SUBMISSION TO THE AUSTRALIAN COMPETITION AND CONSUMER COMMISSION

Application for authorisation by Virgin Australia and Air New Zealand

Introduction

1. Thank you for the opportunity to make a submission on the application by Virgin Australia (VA) and Air New Zealand (Air NZ) to the Australian Competition and Consumer Commission (ACCC) requesting authorisation for a codeshare agreement between the two airlines on the Tasman market. The agreement would allow VA to place its code on a free sale basis on Air NZ operated trans-Tasman services (excluding Queenstown).

2. NZ Airports is the industry association for New Zealand's airports and related businesses. Its members[1] operate 46 airports across the country including the international gateways to New Zealand. This infrastructure network is essential to a well-functioning economy and enables critical transport and freight links between each region of New Zealand and between New Zealand and the world.

3. NZ Airports represents all international and regional airports in New Zealand. This gives us a keen interest in creating and maintaining a competitive aviation market for travel between Australia and New Zealand.

4. We take a first principles approach regarding the issues for approving airline alliances and strongly hold to the principle that aviation as a sector, and air travel consumers, are best served by having strong competition that provides consumers with choice and competitive airfares. We have recently submitted to New Zealand's Ministry of Transport in support of reauthorising some airline agreements, because we recognised the consumer benefit. However, every agreement needs to be considered on its merits.

5. NZ Airports' submits that the ACCC should decline this application because it would limit competition on the trans-Tasman market, resulting in less consumer choice and upward pressure on airfares. Crucially, approval of the application would remove the viable potential for increased competition for the five-year period of the codeshare. We submit the negative impact on trans-Tasman travellers outweighs the benefits that will accrue to the carriers themselves in terms of being able to target high yielding travellers.

[1] Our member airports: Ardmore Airport, Ashburton Airport, Auckland Airport, Bay of Islands Airport, Chatham Islands Airport, Christchurch Airport, Dunedin Airport, Gisborne Airport, Hamilton Airport, Hawkes Bay Airport, Hokitika Airport, Invercargill Airport, Kaikohe Airport, Kaitaia Airport, Kapiti Coast Airport, Marlborough Airport, Masterton Airport, Matamata Aerodrome, Motueka Airport, Nelson Airport, New Plymouth Airport, North Shore Airport, Oamaru Airport, Palmerston North Airport, Pauanui Airfield, Pukaki Airport, Queenstown Airport, Rangiora Airfield, Rotorua Airport, Takaka Airport, Taupo Airport, Tauranga Airport, Te Kowhai Airport, Thames Aerodrome, Timaru Airport, Wairoa Airport, Wanaka Airport, Wellington Airport, West Auckland Airport, Westport Airport, Whakatane Airport, Whanganui Airport, Whangarei Airport.

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6. The key reasons this application should not be approved are:

    - The benefits are limited and accrue to a small number of VA customers, primarily business and loyalty customers, who wish to fly across the Tasman.
    - The trans-Tasman market is less competitive now than it was pre-Covid.
    - Approval would risk short and long-term negative impacts on consumers on the Tasman market. In the short term it could drive up airfares by displacing existing Air NZ passengers with higher yielding passengers without increasing capacity, and in the longer term it entrenches the current level of competition on the Tasman for at least five years.

Benefits of the codeshare are limited would accrue to a small number of consumers at the expense of the potential for stronger Tasman competition.

7. The applicants outline in their proposal the key benefits of their codeshare.

8. VA outlines that the agreement will provide their customers with various benefits including:

    - Access to VA coded trans-Tasman services on Air NZ.
    - Ability to redeem velocity points and accrue status credits on VA coded Air NZ. services.
    - Ability to use Air NZ's seven international lounges.

9. It is vital to highlight that these benefits mainly accrue to Virgin Australia travellers who wish to fly across the Tasman, in particular loyalty and frequent flyer customers. While we acknowledge there will be benefits for this small group, we submit that the benefits are strongly outweighed by the anti-competitive impact on the Tasman that will impact a much wider group of consumers. We go into further detail later in the submission on the Tasman impact.

10. Air NZ state that for them the proposed agreement would 'drive increased passenger numbers (including high yield passengers such as corporates and SME customers) onto its trans-Tasman and domestic services'. Without offering increased capacity, new high yielding customers accessed via the VA network would simply displace existing Air NZ customers and put upward pressure on airfares, which is not in the broader interests of consumers.

11. This is of particular concern in a market where Air NZ short-haul flights (Australia and Pacific) are at 84%[2] load factor, meaning there is little extra capacity on existing flights. Airfares on the Tasman are up 74%[3] on pre-COVID levels. This data indicates the market requires extra capacity, which this codeshare does not require and will in fact act as a disincentive to.

12. Almost 700,000 New Zealanders live in Australia and 70,000 Australians live in New Zealand. These consumers rely on being able to fly back and forth to see family and friends at an affordable price and this agreement would see them displaced by higher paying corporate and SME customers from the Virgin network.

[2] https://www.airnewzealand.co.nz/monthly-investor-updates

[3] AirportIS

The Tasman market is less competitive than it was pre-Covid

13. NZ Airports disagrees with the applicants' characterisation of the trans-Tasman market as highly competitive.

14. The following table shows that prior to Covid around 77% of the Tasman capacity was provided by Air NZ and the Qantas Group. Over the next 12-months, over 90% of Tasman capacity is scheduled to be operated by Air NZ, Qantas and their JV partners Emirates, a significant concentration of power in a two airline duopoly, with the residual 8% provided by airlines that provide limited competition mainly in Auckland (China Airlines, Air Asia X, LATAM Airlines, China Eastern Airlines, Batik Air.).

AKL/WLG/CHC Tasman Capacity				
	YEJan20	Share	YEOct24	Share
NZ	3,426,201	38%	3,176,489	42%
QF/JQ/EK	3,488,457	39%	3,813,705	50%
Other	2,077,867	23%	568,360	8%
Total	8,992,525	100%	7,558,554	100%

Source: Sabre Market Intelligence   Note EK has a Joint Venture with the Qantas Group

15. We note that Emirates (EK) services on the Christchurch-Sydney route is within the EK/QF joint venture, allowing coordination on capacity and pricing for Christchurch to Sydney flights. Also of note is that Air NZ and Qantas group are code-sharing on domestic AU or NZ sectors when part of trans-Tasman journeys.

16. Significantly, Air Asia X announced in December 2023 that they were pulling out of Auckland from February 2024, further reducing competition. Air Asia's forthcoming exit from the Tasman market will increase the Air NZ and Qantas Group's market share to 92%.

17. Passengers departing Wellington for Australian airports are served solely by the two airlines, Air New Zealand and Qantas Group. Auckland and Christchurch passengers have more choice but that is only on international carriers transiting through an Australian airport. These other carriers require 5th freedom rights, and many have limited ability to operate from main gateway airports in Australia due to air rights caps or curfews.

18. Other airlines find it uneconomic due to the impact of Australian government transit visa requirements on passenger demand. Many of the 5th freedom airlines (e.g., Air Asia X and Batik Air) that are operating on the Tasman do not compete directly with Air NZ or Qantas due to their foreign customer base and lower-cost product.

19. The forthcoming exit of Air Asia X is significant as it demonstrates that sustained competition on the Tasman requires an operator for whom the Australia and New Zealand business is core to their business model. VA is the only such carrier that could provide sustained competition.

20. There is no other New Zealand carrier with the ability to operate on the Tasman routes. In Australia, while REX and Bonza have aircraft types within their fleets that could operate on the Tasman, their limited fleet, network and domestic market focus, means this is unlikely to occur in the foreseeable future. In our view, Virgin Australia is the only Australian carrier with the aircraft and customer base to operate on the Tasman, therefore Virgin Australia is the only airline that can provide genuine competition.

21. Airfares are also significantly higher, an increase of 74%, on the Tasman compared to pre-Covid, a consequence of the limited competition and capacity.

The proposed agreement would have negative short and long-term impacts on trans-Tasman travellers.

22. As acknowledged by Air NZ in the application, a key benefit to Air NZ from this agreement would be to drive increased passenger numbers (including high yield passengers such as corporates and SME customers) onto its trans-Tasman and domestic services. Without offering increased services that increase overall seat capacity in the market, new high yielding customers accessed via the VA network would simply displace existing Air NZ customers and put upward pressure on airfares, which is not in the broader interests of consumers.

23. This means the short-term impact of the agreement would simply be to allow Air NZ to access a group of higher paying customers, rather than increasing capacity.

24. In the longer term, this agreement creates a strong disincentive for Virgin to resume Tasman services for the next five years because it allows their customers to access a Tasman service without them having to resume a route themselves. This disincentive to create new capacity for five years is not in the interests of wider consumers and five years is very long period to entrench such a barrier to competition. Even if VA acknowledge new services on the Tasman are not part of their current plans, this agreement would entrench that position for far too long.

25. VA argues that it is merely agreeing to purchase flights and some ancillary benefits, such as redeeming air miles and access to airport lounges, from Air NZ for its existing passengers. However, the application creates a strong disincentive for VA to attempt to deploy their own capacity into more Tasman markets as their customers can access NZ flights.

26. Air NZ benefits by reducing the potential for competition, and potentially greater overall capacity, from the only carrier (VA) that could meaningfully compete on the Tasman.

Approval of this agreement risks maintaining or enhancing the current low levels of competition in the trans-Tasman aviation market

27. Approval of this application immediately reduces the potential future competition that VA presents to Air NZ. To quote the ACCC's submission on the terms of reference for the Commonwealth's Aviation White Paper:

    "A competitive airline sector is vital to meet the needs of consumers and the economy more broadly, ….. Rivalry between airlines can deliver more routes, a greater choice of products, cheaper airfares, more reliable services and better customer service."

28. Referring again to the ACCC's White Paper submission, NZ Airports' notes that Rex's presence as a third airline on some domestic routes between major Australian cities has had the effect of immediately and substantially lowering the combined revenue per passenger for Jetstar, Qantas, Virgin Australia and Rex. The ACCC noted in that case:

    "Competition between more airline groups will generally result in better services and more attractive pricing."

29. The potential for competition from VA (being a well-regarded Australian domestic airline with meaningful sales and distribution strength) entering the trans-Tasman market is a stronger pro-competition factor than any other third airline entering the trans-Tasman market. To state this factor another way, removing the potential competition by VA would

have the greatest possible anti-competitive effect on what is significant market power held by Qantas Group and Air NZ.

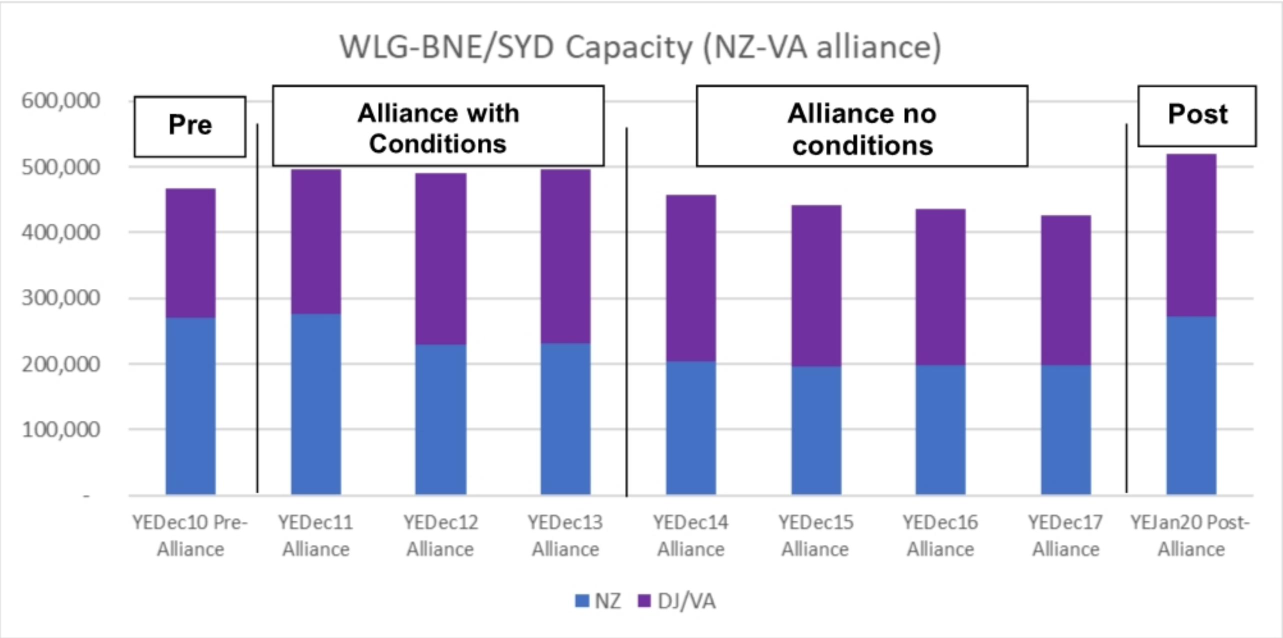
30. The applicants highlight the importance of New Zealand to outbound Australians (second largest market), and the difficulty VA has competing domestically in Australia for certain market segments (e.g. high value corporate customers) without its customers having access to connectivity, lounges and loyalty benefits on trans-Tasman routes beyond Queenstown (ZQN). While the codeshare arrangement gives VA access to New Zealand on Air NZ aircraft, the counterfactual is that the absence of connectivity will place more pressure on VA to reinstate the services they used to operate prior to Covid, thus providing an incentive for VA at some point to provide more competition on the trans-Tasman market to Air NZ and the Qantas Group.

History indicates the proposed agreement will reduce available seat numbers in the trans-Tasman market.

31. In general, the history of airline joint ventures has been to limit competition and reduce capacity rather than enhance markets and grow. That can be justified when there are strong consumer benefits, but in this instance those benefits do not outweigh the risks.

32. A previous agreement between VA and Air NZ which operated between 2010 and 2018 reduced competition and there is no reason this agreement would not have the same impact. Prior to the alliance between Air NZ and Virgin Blue (as VA were known at the time), the two airlines in competition operated around 467k annual seats between Wellington and Brisbane/Sydney. The alliance initially grew capacity (due to ACCC conditions) to reach 496k seats, however when these conditions were removed in 2013, the airlines gradually reduced capacity to below pre-alliance levels, reaching 426k in 2017.

33. In October 2018, at Air NZ's request, the alliance broke up into two independent competing airlines. The two competing airlines' capacity on the routes between Wellington and Brisbane/Sydney grew again, to reach 520k seats, which was greater capacity than both airlines in the pre-Alliance and peak-Alliance periods.

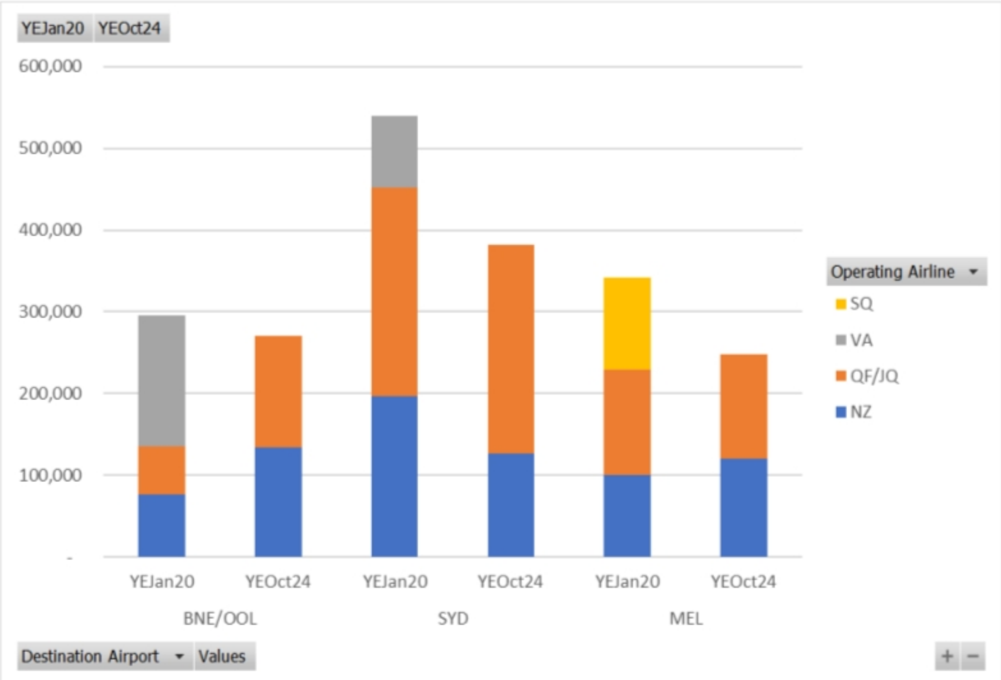


Source: Sabre Market Intelligence

34. Using Wellington Airport as a further example, it has become a duopoly on all Tasman sectors where it used to be fully competitive.

35. Prior to the Covid pandemic, Wellington Airport's trans-Tasman sectors were served by three independent airlines. Brisbane/Gold Coast was served by Air NZ/Virgin/Jetstar, Sydney by Air NZ/Virgin/Qantas, and Melbourne by Air NZ/Qantas/Singapore Airlines. Currently in the absence of Virgin/Singapore Airlines, all three sectors fall under the Air NZ/Qantas duopoly. WLG-Tasman capacity will be -23% lower YEOct24 than pre-Covid (YEJan20). BNE/OOL (grouped together due to overlapping markets) -8% (3 airlines drop to 2), SYD -29% (3 to 2), MEL -27% (3 to 2). Virgin flew 21% of WLG's Tasman capacity which has not returned.

<u>Trans-Tasman airline capacity to/from Wellington for the period 2020 to 2024</u>



Source: Sabre Market Intelligence

Summary

36. NZ Airports appreciates that arrangements between airlines are sometimes necessary and in the interests of consumers. As mentioned, we have made submissions to the New Zealand Ministry of Transport in support of reauthorising particular airline agreements. However, each agreement should be considered carefully for its impact on all consumers, not just certain groups.

37. In this instance, granting approval would substantially move the trans-Tasman market toward becoming a fully authorised duopoly. Approval removes significant competition on the trans-Tasman routes until one of the alliances (Qantas group or VA/Air NZ) decided to break apart.

38. The views of the ACCC expressed in its submission to the Aviation White Paper's Terms of Reference on the benefits from competition should guide its decision making on this application.

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Date:	5 January 2024