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~~Ms Margaret Arblaster~~

General Manager

Transport and Prices Oversight Branch

Australian Competition and Consumer Commission (ACCC)

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Dear Ms Arblaster,

**IATA Submission to the ACCC on the Preliminary Pricing Proposal of
Airservices Australia**

Thank you for inviting IATA to make its submission to ACCC on the Preliminary Pricing Proposal of Airservices Australia (AA). While AA has summarised and averaged their proposed increases on Page 17 of the document, there is no full table as provided in April at the AA industry briefing. IATA has assumed that there has been no change in the detail.

In this climate of significant financial hardship, the majority of the international airlines are simply trying to survive. Hence, it is unacceptable that providers of essential services would increase charges not just to recover the costs, and not even to maintain profitability, but to generate an increased profit. The airlines cannot absorb any further increases in costs.

Air navigation charges to the airlines should be based on the cost of providing the specific service. ICAO policies require that the costs of en-route services be identified separately from those of approach and aerodrome control services. The Australian Government also appears to have a similar view, in that it is opposed to the concept of the single till.

ACCC should also take into consideration that due to the formula being used by AA, the international airlines and the domestic operators of heavier aircraft are being made to subsidise the en-route air navigation services provided to the operators of lighter aircraft. The effect is compounded by the fact that AA maintains a large navigational infrastructure that is only required for local community operations. Further, it appears that AA may also be using the excess revenue from en-route air navigation charges to subsidise other loss making activities.

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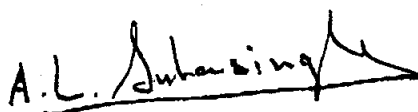
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International Air Transport Association

The international airlines should not be made to subsidise such loss making activities as the fulfilling of community obligations, Government's international obligations, nor any other commercial or non-commercial activity.

Although the time and information made available for our response has been very limited and has prevented IATA in providing a more detailed response, we nevertheless thank the ACCC for giving the industry the opportunity to respond to the Preliminary Pricing Proposal of Airservices Australia. We are confident that the ACCC will take our views into consideration and will endeavour to make a decision that is fair and equitable to all concerned.

Yours sincerely,



Lasantha Subasinghe
Assistant Director, User Charges

Enclosed: (I). IATA Submission to the ACCC on the Preliminary Pricing Proposal of Airservices Australia,

(II). Attachments 1 through 3;

1. *IATA Director General's letter to the Hon John Anderson, MP Deputy Prime Minister and Minister for Transport and Regional Services*
2. *Australian Governments Direction 22 of 19 April 2001*
3. *IATA Traffic Forecast 2001-2005 Special Interim Edition (Relevant Pages Only)*

**International Air Transport Association's Submission to the Australian
Competition and Consumer Commission on the Preliminary Pricing Proposal of
Airservices Australia**

Airservices Australia is the monopoly service provider of an essential public service, without which air transport, as it is currently used in Australia, would not be feasible. AA will continue to be a monopoly in the foreseeable future, particularly in the provision of en-route air navigation services.

AA, as stated on page 5 of its submission, provides several different services to the airlines, other operators of aircraft, and the Australian Government. However, AA has not made public the relevant cost and revenue information of each of these activities, some of which are provided at specific locations to different users.

1 Policies on Air Navigation Services Charges

Australia is a contracting state to the Convention on International Civil Aviation as pointed out by AA. Article 15 of the Convention provides for charges to defray the costs of providing facilities and services for civil aviation.

The International Civil Aviation Organisation, in consultation with the contracting States, Australia being one of the more active participants, has developed policies on charges which are published in ICAO's Doc. 9082/6 "ICAO's Policies on Charges for Airports and Air Navigation Services".

Paragraph 36 of ICAO Doc. 9082/6 states "*...where air navigation services are provided for international use, the providers may require the users to pay their share of the related costs; at the same time, international civil aviation should not be asked to meet costs that are not properly allocable to it. The Council therefore encourages States to maintain accounts for the air navigation services they provide in a manner which ensures that air navigation services charges levied on international civil aviation are properly cost-based.*"

Sub-paragraph iii) of Paragraph 38 states that "*The cost of air navigation services provided during the approach and aerodrome phase of the aircraft operations should be identified separately.*"

Paragraph 40 states that "*The proportions of cost attributable to international civil aviation and other utilisation of facilities and services should be determined in such a way as to ensure that no users are burdened with costs not properly allocable to them according to sound accounting principles.*"

Sub-paragraph v) of Paragraph 41 states that "*Where any preferential charges, special rebates, or other kinds of reduction in charges normally payable in respect of air navigation services are extended to particular categories of users, governments should ensure, so far as practicable, that any resultant under-recovery of costs properly allocable to the users is not shouldered onto other users.*"

The position of the Government of Australia, as stipulated in Direction 22 of 19 April 2001, with regard to assessing prices for airports, is clear that it does not support the concept of a single till. While this position is contrary to the ICAO policies on airport charges, it is perfectly in line with its policies on air navigation services charges. Therefore, there is no reason whatsoever for ACCC to allow AA to cross-subsidise within its portfolio.

AA provides en-route air navigation services in the continental and oceanic airspace of Australia as well as in the international airspace over the Indian and Pacific Oceans. AA also provides air navigation services for the approach and aerodrome phase of flights as well as aviation rescue and fire fighting services at Australian airports. In addition, it also provides consultancy services and conducts a number of other non-commercial activities.

However, the information provided by AA to the users does not provide the necessary transparency of costs or revenue of these separate activities. This is totally unacceptable to IATA and its Member airlines.

We seek the assistance of ACCC to obtain more detailed information so that we could determine the reasonableness or otherwise of the AA's pricing proposal.

In the event that ACCC is unable to obtain such information for review by the users, we urge the ACCC to determine the following:

- Cost and revenue of each specific service,
- The accuracy of cost allocation to the various businesses, particularly to consultancy and other non-commercial activities,
- The accuracy of the allocation of management and expert time and costs to each separate activity,
- Any negative impact of management involvement in activities outside core activities and the possible resultant efficiency loss in the core business of providing air navigation services,
- Services that do not recover full costs and the shortfall.

ACCC should ensure that the loss-making activities are not subsidised with revenue generated from charges to airlines in other services, particularly en-route air navigation services.

2 Efficiency of Airservices Australia's Operations

2.1 Efficiency of AA's Cost Base

Due to the lack of transparency of information, IATA is unable to comment on the efficiency of the various specific costs for the different services provided by AA, and for which separate charges apply.

Although IATA does not support the comparison of charges in different countries, in the absence of the required information, such comparison appears to be the next best alternative to ascertain the efficiency of the cost base. Due to time constraints, IATA has only been able to compare the charges for en-route air navigation services. The comparison has been made with the charges in Canada, South Africa, Russian Federation and New Zealand. These States have been chosen in view of the similarity of the airspace with that of Australia and the type of traffic.

En-route Charges Comparison

	Distance	Charge in AUD		
	KM	737-400	747-400	DHC-8 300
Australia	100	37.45	92.57	19.34
Australia Proposed	100	38.90	96.14	20.09
Canada	100	30.20	74.64	16.20
New Zealand	100	47.02	110.15	21.63
New Zealand Oceanic	100	12.39	22.46	8.41
Russian Federation	100	106.39	139.64	78.13
South Africa	100	19.74	45.72	11.56

(All charges are for en-route air navigation services for 100 km of flight.)

Canada and South Africa have the most number of similarities with the Australian airspace, its level of complexity, traffic density, and the aircraft mix. The Canadian charges, which include the cost of MET services, are 25% less for a DHC-8 aircraft while they are 29% less for B747 and B737 aircraft than the proposed charges in Australia. The South African charges are 74% less for a DHC-8, 90% less for a B737 and less than half the price for a B747 aircraft. AA comment on Page 18 of 6% and 10% increases for NAVCANADA and South Africa are not relevant as even after the increases they are still less costly than AA.

New Zealand has two different sets of charges, in keeping with the vastly different costs and infrastructure requirements for continental airspace and for the oceanic airspace. While the continental charge is on average around 15% higher than the proposed charges for Australia, the oceanic charges are over 3 and 4 times cheaper for the B737 and B747 respectively, while the charge for a DHC-8 is nearly two and a half times less than the proposed charges. Hence, the charge per flight for services provided by Airways Corporation of New Zealand are much less than they are for the same distance in Australia.

It should be noted that the domestic or continental airspace in New Zealand is so different to that of Australia that their ability to recover income for the similar level of services provided is very restricted. Given the limited distances in New Zealand, it is a testimony to the lower cost of Airways Corporation that the charges between the two countries are so close.

Russian Federation also has an airspace similar to that of Australia, although unlike Australia, a large area of the country is influenced by extreme weather conditions for most part of the year. The published charges have been adjusted to take account of the MET and SAR costs so that the comparison is meaningful. The charge for a B747 in the Russian Federation, which does not have the most up to date air services system and carries with it numerous inefficiencies, is just 27% higher than the proposed charges.

Given that all these air navigation service providers fully recover their costs, it could be concluded that there still is significant room for improvement in AA's cost efficiency.

2.2 The Level of Operating Costs Included in AA's Proposal

As stated earlier, in the absence of a detailed cost breakdown, IATA has not had the opportunity to examine the different cost items and hence, is unable to comment in any great detail. However, we still have the following comments on the summary version of the consolidated accounts of AA:

IATA was made to understand that AA did not recover full costs of providing approach & aerodrome navigation services and aviation rescue & fire fighting services at several locations. AA also informed that the AUD 7 million government subsidy was insufficient to cover all the costs at some of these locations. Therefore, it could be deduced that AA is using revenue from other activities to subsidise the said services.

ACCC should ensure that AA does not over-charge the international airlines in order to recover these losses. Allowing AA to do so would be against the ICAO policies on user charges. This also applies to the activities carried out by AA on behalf of the government. The Australian Government's international obligations should be paid for through either the general treasury or an equivalent reduction in AA's returns and not by airlines through inflated charges.

2.3 AA's Incentive, and effectiveness, to contain and reduce costs

AA appears to have concluded that it has achieved close to maximum efficiency during the past 4-5 years. During the Industry Consultative Forum "Waypoint 2002" on 22 April 2002, AA stated that "Another financial objective of the Business Transformation Program was to reduce costs by AUD 90-100 million. This target has now been achieved. As staff numbers are the primary driver of operating expenses, continual year-on-year cost reductions would be difficult to achieve."

As stated elsewhere in this submission, IATA believes that significant further efficiencies could be achieved. IATA Member airlines, operating in a competitive market environment, have been successful in continually reducing their unit costs during the past decade. IATA does not see any reason why the air navigation service providers cannot do the same. However, similarly to the airline industry, it may require some form of stimulus for AA to undertake further cost reductions.

In the event the Australian Government were to consider liberalisation of the provision of en-route air navigation services, such competition could be possible. As a first step, the services provided in the oceanic airspace could be considered.

However, such changes may not be a reality in the near future. Hence, the drive towards further efficiencies would have to be encouraged through regulatory means, the only real alternative to competition. IATA and its Member airlines depend on ACCC to ensure such an outcome.

3 Traffic Volumes

3.1 *The Appropriateness of Lower volumes as a case for increased prices*

Civil aviation is a cyclical industry with downturns that normally correspond to the state of the economy. However, the current situation in Australia is a culmination of several extraordinary events, such as the unfortunate events of 11 September and the demise of Ansett Australia. Therefore, it would be highly inappropriate for a monopoly provider of an essential service to be allowed to increase charges, particularly when the increase is being sought in order to increase profitability and not just to recover the costs of providing the service.

AA is a going concern, and should take into account the future growth prospects in developing its pricing policies. The short-term less than average growth in activity, particularly given that it is due to extraordinary circumstances, should not be allowed to form part of any consideration as the basis for an increase in charges.

In developing its building block analysis, AA appears to be advocating the use of a five-year nominal risk free rate. This appears to confirm IATA's view that the business plan, which includes the activity forecast, should also be considered on a rolling mid-term basis.

3.2 *The Reasonableness of AA's Forecast for Activity Growth*

IATA is of the view that the 0.6% activity growth for international traffic is conservative. This view appears to be supported by the independent review carried out on behalf of AA by the Centre for Asia Pacific Aviation.

Further, IATA is also of the view that a pricing proposal of a going concern should not be based on a very short-term forecast, particularly when exceptional circumstances are at play. Given that AA has been able to achieve a profit of 7.4% even in the worst possible year for civil aviation in its entire history, it would be more reasonable and prudent to take a longer-term view. A mid to long-term forecast would also be more accurate given the current uncertainties not only in the economy but also on security.

IATA has had to revise its forecasts in view of the unfortunate events of 11 September 2001. The revised full forecast is only expected to be completed by September this year and hence, regret that we are unable to provide our views in detail.

However, IATA has published a special interim edition of its passenger forecast, which takes in to account the events of last year. This interim forecast unfortunately, does not give specific details on the Australian market. Nevertheless, it gives an indication of the trends, as the more global figures are available.

The total world-wide international passenger traffic growth is expected to be 0.9% in 2002, while it is forecast to grow at a rate of 7.9%, 5.9% and 5% during 2003, 2004 and 2005 respectively. The South Pacific, which includes Australia, Far East routes traffic is expected to grow at 1% in 2002 and 3%, 4% and 4% in 2003, 2004 and 2005 respectively. Australia in view of its economy, and the general situation with the country's security, has the greatest potential and would have growth rates higher than the average for the region. Hence, AA's activity growth, which starts from a contracted base, would be significant during the next three years and it is unacceptable that pricing would be based on the uncertainties of the very short-term.

4 Rate of Return

IATA, given the timeframe to respond, does not intend to make a detailed submission with regard to this matter. However, IATA would like to make the following observations:

AA's assertion in Page 19 of its submission that; "the 5 year results reflect the extent to which customers have benefited while the shareholder has foregone profitability" is inaccurate.

As per the Convention on International Civil Aviation to which Australia is a signatory, the provision of air navigation services is the responsibility of the State. The Australian Government has commercialised this service in order to minimise the significant inefficiencies inherent in the provision of such services through a Department of Government. The level of inefficiencies that existed, as stated in AA' submission on Page 11, is clear from the fact that the commercialised AA has been able to reduce operating costs by over AUD 80 million per annum within the short span of four years since 1998. The staff numbers are also said to have been reduced by 37%. Prior to adopting commercial practices, the provision of air navigation services in Australia is said to have been making a loss. Hence, AA would have been a strain on the general treasury.

Since becoming a commercial authority, AA has been making profits and would have paid over a AUD 100 million to the Government as taxes and dividends during the past 3 years alone. Funds, that were not available to the Government, prior to commercialisation. In addition, the major liability of employee superannuation has been transferred from a Government responsibility to AA. Therefore, as much as the users of services have benefited from the transformation to a more efficient entity, the Government of Australia, the shareholder has also benefited significantly over the past five years.

The profitability analysis in Page 19 of the AA's submission is misleading. The indicated EBIT/Sales measure for 1998/99 appears to be inclusive of the massive amount of abnormals amounting to AUD 219 million. These abnormals should not be taken into consideration in the profitability analysis of AA.

Over AUD 200 million of the AUD 219 million had been incurred in the effort to improve efficiency in the form of Separation and Redundancy payments, Devaluation of property, Plant & equipment and Business Transformation programme costs. Cost of inefficiencies that the airlines have previously had to pay through inflated charges.

Once the abnormals are removed from the calculation, the true profitability of AA becomes evident. In our calculations, the EBIT/Sales measure for 1998/99 is 9.4% and not -27.2% as stated by AA.

AA also appears to have inflated operating costs by 5%, as stated in Page 22 of its submission, in order to mitigate some perceived risk, which we do not understand. This 5%, if allowed by ACCC to be used to inflate costs, should also be included in the calculation of profitability, given that the allowable profitability should be in line with the total risk of the business. Hence, the total profitability of AA in its pricing proposal for 2002/03 is 13.6% and not 9.1% as claimed.

Therefore, the 3-year average profitability of AA is in fact a very healthy 12.4% while the 5-year average is 12%.

5 Structure of Prices

5.1 *Whether the proposed prices are likely to reflect AA's costs of providing services*

As stated earlier, IATA is disappointed that AA has not provided all the necessary information to ascertain whether or not the charges for the different services are cost justified. As demonstrated in Paragraph 1.1, AA's charges for en-route air navigation services are considerably higher than those that are charged by other air navigation services providers with comparable airspace and traffic mix.

Further, it has been identified that the Government subsidy to AA is insufficient to cover all the losses AA is making on community services. IATA is concerned that the revenue from the high en-route charges may be being used to cover the difference.

AA continues to maintain and operate a significant amount of navigational infrastructure that is not required by the airlines operating modern aircraft. Such navigational infrastructure, it is understood, is an Australian requirement for local community operations. IATA urges ACCC to ensure that the cost of these facilities are not burdened on the airline operators, who have invested significant amounts on new technology as required by the international civil aviation community, and are already paying higher charges than those operating lighter aircraft for similar services.

Cost of providing air navigation services is independent of the weight of the aircraft. However, as per AA's pricing structure, the charge for 100 km for a DHC-8 would be AUD 20, while the charge for the similar service for a B747 is nearly five times more. Hence, it is questionable whether the AA's pricing structure reflects the cost of providing services.

6 Impact on Users

IATA begs to differ with the analysis of the impact on users provided by AA. Appendix 8 of AA's submission, as far as the effect on international traffic is concerned, is misleading.

First of all, air traffic is quite often seasonal and it is unusual for international airlines to regularly achieve 80% cabin factor on B747-400 aircraft. A more realistic annual average would be around 65% for paying customers. AA provides air navigation services only on part of a flights full distance. In some cases, this part could be half, while for most international flights (Hong Kong, Bangkok, Tokyo, Los Angeles, etc.) the distance within Australian airspace is much less. There are no guarantees that other air navigation service providers will not follow AA's example. Hence, only the corresponding part of the airfare should be taken into account for such calculation. The fares used themselves raise doubts in our minds, but we do not wish to make any further comment on this matter at this stage. Except to say, that the airlines and their passengers are also facing unknown imposts following de-regulation of the major airports on 1 July this year.

Unlike Qantas and Virgin Blue, which appear to enjoy substantial growth due to very local extraordinary circumstances, the rest of the international airlines are currently going through significant hardship. It is believed that AA is using the short-term domestic loads of Qantas and Virgin Blue in this and most of the rest of its thinking. IATA believes, as previously stated, that AA is not considering the international airlines that provide around 40% of their income.

During the decade up to 31 December 2000, yields in US cents per Tonne-Kilometer, for IATA Member airlines on their scheduled international operations had declined on average by 1.7% per annum while the decrease during the last five years up to December 2000 was on average 3.3% per annum. Even with such drop in yields, the airlines were able to generate a cumulative profit for the past ten years of USD 10.2 billion on their scheduled international operations, mainly due to their success in reducing costs that were under their direct control.

However, the downturn in the global economy accelerated by the events of September 2001 has resulted in a loss of over USD 12 billion for the year, wiping out all the profits that had been earned up to that point. Making matters worse, passenger confidence has plunged to its lowest in history.

A number of airlines did not survive the crisis. Those airlines that did, have had to undertake very stringent cost reduction programmes in order to survive. Over 200,000 airline employees have lost their livelihood.

The airlines have had to embark on further reducing airfares to stimulate the market. The total world-wide international market has not yet recovered to its pre-crisis levels and the airlines will have to continue to offer discounted fares. Therefore, passing on the increased cost of AA's services may not be an option for many of IATA's Member airlines on their international routes.

Airline costs have also gone up in view of additional security, insurance, new taxes imposed by Governments and charges increases imposed by some monopoly service providers.

In this climate, the majority of the airlines are simply trying to survive. Hence, it is unacceptable that providers of essential services would increase charges not just to recover the cost and not even to maintain profitability but to generate an increased profit. The airlines cannot absorb any further increases in costs.

The Director General of IATA has appealed to the Minister of Transport and Regional Services of Australia, not to seek a profit from AA's operations for 2002/03. The letter is attached as part of IATA's submission.

7 Conclusions

AA's proposal to increase charges on average by 5.1%, which includes a 3.9% increase on en-route air navigation charges, is largely to increase its profitability from the current 7.4% EBIT/Sales to 9.1% for 2002/03. In fact, the real EBIT/Sales target appears to be 13.6%, given that a 5% risk factor has been used in the estimation of operating costs.

This is not acceptable to the international airline community, which is going through significant financial hardship, having lost USD 12 billion during 2001.

AA is a going concern, and should take into account the future growth prospects in developing its pricing policies. The very short-term less than average growth in activity, particularly given that it is due to extraordinary circumstances, should not be allowed to form part of any consideration as the basis for an increase in charges.

AA's charges for en-route air navigation services are higher than those charged by service providers with similar airspace and traffic mix. Hence, it could be concluded that there still is significant room for improvement in AA's cost efficiency.

Charges to the airlines should be based on cost of providing the specific service. ICAO policies require that the costs of en-route services be identified separately from the costs of approach and aerodrome control services.

ACCC should also take into consideration that due to the charges formula being used by AA, the international airlines and the domestic operators of larger aircraft are being made to subsidise the en-route air navigation services provided to the operators of lighter aircraft. The effect is compounded by the fact that AA maintains a large navigational infrastructure that is only required for local community operations.

Further, it appears that AA may also be using the excess revenue from en-route navigation charges to subsidise other loss making activities.

The international airlines should not be made to subsidise such loss making activities of AA, including fulfilling community obligations, Government's international obligations and other commercial and non-commercial activities.

AA appears to have become complacent with regard to the need for further efficiencies and cost containment. In the absence of competition, the only real way to ensure further improvement is through proper economic regulation. IATA and its member airlines are dependent on ACCC to ensure such outcome.

The information provided by AA to the users is inadequate and does not provide the required level of transparency. In the absence of sufficient detail, IATA has not been able to examine the pricing proposal in any detail, and hence is dependent on ACCC to ensure a thorough analysis of the proposal and a decision that is fair and equitable to all concerned.



Pierre J. JEANNIOT, o.c.
Director General & CEO

International Air Transport Association
MONTREAL/GENEVA

2 May 2002

Honourable John Anderson, MP
Deputy Prime Minister and Minister for Transport and Regional Services
Parliament House
Canberra, ACT 2600
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Dear Minister,

On behalf of IATA Member airlines I must bring to your urgent attention our concern at the proposed increase in charges by Airservices Australia. The events of 11 September, together with the downturn in the global economy, have resulted in an estimated loss of USD 12 billion for IATA Member airlines' international operations. Further, since September last year, some 200,000 airline employees have lost their livelihood and more job cuts are being announced.

We are fully aware of the impact on Airservices' revenues of the events of 11 September and the demise of Ansett. We were also encouraged by the stance taken by Airservices in the immediate aftermath of these events in deciding not to burden the airlines with increased charges. They are to be congratulated for the cost mitigation initiatives implemented, especially the personal sacrifices by some of the Airservices staff. However, even under such circumstances, Airservices still expects to return a profit of 7.4%. Regrettably the majority of the international airlines will not be able to recover their losses in the near-term, let alone make a profit or even consider raising airfares. Therefore, the airlines find the current proposal by Airservices to increase charges on average by 5.1% unacceptable, especially since the increase is largely to meet a target of 9.1% Earnings Before Interest and Tax (EBIT).

I urge the Government of Australia to consider a lower profitability for the next financial year such that Airservices would not be required to increase charges to the airlines. Your personal support and assistance to resolving this issue would be deeply appreciated.

Respectfully,

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CEOs of IATA Member airlines operating in Australia

COMMONWEALTH OF AUSTRALIA

Prices Surveillance Act 1983

DIRECTION NO 23

I, Joe Hockey, Minister for Financial Services and Regulation, in pursuance of section 20 of the *Prices Surveillance Act 1983*, hereby direct the Australian Competition and Consumer Commission, in exercising its powers and performing its functions under the Act in relation to the pricing of services at Sydney (Kingsford-Smith) airport, to give special consideration to the following matter:

- In assessing prices for aeronautical services, the Commission should not take into account the revenues generated, or costs incurred, in the provision of services other than aeronautical services.



JOE HOCKEY

19 April 2001



Passenger Forecast 2001-2005

Special Interim Edition

January 2002

International Air Transport Association

Page 1 of 11

EXECUTIVE SUMMARY

Special Interim Edition

This Special Interim Edition of IATA's five year passenger forecast has been produced as a direct consequence of the need to re-examine existing forecasts after the events of September 11th 2001. This edition provides a new forecast, based on the opinions of member carriers at the end of 2001, and contrasts this revised forecast with the original 2001-2005 forecast completed prior to September 11th.

Historical Developments

Based on figures from the International Civil Aviation Organisation (ICAO), international scheduled passengers reached 537.8m in 2000, an increase of 10.0% on 1999. This healthy rise, the highest since 1992, was helped by world GDP growth reaching its highest level (+4.7%) since 1984.

The graph below demonstrates that economic growth is a primary driver of international air passenger traffic growth. The period 1981-2000 saw international passenger traffic growth average 6.0% per annum, whilst the average growth in world GDP was 3.5% per annum,

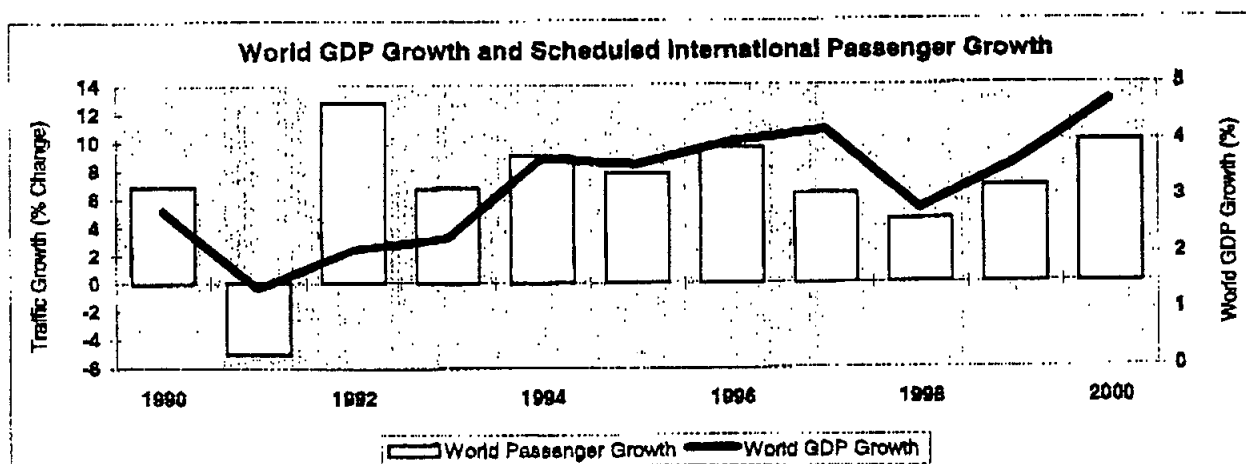
establishing a traffic growth rate at just below double the rate of GDP growth.

IATA's Original 2001-2005 Forecast

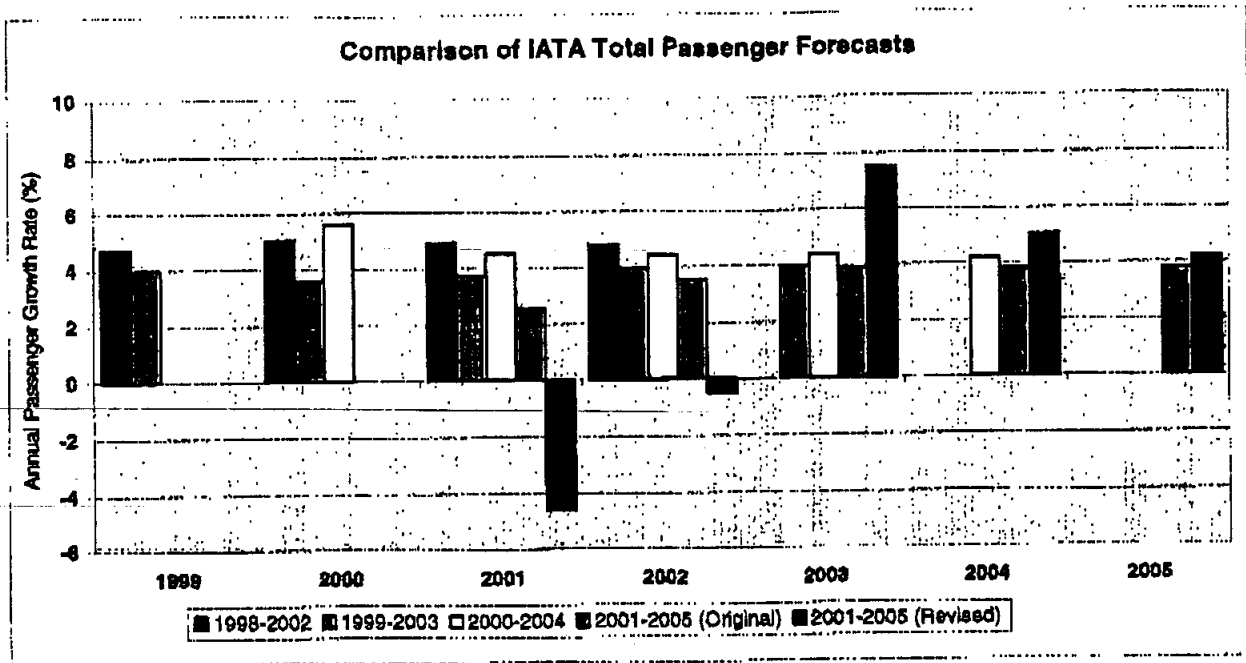
Completed in the third quarter of 2001, IATA's original 2001-2005 forecast predicted growth in *international* traffic to average 4.7% per annum during 2001-2005, down by 0.9 percentage points on the previous year's IATA five year forecast. This was primarily due to increased pessimism about global economic prospects, particularly in the US.

IATA's original *domestic* traffic projections were also markedly lower than in the 2000 forecast. Growth in scheduled domestic traffic was forecast to average 2.8% between 2001 and 2005, down 1.3 percentage points on the previous five year forecast.

For global total passengers, IATA's *combined* average annual growth rate (AAGR) for scheduled passenger services was projected at 3.5% for 2001-2005. Using the 2000 ICAO passenger data as a base, this equated to 1.95bn passengers being carried in 2005, 305m more than in the year 2000.



Source: IMF World Economic Outlook (December 2001); ICAO



IATA's Revised Forecast

The events of September 11th 2001 prompted a sharp downturn in passenger numbers in many markets, particularly to, from and within the USA, and prompted IATA to revisit the 2001-2005 forecast. Revised forecasts were submitted from member carriers during November and December 2001, to provide a post-September 11th consensus forecast.

Our revised forecast, taking into account the views of our member carriers and our own industry experts, projects growth in *International* passenger traffic averaging 3.5% per annum between 2001-2005, down 1.2 percentage points from our original forecast. This would result in 637m international passengers in 2005.

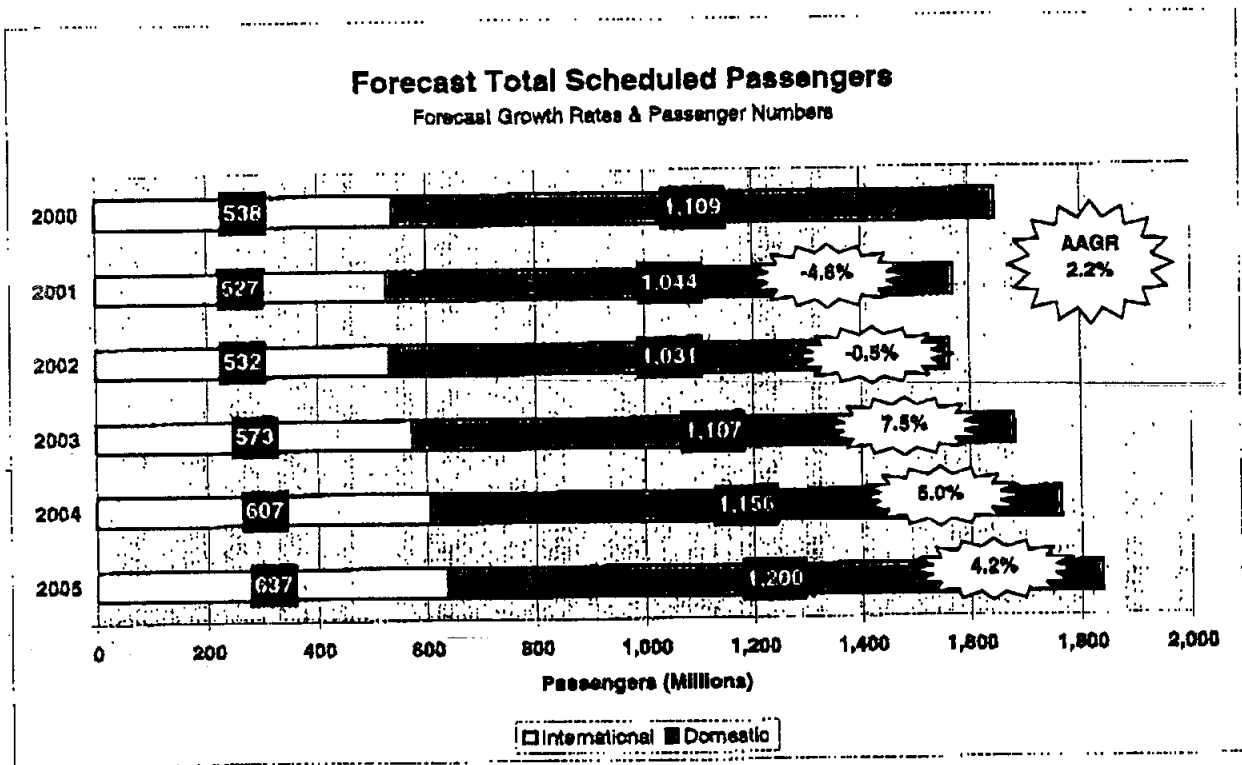
Domestic passenger traffic is now projected to grow at an annual average rate of only 1.6%. This provides a *combined* passenger traffic AAGR of 2.2%, down by 1.3 percentage points on our original forecast. In total, this equates to

an additional 190m passengers per annum at the end of the five years, bringing the annual total to 1.84bn in 2005.

In particular, it is now forecast that both international and domestic passenger numbers contracted in 2001, and that domestic numbers (of which US domestic are the largest group) will also contract in 2002. The combined passenger number for 2002 will be lower than in 2001. Both elements are projected to recover strongly in 2003, when passenger numbers should exceed 2000 levels for the first time.

Long-Term Passenger Prospects

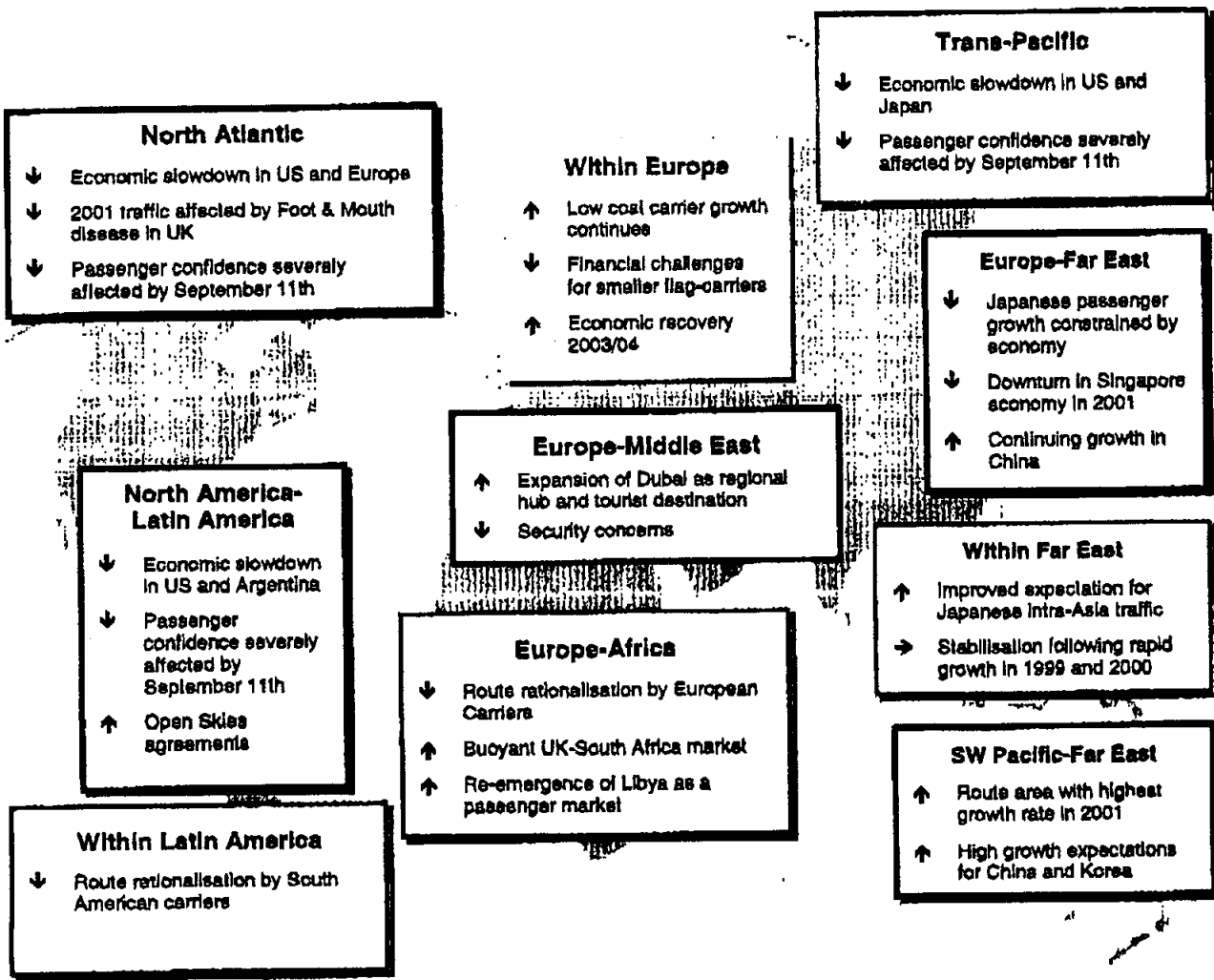
The AAGR for scheduled international passenger growth over 2006-2015 was forecast at 4.5% in the original forecast. We have retained this average growth projection for the longer term. Applying this growth rate to the 637m passengers projected in 2005, would result in 989m passengers per annum by 2015, an increase of 352m over the ten year period.



Annual Growth Rate (%)	2001	2002	2003	2004	2005	AAGR
TOTAL INTERNATIONAL	-2.1 (3.0)	0.9 (4.0)	7.9 (5.0)	5.9 (4.9)	5.0 (4.7)	3.5 (4.7)
North Atlantic	-10.5	1.0	11.7	5.3	4.8	2.3
Trans-Pacific	-9.5	-5.7	7.5	4.5	4.0	-0.1
Europe-Far East	-3.0	0.5	6.6	5.7	5.3	3.0
Europe-Middle East	-11.0	1.7	7.0	8.8	4.9	1.8
Europe-Africa	-0.8	2.0	8.0	8.0	4.8	3.6
North America-Latin America	-0.9	-4.0	8.8	6.5	5.2	3.0
South Pacific-Far East	1.1	1.0	3.0	4.0	4.0	2.8
Europe-Latin America	0.1	0.5	7.1	6.2	5.5	3.8
Within Europe	0.1	1.5	8.8	5.9	4.3	4.0
Within Far East	0.9	4.2	5.6	6.8	7.0	4.6
Within Latin America	-2.7	0.5	7.7	6.0	5.0	3.2
TOTAL DOMESTIC	-5.9 (1.0)	-1.2 (2.7)	7.3 (3.2)	4.5 (3.1)	3.8 (3.2)	1.8 (2.5)
TOTAL	-4.6 (2.0)	-0.5 (3.5)	7.5 (3.9)	5.0 (3.5)	4.2 (3.5)	2.2 (3.5)

Note: Original 2001-2005 Forecast growth rates are shown in brackets.

Regional Outlook 2001-2005: Broad Factors Affecting Passenger Growth Trends





3.2 International Outlook 2001-2005

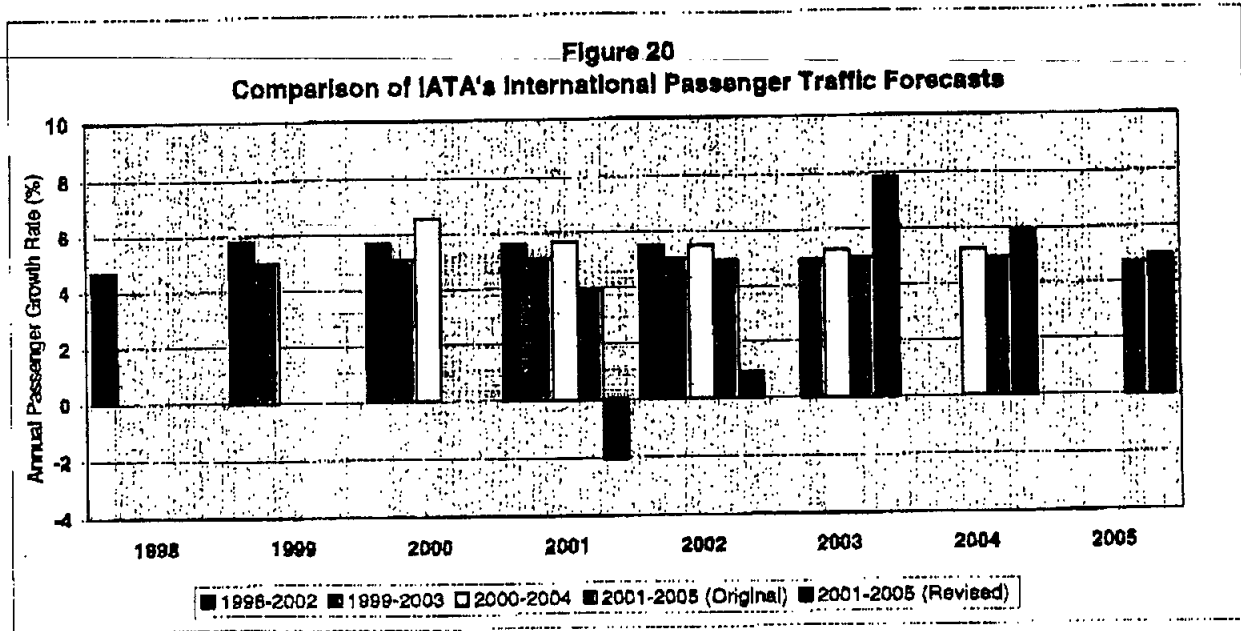
Following the increased optimism of IATA's 2000-2004 forecast when a five year AAGR of 5.6% was presented for international scheduled services, the original outlook for 2001-2005 was more cautious at 4.7%, reflecting the more difficult economic conditions then evident. Events since then have required a further reduction, to 3.5%. This is IATA's lowest ever five year AAGR forecast.

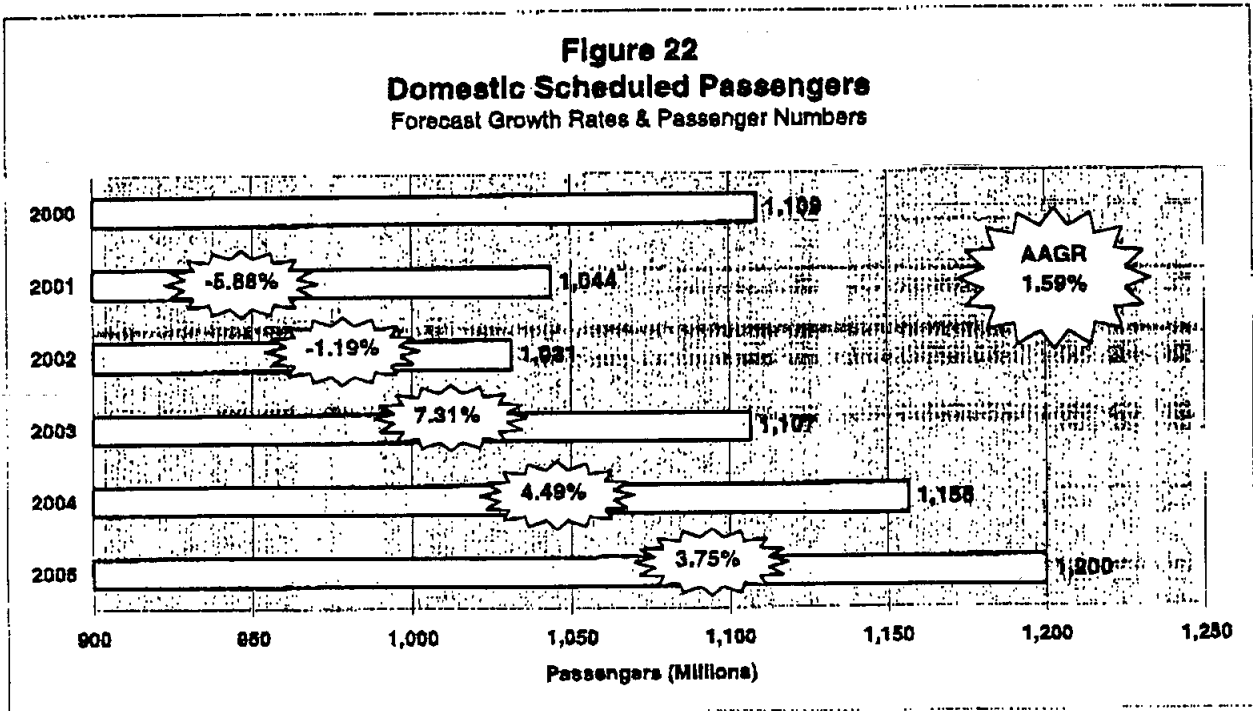
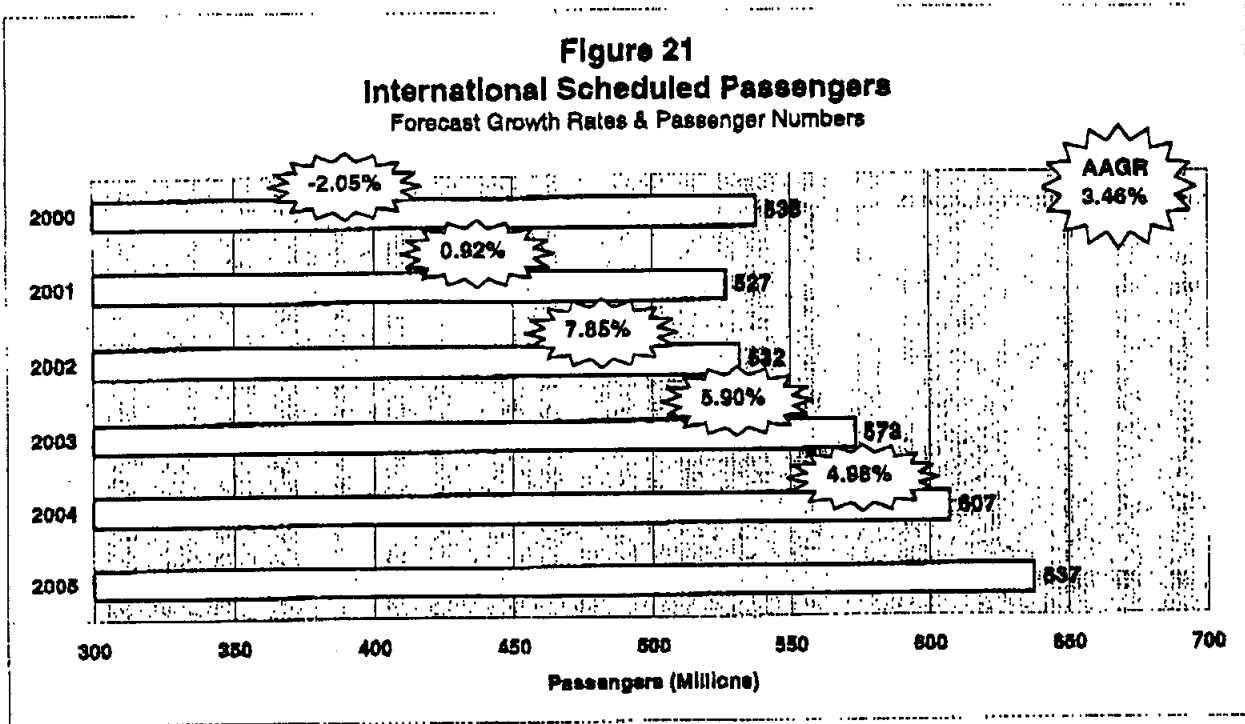
Based on ICAO figures for 2000, this Interim projection would generate 637m international scheduled passengers in 2005.

This forecast represents a rise of almost 100m passengers from the base 2000 figure of 538m passengers, but is 39m passengers fewer than projected for 2005 in the original 2001-2005 forecast.

**Table 3
Comparison of IATA's International Passenger Traffic Forecast Growth Rates (%)**

Period	1997	1998	1999	2000	2001	2002	2003	2004	2005	AAGR
1997-2001 Forecast	7.00	6.80	6.90	6.60	5.90	-	-	-	-	6.60
1998-2002 Forecast	-	4.70	5.80	5.70	5.60	5.50	-	-	-	5.50
1999-2003 Forecast	-	-	4.96	5.08	5.08	5.05	4.91	-	-	5.02
2000-2004 Forecast	-	-	-	6.56	5.66	5.46	5.27	5.24	-	5.64
2001-2005 Forecast (Original)	-	-	-	-	3.89	4.89	4.87	4.92	4.74	4.68
2001-2005 Forecast (Revised)	-	-	-	-	-2.05	0.92	7.86	5.90	4.98	3.46
Actual Growth (ICAO)	6.50	4.50	6.60	10.0						







3.3 Domestic Traffic Outlook 2001-2005

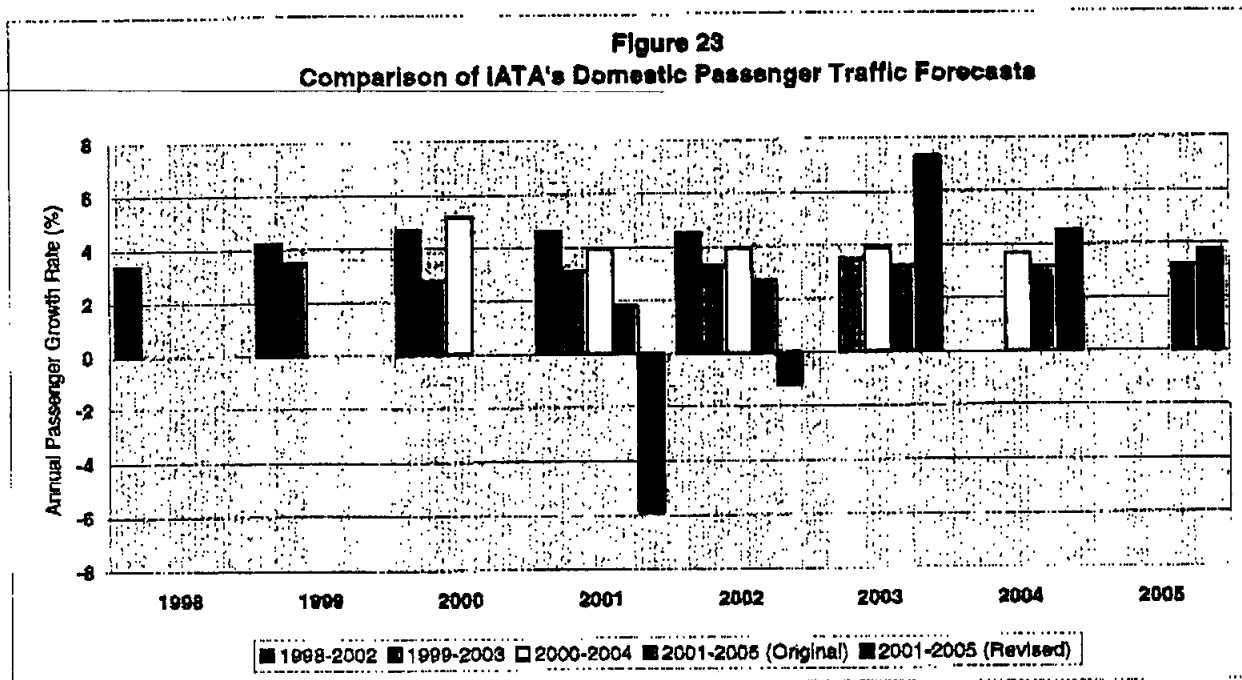
US domestic market trends have particularly impacted on the overall domestic outlook for the period 2001-2005 shown in Table 4 and Figure 23. Our original forecast predicted a decline in the five year AAGR to 2.8% for domestic passengers. It is now evident that US domestic passenger numbers fell in 2001, contributing to a decline in global domestic passengers. Using

ICAO numbers as a base for 2000, our revised AAGR of 1.6% will result in the total number of scheduled domestic passengers climbing from 1.11bn in 2000, to 1.20bn in 2005, an increase of 91m passengers.

Our original forecast would have realised an increase of 169m passengers. IATA's recent domestic forecasts are shown in Figure 23.

Table 4
Comparison of IATA's Domestic Traffic Forecast Growth Rates (%)

Period	1997	1998	1999	2000	2001	2002	2003	2004	2005	AAGR
1997-2001 Forecast	5.40	5.60	5.10	5.40	5.00	-	-	-	-	5.30
1998-2002 Forecast	-	3.40	4.20	4.70	4.80	4.50	-	-	-	4.30
1999-2003 Forecast	-	-	3.49	2.81	3.07	3.33	3.45	-	-	3.23
2000-2004 Forecast	-	-	-	5.18	3.94	3.93	3.93	3.64	-	4.12
2000-2005 Forecast (Original)	-	-	-	-	1.89	2.73	3.22	3.14	3.21	2.82
2001-2005 Forecast (Revised)	-	-	-	-	-5.88	-1.18	7.31	4.49	3.75	1.59
Actual Growth (ICAO)	4.1	-0.4	5.5	3.8						





3.4 Total Market Outlook 2001-2005

Table 5 shows that IATA's revised five year AAGR for scheduled international and domestic passenger services is now 2.2% for 2001-2005, compared to 3.5% in our original forecast and 4.6% for 2000-2004. The revised forecast represents IATA's lowest ever AAGR for passenger growth.

Using ICAO actual passenger numbers and IATA's revised projections, total passenger

numbers are projected to reach 1.84bn per year by 2005, an additional 190m over 2000.

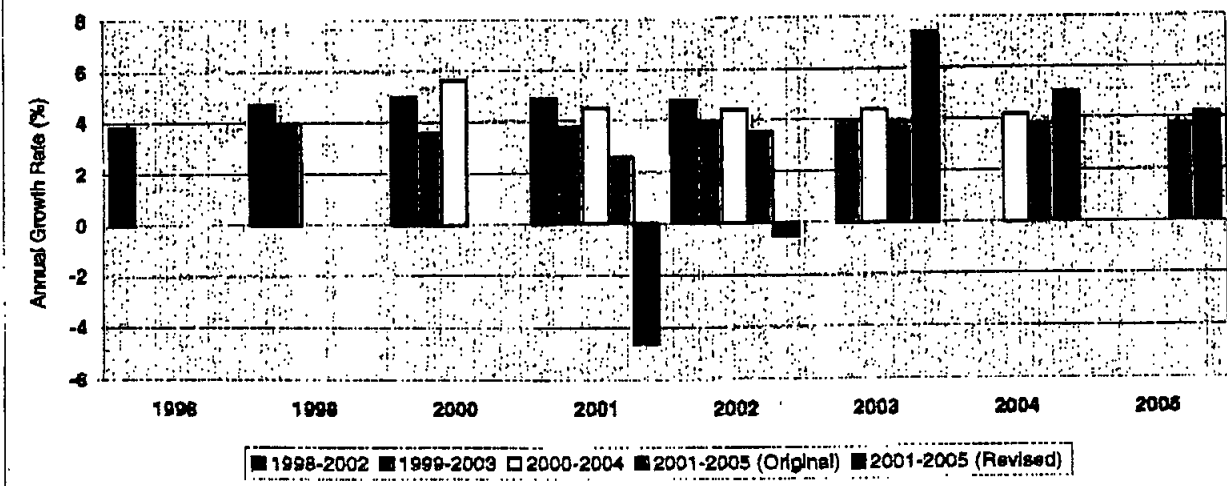
Figure 25 shows the division in scheduled passenger numbers between domestic and international traffic. The former accounted for 67.3% of total international passenger numbers in 2000.

However as growth in international traffic continues to exceed its domestic counterpart over the forecast period, this share is set to fall to 65.3% by 2005.

**Table 5
Comparison of IATA's Total Traffic Forecast Growth Rates (%)**

Period	1997	1998	1999	2000	2001	2002	2003	2004	2005	AAGR
1997-2001 Forecast	5.80	6.00	5.60	5.70	5.90	-	-	-	-	5.70
1998-2002 Forecast	-	3.80	4.70	5.00	4.90	4.80	-	-	-	4.70
1999-2003 Forecast	-	-	3.97	3.57	3.75	3.92	3.96	-	-	3.83
2000-2004 Forecast	-	-	-	5.61	4.49	4.42	4.37	4.16	-	4.61
2001-2005 Forecast (Original)	-	-	-	-	2.58	3.51	3.88	3.80	3.78	3.50
2001-2005 Forecast (Revised)	-	-	-	-	-4.6	-0.5	7.5	5.0	4.2	2.21
Actual Growth (ICAO)	4.80	1.00	6.10	5.76						

**Figure 24
Comparison of IATA's Total Passenger Traffic Forecasts**



Far East-SW Pacific

When viewing the forecast for this route area, perhaps the most noticeable feature is not the decrease between the original and revised forecasts, but between the 2000 growth and that predicted in the following years.

The remarkable growth in traffic in 2000 was attributable to the Sydney Olympics, and a decline following this was to some extent a natural market correction. Nevertheless, this route area (being geographically far removed from North America and the Middle-East) not only retained a positive 2001 growth rate in the revised forecasts, but also has the highest growth predicted for any route area in 2001.

Over the five year period the region still exhibits a decline in AAGR of nearly two percentage points (Table 18), the main contributor being a further softening of the forecasts growth from Japan to Australia and in particular to Guam. Whilst uncertainty over the Japanese economy is felt in many route areas, these two (in common with Hawaii) are based on an expectation of reduced Japanese-originating leisure travel over the forecast period. In contrast, growth prospects between Australasia and such countries as Malaysia, Thailand and Indonesia, remain strong, and are relatively unaffected by this revision to IATA's forecasts. Lastly, it should be noted that, although presently small market-pairs, both China and Korea are forecast to achieve AAGRs to Australasia approaching or exceeding double-digit levels during the period 2001-2005.

4.6 Far East-South West Pacific

Table 18
Comparison of IATA's Far East-South West Pacific Passenger Forecast: Post-Sept. 11th v. Pre-Sept. 11th

	2000 (actual)	2001	2002	2003	2004	2005	AAGR
Forecast Annual Growth Rate (%)							
Revised Forecast	12.1	1.1	1.0	3.0	4.0	4.0	2.6
Original Forecast	12.1	3.4	4.5	4.9	4.8	5.0	4.5
Variance	0	-2.3	-3.5	-1.9	-0.8	-1.0	-1.9

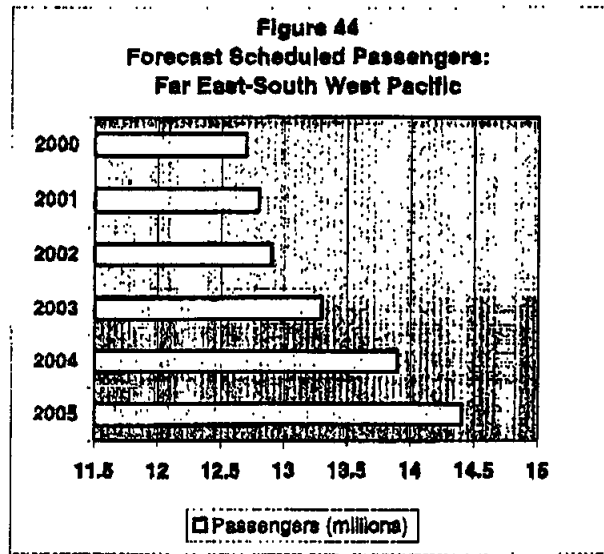
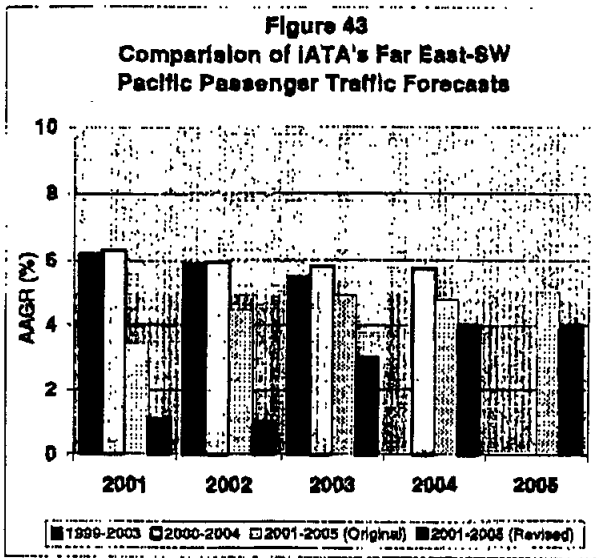
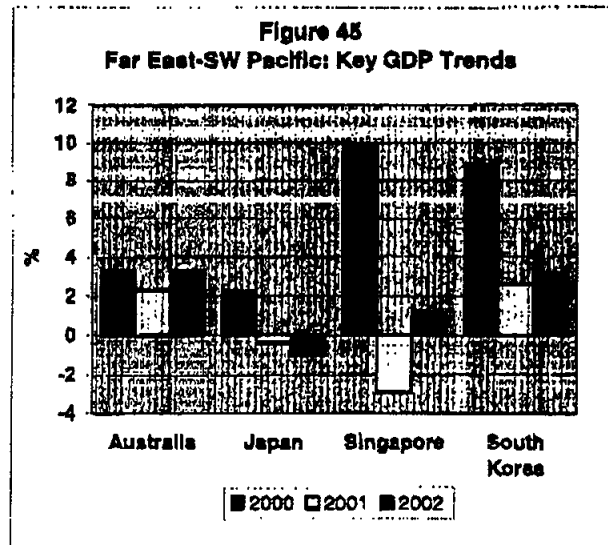


Table 19
Far-East-South West Pacific - Selected Key Country Pairs

Rank	Country-Pairs	2000 Passengers (Million)	2005 Passengers (Million)	AAGR
1	Australia-Singapore	2.87	3.20	3.65%
2	Guam-Japan	2.23	1.99	-2.26%
3	Australia-Japan	1.80	1.73	1.50%
4	Australia-Hong Kong	1.25	1.41	2.50%
5	Australia-Malaysia	1.00	1.30	5.37%
6	Australia-Thailand	0.80	0.99	6.60%
7	Australia-Indonesia	0.75	1.05	6.97%
8	New Zealand-Singapore	0.33	0.41	4.59%
9	Australia-Korea	0.32	0.49	9.00%
10	Australia-Chinese Taipei	0.22	0.22	0.30%



Source: IMF World Economic Outlook (December 2001)