to the advantages of operating carriers over marketing carriers including ability to

determine timings, frequency, routes, aircraft types and available seating inventory and fare categories under the free-sale code share agreement. Qantas also raised uncertainty about its ability to access its current level of code share capacity with Air Pacific in future, if Air Pacific decided not to renew the code share or ceased operating some or all services from Fiji to Australia. Qantas said that the existing distribution of capacity and market shares indicated that the combination of Jetstar and Air Pacific/Qantas did not have an advantage over V Australia.

6.8 Qantas suggested that there could be other capacity splits which minimised the number of residual seats, if a mix of A321 and A320 aircraft were to be operated by Jetstar, and which would give Qantas a more competitive frequency outcome relative to V Australia.

6.9 Qantas expressed concern at the Commission's references to past opportunities for Qantas to operate its own aircraft. It considered this was inappropriate to the airline's present proposal which responded to changes in current circumstances.

6.10 Qantas considered that the Commission had attached too much weight to the importance of frequency to premium travellers and the freight market, arguing that both are relatively small components of overall demand on the route. It provided data in support of this view.

6.11 Qantas argued that the Commission's statement that there should be scope for Jetstar to obtain approvals for supplementary services in peak periods was not valid for the purposes of differentiating between the airlines' proposals. The relevant provision under the air services arrangements provided no certainty and should not be taken into account, in the same way that the Commission had not taken account of the outcome of possible air service discussions.

7 Commission's assessment

Introduction

7.1 The start-up provisions of the Minister's policy statement do not apply in this case, as the Commission has previously made determinations allocating passenger capacity to Ansett International, then the initial new entrant at a time when Qantas was an incumbent carrier on the route, thus ending the start-up phase on the Fiji route. As there is not sufficient available capacity to satisfy fully the requirements of both applicants the additional criteria in paragraph 5 of the policy statement are applicable in this case, as well as the paragraph 4 criteria.

Paragraph 4 assessment

7.2 Under paragraph 4, the use of Australian entitlements by a carrier that is reasonably capable of obtaining the necessary approvals (4(b)(i)) and of implementing its proposals (4(b)(ii)) is of benefit to the public. Qantas and V Australia are established carriers on international routes and, as such, the Commission is satisfied that both airlines meet the paragraph 4 criteria.

Paragraph 5 assessment

7.3 The Commission's comparative assessment of the respective proposals against the paragraph 5 criteria in the Minister's policy statement is set out below. As both carriers have been found to meet the paragraph 4 criteria, the paragraph 5 criteria are used to assess the comparative merits of the competing applications. The Commission notes the requirement in paragraph 5.2 of the Minister's policy statement that, in applying all criteria, the Commission should take as the pre-eminent consideration the competition benefits of each application.

Competition Benefits

The extent to which proposals will contribute to the development of a competitive environment for the provision of international air services. The Commission should have regard to:

- *the need for Australian carriers to be able to compete effectively with one another and the carriers of foreign countries;*
- *the number of Australian carriers on a particular route and the existing distribution of capacity between Australian carriers;*
- *prospects for lower tariffs, increased choice and frequency of service and innovative product differentiation;*
- *the extent to which applications are proposing to provide capacity on aircraft they will operate themselves;*
- *the provisions of any commercial agreement between an applicant and another carrier affecting services on the route but only to the extent of determining comparative competition benefit between competing applications;*
- *any determinations made by the Australian Competition and Consumer Commission or the Australian Competition Tribunal in relation to a carrier using Australian entitlements under a bilateral arrangement on all or part of the route; and*
- *any decisions or notifications made by the Australian Competition and Consumer Commission in relation to a carrier using Australian entitlements under a bilateral arrangement on all or part of the route.*

7.4 Both proposals involve the planned entry of a new Australian carrier to the Sydney – Nadi sector of the Fiji route. In the case of V Australia, this carrier's services would be substituting for flights already operated by its sister carrier Pacific Blue Australia, so there would be no increase in frequency. However, V Australia's B777-300ER aircraft have twice the seating capacity of Pacific Blue Australia's B737-800 aircraft (361 seats compared with 180 seats).

7.5 The Qantas proposal involves the entry of Jetstar with A321 (213 seat) aircraft, although in responding to the draft determination Qantas has indicated Jetstar could use a mix of A320 and A321 aircraft. Its proposal would see an additional seven frequencies per week on the Sydney – Nadi sector. There would be slightly more seats operated by Jetstar

(1,491 per week) than the additional 1,267 seats per week which V Australia would provide.

7.6 An important issue the Commission is required to have regard to under this criterion is the number of carriers on the route and the existing distribution of capacity between Australian carriers. Currently, Pacific Blue Australia is the only carrier with an allocation of capacity on the route. A total of 3,240 of the 5,000 seats available to Australian carriers has been allocated to Pacific Blue Australia.

7.7 No other Australian carrier has an allocation of capacity on the route but this does not mean that there is not competition from other Australian carriers on the route. Qantas has participated as a marketing carrier for many years and at one time held a capacity allocation from the Commission to do so. However, Qantas relinquished its 2,590 seats per week of Australian capacity entitlements during 1999 and 2000 when the air services arrangements were changed so that capacity offered by a marketing carrier no longer counted against the entitlements of that airline. Qantas continues to have access to Fiji route capacity through its code share agreement with Air Pacific, without any longer requiring a capacity allocation to achieve this access.

7.8 In the Commission's opinion, Qantas' access to capacity through the code share is a relevant factor in considering the existing distribution of capacity available to Australian carriers. Qantas is already able to compete effectively against Pacific Blue Australia on the Sydney, Melbourne and Brisbane sectors, despite not having any capacity allocation, and has done so on that basis for a number of years. Air Pacific serves all those points with the same or similar frequencies to Pacific Blue Australia. On the Sydney sector, which is the subject of the current applications, Air Pacific operates daily B747-400 (453 seats) services to and from Nadi, and some additional B737 services for short periods. This is more than twice the amount of capacity currently operated on that sector by Pacific Blue Australia although the frequencies are usually the same. Qantas indicated in its original submission against the paragraph 5 criteria that there are no plans to end its code share arrangement with Air Pacific, although it indicated in its response to the draft determinations that there was no certainty about its ability to access the current level of code share capacity in future. According to Qantas, this would reduce its ability to compete in the market, potentially to a substantial degree.

7.9 It seems to the Commission unlikely that Air Pacific would wish to end a very long standing commercial arrangement with Qantas. It is difficult to see the advantages for Air Pacific from doing so and there is no indication that this might occur in the foreseeable future. The Commission also considers that the risks are low of Air Pacific significantly reducing operations on the route. The Fiji market is growing and is one of only three major routes served by Air Pacific (the United States and New Zealand being the others, with services to Hong Kong due to start in December 2009). It seems most unlikely that Air Pacific would withdraw from such a major route, or to reduce capacity in a significant way in a market which has been generally growing over a long period and which has held up well even through the global financial crisis. The most likely probability is that Qantas can be reasonably expected to have continuing access to the pool of capacity available to Fiji's designated airlines, which is an opportunity not likely to be available to V Australia or Pacific Blue Australia. There is also unused capacity available to the designated airlines of Fiji which provides for future expansion.

However, the Commission discussed in the draft determinations the possible implications in the unlikely event of the code share ending. The Commission has again taken that small possibility into account in making its final determinations, because there would be significant implications for competition on the route if Qantas access to capacity through the code share was significantly lessened for whatever reason. The Minister's policy statement also indicates that the Government considers the use of capacity in own-aircraft operated services delivers greater benefits per unit of capacity than code share operations involving arrangements for marketing seats on another carrier. These factors suggest to the Commission that it should modestly discount the amount of capacity available to Qantas through the code share in considering the existing distribution of capacity and its relevance to the competing applications. A factor supporting this approach is that market share data available confidentially to the Commission suggests that Qantas market share is significantly less than that for Pacific Blue Australia.

7.10 The additional capacity sought by V Australia, if granted, would shift the balance of market capacity shares towards the Virgin Blue Group relative to the Qantas Group. Conversely, if Qantas was allocated the capacity it has sought, the balance would shift in favour of that Group.

7.11 Allocating capacity only to V Australia would result in a doubling of capacity on the Sydney sector, but no frequency change, and no increase in the number of operators (with Pacific Blue Australia withdrawing). The Virgin Group would then hold over 4,500 of the 5,000 seats per week of capacity available to Australian carriers but bring it closer to parity in capacity shares relative to Qantas/Air Pacific taken together on the Sydney sector. It would result in increased competition for Qantas/Air Pacific but reduce Qantas' market share of capacity. However, this should not significantly impair Qantas' ability to compete effectively with V Australia as it can increase its market share relative to Air Pacific through price and marketing initiatives under the code share. There is also scope for Air Pacific to increase capacity on the Sydney sector within the Fiji capacity entitlements.

7.12 If the Commission was to facilitate Qantas' plans for Jetstar, this would see an additional carrier enter the Sydney sector. It would bring competition to all incumbent carriers. However, it would place Pacific Blue Australia at a frequency and capacity disadvantage relative to the Qantas Group on the Sydney sector, which is the largest source of traffic on the Fiji route. Jetstar and Air Pacific/Qantas would be operating 14 times per week (and sometimes more) compared with daily flights by Pacific Blue Australia and have over three and a half times the number of seats (4648 seats or more per week compared with 1,260 seats). Even discounting the extent of Qantas' participation through the code share, Qantas and Jetstar between them would have about the same or more capacity than Pacific Blue Australia, as well as the frequency advantage noted. This would weaken Pacific Blue Australia's ability to compete effectively with Qantas, Jetstar and Air Pacific.

7.13 On the other hand, there is sufficient capacity available to be allocated for the Commission to consider splitting the capacity between the two airline groups in a way that has regard to the overall balance of capacity as well as other elements of the competition criterion, and which could potentially generate a higher level of public benefits than could be obtained from an allocation to one or the other alone. It would also be consistent with paragraph 3.5 of the Minister's policy statement which requires the Commission to "have

regard to the objective of providing reasonable growth in entitlements to Australian carriers operating on that route” (subject to other relevant paragraphs) or, considered more broadly in this case, the growth ambitions of both airline groups operating on the route.

7.14 In considering the balance of a split of the capacity, the factors the Commission needs to weigh up include the relative shares of Australian capacity entitlements but also: the balance of capacity and frequencies to be operated to achieve the most competitive outcome; the best outcome in terms of lower fares in all travel classes; and choice and product differentiation and the most efficient allocation of the available capacity, so as to minimise the number of residual and therefore unusable seats.. The elements of the Other Benefits criterion are also relevant, such as in relation to freight competition and industry structure considerations. These are discussed under the respective sub-headings below.

7.15 In relation to the distribution of capacity between Australian carriers, the applicants have understandably adopted different perspectives on capacity shares which best support their proposals. The Virgin Group has focussed on the fact that Qantas has access to substantial capacity through its code share agreement with Air Pacific, noting that Qantas has chosen to participate in the market this way for many years. It notes that there is scope for further capacity expansion on the Fiji side, in which Qantas could also participate. The Virgin Group points to the fact that the capacity arrangements as they stand have resulted in Pacific Blue Australia having a passenger market share of about 35 per cent, even though it holds about 65 per cent of the available Australian capacity entitlements. On the other hand, Qantas has pointed out that it has no Australian capacity entitlements and, if V Australia’s application is granted, the Virgin Group would hold over 90 per cent of Australian rights.

7.16 The Commission understands both points of view but, as discussed above, is of the view that Qantas has access to substantial capacity through the code share and so is able to compete effectively and has done so on this basis for many years. In responding to the draft determinations, Qantas said that competing through the free-sale code share arrangement as a marketing carrier placed it a fundamental disadvantage to operating carriers. However, Qantas has argued to the Commission in many cases on other routes that code sharing offers a competitive form of market participation which delivers benefits to the public. Until 1999/2000 Qantas held an allocation of over 2,500 seats per week which it needed to participate in the code share. It handed these seats back after the air services arrangements were changed so that capacity used by a marketing carrier no longer counted against capacity entitlements. While Qantas’ market share of passengers carried has been falling, it has been losing share to Air Pacific as well as Pacific Blue Australia. The code share arrangement is a free sale type, so Qantas is able to increase its market share by price and marketing initiatives should it wish to do so.

7.17 However, although there is no indication that the code share might end, in the unlikely event it was to do so, as noted above there would be limited scope for the Qantas Group to enter the market if V Australia was allocated all of the capacity it seeks and Qantas none. Qantas has reinforced this point in responding to the draft determinations, and also raised the possibility of V Australia withdrawing from the market, enabling Pacific Blue Australia to add a substantial number of frequencies in its place. V Australia has responded on the latter point made by Qantas, asserting that it intends to maintain operations on the Fiji route. However, the possibility of market circumstances changing on

the route over a period of years means that the scenarios outlined by Qantas, while low in probability, cannot be entirely ruled out.

7.18 From a risk-management point of view, the Commission considers that a judicious course of action is to ensure there is competitive provision made for other Australian carriers in addition to the Virgin Blue Group airlines. Accordingly, in considering the split of capacity, the Commission considers that Qantas should be allocated a commercially viable amount of capacity which would enable Jetstar to compete effectively. However, Jetstar is a leisure-only carrier and, in the Commission's view, this market segment does not necessarily require daily services particularly in circumstances where Qantas already provides a competitive presence on behalf of the Qantas Group.

7.19 The Commission notes that Jetstar serves a range of other international destinations with less than daily services. Qantas has argued in its application and in responding to the draft determinations that Jetstar operates less than daily frequencies only when its operations are complementary to existing Qantas own aircraft services, or there is limited demand. Qantas stated that neither situation prevails on the Fiji route, and therefore daily services for Jetstar are warranted and necessary from an operating efficiency and competition viewpoint. However, the Commission considers that the Qantas participation through the code share clearly gives Qantas a market presence, albeit not an operating one. Accordingly, any frequencies added by Jetstar would complement the existing daily (or more) services offered by Air Pacific/Qantas on the Sydney sector. This provides the Qantas Group with a combined competitive presence which should offset any competitive disadvantage which might otherwise have been associated with Jetstar operating less than daily services in the absence of Qantas.

7.20 By contrast, V Australia would be replacing Pacific Blue Australia's services and, as noted above, would be at a frequency and possibly a capacity disadvantage to Air Pacific/Qantas plus Jetstar. The extent of the disadvantage depends on the relative allocation to V Australia and Jetstar and the practical extent of access to code share capacity by Qantas. Because V Australia would be operating in the premium market, as well as the leisure sector, this suggests to the Commission that a higher number of frequencies is important for V Australia to be competitive in the premium market segment. Business travellers are generally more time sensitive, so daily services would be ideal to meet the needs of this market.

7.21 Turning to other issues, the Commission considers that both V Australia and Jetstar would bring a high quality passenger service, although there are important differences. The modern wide-body B777-300ER aircraft proposed by V Australia brings excellent per seat operating cost efficiency which should provide scope for V Australia to compete strongly on price. This aircraft also offers qualitative attractions to customers through its quiet operation, spaciousness, and modern fit-out and facilities. It is a clearly differentiated product from the older Air Pacific B747-400s and also offers product improvements over Pacific Blue Australia's B737-800s which it would replace.

7.22 More specifically, V Australia would bring strong competition in the premium market to Air Pacific/Qantas. Its aircraft have a three class configuration – business, premium economy and economy. Pacific Blue Australia's B737-800 aircraft operating on

the Fiji route are one-class services and therefore offer no competition in the premium market.

7.23 Qantas has submitted in response to the draft determinations that business travel is a small market segment and therefore daily frequency is not essential. The Commission did note in its draft determinations that the business and convention segment of the Fiji market is relatively small in what is predominantly a leisure-based route. However, it is by no means insignificant and the ability to operate daily services against a competitor already doing so is likely to be important in maximising competitive outcomes. Premium class traffic typically produces much higher revenue yields per passenger than discount economy traffic and while the premium market tends to be relatively insensitive to price, the presence of a competitor for Air Pacific/Qantas in this segment will place downward pressure on business fares for travel on every day of the week. The premium economy seating provides an option currently not available to travellers on the incumbent operators, and could be attractive to some leisure travellers as well as business passengers. As Qantas noted in responding to the draft determinations, some business passengers currently travel in the economy cabin, so the premium economy cabin may well encourage some of those travellers to opt for the intermediate class. V Australia could be expected to stimulate non-price competition through its clear product differentiation and create an incentive for the incumbents to improve service quality further. These developments are likely to generate important public benefit gains.

7.24 V Australia could also be expected to compete vigorously on price in the leisure market. If V Australia was allocated the full amount of capacity sought, its daily B777-300ER services would see a doubling of seating capacity compared with Pacific Blue Australia's current operations on the Sydney sector. Price initiatives would be necessary to stimulate the additional demand needed to achieve profitable load factors, and this is likely to provoke a competitive response from Air Pacific and Qantas. Leisure passengers may prefer the more spacious cabin offered by the wide-bodied B777-300ER to the narrow-bodied B737-800 which it replaces.

7.25 Jetstar also proposes to operate daily services with modern aircraft, but in a narrow-body single class format. Its entry would add frequencies to the market, whereas V Australia would not, as that carrier would replace Pacific Blue Australia's services. This means that Jetstar would offer travellers additional flight times and Qantas has highlighted that these are at appealing times of the day. Jetstar would bring competition to the route, leveraging its low-cost base to be able to offer lower fares than might be possible for Qantas and Air Pacific with older equipment and a different cost structure. Jetstar would offer a broadly similar product experience to Pacific Blue Australia, although Qantas has noted some specific innovations both current and in prospect which might enhance traveller experience. Jetstar would not offer a premium class and so does not offer competition in the premium market segment.

7.26 It is apparent that both V Australia and Jetstar would bring competition benefits, but each brings some features that the other does not. Public benefits are likely to be magnified through splitting the available capacity between the two carriers. That would facilitate increased choice, a higher frequency of service and more capacity than if an allocation is made only to one of the two applicants. It would create intense competition between the two as well as with the incumbent Qantas/Air Pacific partnership.

7.27 The Commission considers that competition benefits would be greatest if V Australia was to operate daily B777-300 services and Jetstar four A321-213 services per week. An allocation of 907 seats per week to V Australia and 852 seats per week to the Qantas Group for Jetstar can achieve this outcome. It would involve the allocation of all but one of the 1,760 seats per week of the available capacity. All other potential splits of capacity leave a higher residual of unallocated seats. The proposed split of capacity grants approximately equal amounts of the remaining available capacity to both carriers, providing equal scope for both carrier groups to grow consistent with paragraph 3.5 of the Minister's policy statement. It would lift the Virgin Blue Group's share of Australian capacity entitlements to about 83% (compared with 65% now and over 90% if it had received the full allocation sought), with the Qantas Group having 17% (compared with nil now and about 30% if it had received all the allocation sought).

7.28 Qantas has referred to scope for the Commission to split the capacity in other ways and that if Jetstar was to operate a combination of A320 and A321 aircraft with differing seating configurations this could also involve a small residual of seats together with a shift in the balance of the capacity and frequency split towards Jetstar. The Commission has considered other options for splitting the capacity but taking all of the factors discussed above into account, considers that the balance proposed is most likely to maximise public benefits.

7.29 On the most likely scenarios for the future, the Qantas Group would continue to have access to substantial market capacity through the code share with Air Pacific and scope to grow further if Air Pacific increases capacity over time. By contrast, the Virgin Group would have no further scope for expansion unless more capacity is negotiated under the air services arrangements. Further, for V Australia to operate daily services, there needs to be a transfer of a further 360 seats per week from Pacific Blue Australia to V Australia (see below). This means that Pacific Blue Australia could not implement the planned additional two services per week on other sectors between Australia and Fiji as previously planned, reducing its scope to compete more strongly on those sectors in future.

7.30 The proposed allocation to V Australia of 907 seats is 360 seats less than the 1,267 seats per week it has sought. This allocation is sufficient on its own for V Australia to operate six services per week. To achieve the daily services V Australia wishes to operate, it would be necessary for the Virgin Blue Group to transfer additional capacity from Pacific Blue Australia to V Australia above the 1,260 seats per week currently proposed. The Commission notes that Pacific Blue Australia holds 360 seats per week unused on the Fiji route. The Virgin Blue Group said in its original submissions that these seats would enable Pacific Blue Australia to add services to Melbourne and Adelaide in 2010. However, in light of the allocations proposed in the draft determinations, the Virgin Group indicated in response that it wished to transfer the seats in question from Pacific Blue Australia to V Australia and has applied to the Commission to do so.

7.31 In relation to future capacity requirements for Australian carriers, the Commission understands that there is the prospect of air services consultations later in 2009. However, as the outcome of any negotiations cannot be prejudged, the Commission has not taken this into consideration in its decision making process. Should additional capacity entitlements be settled, this would open the way for the full requirements of both applicants to be satisfied.

Other benefits

Tourism benefits

(b) In assessing the extent to which applications will promote tourism to and within Australia, the Commission should have regard to:

- *The level of promotion, market development and investment proposed by each of the applicants; and*
- *route service possibilities to and from points beyond the Australian gateway(s) or beyond the foreign gateway(s).*

7.32 The inbound Fiji tourist market to Australia is small and is likely to continue to be for the foreseeable future. The vast majority of traffic on the route is Australian resident passengers. This means that there is limited scope for either applicant to develop tourism to Australia from Fiji in a substantial way. However both carriers will promote Australia in the Fiji market and both offer connections behind the Sydney gateway. Qantas is able to offer travellers from the United States to Fiji on Air Pacific connections to and from Australia. V Australia has indicated that Fiji could become a hub for international travel beyond Fiji, but there is no timetable proposed.

7.33 The Commission finds there is little difference between the proposals against this criterion and, in any case, gives the criterion little weighting as the route has little tourist traffic to Australia.

Consumer Benefits

(c) In assessing the extent to which the applications will maximise benefits to Australian consumers, the Commission should have regard to:

- *the degree of choice (including, for example, choice of airport(s), seat availability, range of product);*
- *efficiencies achieved as reflected in lower tariffs and improved standards of service;*
- *the stimulation of innovation on the part of incumbent carriers; and*
- *route service possibilities to and from points beyond the Australian gateway(s) or beyond the foreign gateway(s).*

7.34 Most of the elements of this criterion have been discussed in the context of the competition criterion above. As noted there, operations by both carriers are likely to generate the highest public benefit gains and the same is true against the consumer benefit criterion. There will be substantial extra choice for consumers in style of travel, with premium market travellers in particular having access to new product choices with V Australia (both business and premium economy). This is particularly likely to stimulate innovation on the part of the incumbents in this market segment. Both carriers offer modern aircraft with low operating costs and these efficiencies should be reflected in lower tariffs. Jetstar gives its consumers flexibility to purchase additional onboard options should they so wish. Together, the two carriers offer a range of product which give consumers excellent new choices above those currently on offer in the market. Both carriers would operate from Sydney, so there is no additional choice of airport.

Trade Benefits

(d) In assessing the extent to which applications will promote international trade, the Commission should have regard to:

- *the availability of frequent, low cost, reliable freight movement for Australian exporters and importers.*

7.35 Commission considers that V Australia's proposal offers considerably greater public benefits than the Qantas plan for Jetstar. This is because the B777-300ER has the ability to accommodate pallets and containers, offering exporters and importers an alternative to Air Pacific's B747. The Commission understands that the volume of freight able to be carried on the V Australia aircraft is about 200 cubic metres, or over 20 tonnes by weight. V Australia's entry with its large capacity and cost efficient aircraft could be expected to bring strong competition on rates as well as additional choice of time of day. As noted above, frequency can be an important factor in freight decisions especially where time sensitive freight, such as perishables, is concerned. Daily services would therefore offer the maximum level of benefits against this criterion.

7.36 By contrast, Jetstar's A321 aircraft offers very limited freight capability with no container capability. According to Qantas, the aircraft can carry about half a tonne of freight, although this will vary depending upon passenger loads and season of operation.

7.37 Qantas stated, in responding to the draft determinations, that only 143.6 tonnes of outbound freight had been carried on the Sydney – Nadi sector in the 2009 calendar year, although clarifies in a footnote that the figure is for the month of July 2009 only. According to statistics from the Bureau of Infrastructure, Transport and Regional Economics, in the year ending June 2009, 2,311 tonnes of freight was carried outbound (from Sydney to Nadi), with a further 2,490 tonnes inbound (from Nadi to Sydney). This is about an average of 200 tonnes per week in each direction. While this is not a large market, making the weighting given to this criterion relatively modest, nevertheless international trade will be most effectively promoted through V Australia having daily services.

Industry Structure

(e) The Commission should assess the extent to which applications will impact positively on the Australian aviation industry.

7.38 The Commission considers that both carriers proposals would have a positive impact on the Australian aviation industry. However, the public benefits are potentially higher in the case of V Australia.

7.39 The Commission is aware that V Australia's operations on the United States have been loss-making, as has been disclosed publicly by the company. Its entry to the route has coincided with the global financial crisis which has affected the profitability of all carriers but has intensified the normal challenges faced by a new entrant carrier. For V Australia, developing scale and broadening its portfolio of routes is likely to be important in enabling the airline to establish its operations profitably over the longer term and so ensure Australia continues to be represented by a second long-haul carrier outside the

Qantas Group. Thus far, the United States route is the only one on which V Australia has operated. However, the airline will launch flights on the Thailand route later this year, and start services to South Africa in early 2010. Access to the Fiji route on the scale it has proposed will further broaden its market access, improve aircraft utilisation and allow greater spreading of the airline's fixed costs.

Conclusion

7.40 The Commission considers that both V Australia and Qantas are reasonably capable of obtaining the necessary approvals and of implementing their proposals, and therefore meet the paragraph 4 criteria. The Minister's policy statement makes it clear that use of capacity by Australian carriers which meet paragraph 4 is of benefit to the public.

7.41 Under paragraph 5.2 of the Minister's policy statement, in applying all criteria, the Commission should take as the pre-eminent consideration the competition benefits of each application. The Commission considers that both proposals bring strong competition benefits, but there are clearly greater competitive benefits likely to be associated with the splitting of capacity in the way proposed. The capacity splitting proposed results in two new carriers rather than one, and will see greater frequency and capacity operated. This should further intensify competition to fill seats.

7.42 Each carrier brings unique product features to the route. Both offer efficient modern aircraft with low cost structures which should enable them to compete vigorously with one another and the incumbent carriers.

7.43 There will be new competition for the premium market component and in the freight market through V Australia's entry. The ability to offer daily flights is important in both these market segments.

7.44 Both V Australia and Jetstar will compete strongly in the leisure market, which makes up the bulk of demand on the route. Four services per week for Jetstar should be sufficient for it to compete effectively in the leisure market. The air services arrangements provide scope for airlines to seek approvals for supplementary services in the peak periods which are characteristic of the pattern of demand on the Fiji route. Qantas argued in responding to the draft submissions that the Commission should not take account of this possibility in the same way as it has not taken account of any possible capacity expansion under any air services talks which might take place. However, the Commission notes that potential for approvals for supplementary services in peak periods is already provided for under the existing arrangements. While it would be a matter for the authorities to decide whether or not approve any such application, it would be open to Jetstar to seek supplementary services should it so wish.

7.45 Both carriers offer extensive networks behind the Sydney gateway, which will enable competition for traffic from regions other than Sydney, such as Perth. These networks may become more important if capacity becomes constrained from other gateways such as Brisbane and Melbourne as demand grows.

7.46 Having assessed the two applications against the paragraph 5 criteria, the Commission finds public benefit is likely to be maximised by the allocation of 907 seats per week to V Australia and the allocation of 852 seats per week to Qantas. This gives the

two carriers approximately an equal share of the available capacity and results in the allocation of all but one seat from the pool of available seats. The Commission will make allocations on this basis.

7.47 The Commission will also authorise code sharing by Qantas on Jetstar's services as requested. This will strengthen marketing of those services.

7.48 The Commission's allocations effectively exhaust the Australian capacity entitlements remaining available to be allocated. The Commission is therefore keen to see that both airlines implement their services as quickly as possible, and that neither leaves capacity idle beyond the times they have indicated they will use the capacity. The Commission will require the capacity to be fully utilised by the dates proposed by the airlines and will monitor their implementation plans. Any extension of time that might be sought for the implementation of services would be granted only in exceptional circumstances. However, the Commission would maintain its normal flexibility towards capacity utilisation over the life of the determinations to take account of particular circumstances which might eventuate from time to time, consistent with the requirements of the Minister's policy statement.

7.49 As noted above, the Commission is concerned about the possible effect on the balance of public benefits if circumstances change materially, during the life of the determinations, from those on which the Commission has based these determinations. Accordingly, the Commission will issue interim (three year) determinations which will mean that the allocations of capacity can be reviewed at the renewal stage earlier than compared with a full five year determination.

8 Interim Determination allocating capacity on the Fiji route to Virgin Blue International Airlines Pty Ltd (V Australia) ([2009] IASC 131)

8.1 The Commission makes a determination in favour of V Australia allocating 907 seats of capacity per week in each direction on the Fiji route, in accordance with the Australia – Fiji air services arrangements.

8.2 The determination is for three years from the date of the determination.

8.3 The determination is subject to the following conditions:

- V Australia is required to fully utilise the capacity from no later than 31 December 2009 or from such other date approved by the Commission;
- only V Australia is permitted to utilise the capacity;
- V Australia is not permitted to utilise the capacity to provide services jointly with another Australian carrier or any other person without the approval of the Commission;
- changes in relation to the ownership and control of V Australia are permitted except to the extent that any change:

- results in the designation of the airline as an Australian carrier under the Australia – Fiji air services arrangements being withdrawn; or
 - has the effect that another Australian carrier, or a person (or group of persons) having substantial ownership or effective control of another Australian carrier, would take substantial ownership of V Australia or be in a position to exercise effective control of V Australia, without the prior consent of the Commission; and
- changes in relation to the management, status or location of operations and head office of V Australia are permitted except to the extent that any change would result in the airline ceasing to be an airline designated by the Australian Government for the purposes of the Australia – Fiji air services arrangements.

9 Interim Determination allocating capacity on the Fiji route to Qantas Airways Ltd (Qantas) ([2009] IASC 132)

9.1 The Commission makes a determination in favour of Qantas, allocating 852 seats of capacity per week in each direction on the Fiji route, in accordance with the Australia – Fiji air services arrangements.

9.2 The determination is for three years from the date of the determination.

9.3 The determination is subject to the following conditions:

- Qantas is required to fully utilise the capacity from no later than 30 April 2010 or from such other date approved by the Commission;
- only Qantas or another Australian carrier which is a wholly-owned subsidiary of Qantas is permitted to utilise the capacity;
- Qantas is not permitted to utilise the capacity to provide services jointly with another Australian carrier or any other person without the prior approval of the Commission;
- the capacity may be used by any wholly-owned subsidiary of Qantas to provide joint services with Qantas;
- to the extent that the capacity is used to provide joint services on the route, Qantas and any wholly-owned subsidiary of Qantas must take all reasonable steps to ensure that passengers are informed of the carrier actually operating the flight at the time of booking;
- changes in relation to the ownership and control of Qantas are permitted except to the extent that any change:
 - results in the designation of the airline as an Australian carrier under the Australia – Fiji air services arrangements being withdrawn; or

- has the effect that another Australian carrier, or a person (or group of persons) having substantial ownership or effective control of another Australian carrier, would take substantial ownership of Qantas or be in a position to exercise effective control of Qantas, without the prior consent of the Commission; and
- changes in relation to the management, status or location of operations and head office of Qantas are permitted except to the extent that any change would result in the airline ceasing to be an airline designated by the Australian Government for the purposes of the Australia – Fiji air services arrangements

Dated 5 November 2009

John Martin
Chairman

Philippa Stone
Member

Ian Smith
Member