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## **PUBLIC REGISTER VERSION**

Ms Jaime Martin  
Acting Director – Competition Exemptions  
Australian Competition and Consumer Commission  
23 Marcus Clarke Street  
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**By Email:** [jaime.martin@acc.gov.au](mailto:jaime.martin@acc.gov.au)

Dear Jaime

### **Qantas-JAL: Response To Submission From Virgin Australia**

We refer to the application (**Application**) for authorisation lodged with the Commission on 18 December 2020 by Qantas Airways Limited (**Qantas**) and Japan Airlines Co Ltd (**JAL**) (together, the **Applicants**) in relation to a proposed Joint Business Agreement (**JBA**) (**Proposed Conduct**) and to the submission lodged by Virgin Australia (VA) dated 27 August 2021 (**VA Submission**).

The Applicants wish to respond to certain points made in the VA Submission.

Although VA acknowledges that airline alliances can deliver benefits that are not otherwise possible, it is disappointing that this is not reflected in its views on the Proposed Conduct – particularly given the obvious context of international flying markets needing to be rebuilt as quickly and as sustainably as possible. In this environment, the Proposed Conduct maximises the likelihood of air links being sustainably restored across a wide range of routes between Australasia and Japan as demand recovers and borders open.

As the Applicants have previously said, the focus for the Commission's assessment of public benefit and public detriment needs to be pragmatic and realistic in the context of current, unprecedented market conditions. A theoretical risk of future competitive harm should not be given disproportionate and undue weight when there are immediate and tangible public benefits that would be delivered by the Proposed Conduct, and actual and immediate public detriments which would occur without it.

The VA Submission focuses on the challenges to its own ambitions to potentially operate to Japan in future. These challenges flow from fleet decisions, difficult market conditions and structural issues that are unrelated to the Proposed Conduct and which are likely to persist, irrespective of whether authorisation is granted.

The Applicants' response to specific points in the VA Submission are set out below:

- **VA suggests that the effects of the Proposed Conduct would extend beyond the term of the authorisation.** This assertion is baseless. Qantas/Jetstar and JAL take compliance with competition laws extremely seriously. Any suggestion about inappropriate future coordination is unwarranted. Qantas has had experience of unwinding alliances in the past (such as when the Qantas-British Airways joint business ceased in 2012) and the Applicants would assume that Virgin Australia has



also had similar experience in respect of its relationships with Delta Airlines and Air New Zealand, which are no longer authorised by the Commission.

- **VA suggests the Proposed Conduct would raise barriers to entry on Australia-Japan routes.** This is not a credible objection to the Proposed Conduct. The facts are:
  - Contrary to VA's claims, from an air services perspective there are no material regulatory barriers to entry or expansion on services between Australia and Japan. The Australia-Japan air services arrangements permit the entry of multiple Australian and Japanese air passenger and freight carriers on routes between Australia and Japan. The open skies agreement between Australia and Japan, signed in 2011, provides for unrestricted capacity to operate international air services between the two countries. The Proposed Conduct has no bearing on this open access.
  - While there are some restrictions on access to Tokyo's Haneda Airport, this does not prevent entry to other ports in Japan. For example, slots at Tokyo's Narita Airport or at other gateways (such as Osaka or Sapporo) are easy to obtain. Again, the Proposed Conduct has no bearing on access to Haneda or any other port.
  - In any event, VA has been granted slots at Haneda Airport and its utilisation of those slots will be unaffected by the Proposed Conduct. The air services arrangements between Australia and Japan provide for one frequency per day for an airline of each country to operate a passenger service between Australia and Haneda during prescribed late night and early morning hours (between 2200 and 0655 hours).<sup>1</sup> In 2019, the Japanese MLIT released four new Haneda day slot pairs for Australian carriers (two slots pairs) and Japanese carriers (two slot pairs) and these slots became available for use in April 2020. The IASC has most recently granted VA an extension until 31 October 2021 to use those slots, which is consistent with the extension granted to Qantas.<sup>2</sup> This waiver, or the ability for the IASC to grant a further waiver if deemed necessary, is not impacted by the Proposed Conduct.
  - If VA's 'strong intentions' to enter Australia-Japan routes are credible, the Applicants note that:
    - such intentions support the Applicants' argument that VA – in addition to ANA – is an actual direct competitive constraint, which should give the Commission further comfort in relation to any perceived competitive detriment;
    - if VA decides to enter Australia-Japan routes, VA itself has acknowledged challenges relating to demand volatility and ongoing uncertainty. These barriers to entry and ongoing threats to sustainability will exist irrespective of the Proposed Conduct. The Applicants believe that any failure or further delay in VA's plans to launch the services would be more likely attributable to the ongoing impacts of the Pandemic and VA's fleet planning, rather than to the Proposed Conduct. It is notable that VA has prioritised the acquisition of narrow body 737-800 NG aircraft to be deployed on its mainline domestic network in 2022,<sup>3</sup> and which would not be capable of flying Australia-Japan routes; and
    - if, as some of VA's comments suggest, demand will take some time to return, then it follows that VA's potential entry is more likely part of a longer term plan (which in turn suggests any assessment of whether and how such entry could be impacted by the Proposed Conduct is premature). As noted above, hypothetical theories of future potential detriment should not outweigh actual and significant public benefits deliverable now.
- **VA proposes slot divestment as a remedy to address barriers to entry.** The Applicants do not agree that the Proposed Conduct raises barriers to entry. In any event, VA's suggestion of slot

<sup>1</sup> See further 'Haneda Airport open for Australian airlines', Media Release Hon Anthony Albanese MP, (then Minister for Transport), 30 September 2011. Available: <https://anthonyalbanese.com.au/haneda-airport-opens-for-australian-airlines> and <https://www.executivetraveller.com/australia-japan-open-skies-agreement-flights-to-haneda-allowed>.

<sup>2</sup> See [IASC Resolution](#) [2021] IASC R03 in respect of the Japan Route.

<sup>3</sup> See [Virgin Australia media release](#) 'Virgin Australia Finalises new agreements for nine Boeing 787-800 G Aircraft,' 27 August 2021.

divestment as a remedy is as extraordinary as it is untenable. Slots at Haneda Airport are a valuable economic resource. VA already has slots available for use at Haneda Airport and easy access to slots in ports in other parts of Japan but is not utilising those rights, nor indicating it will do so (i.e. VA has not published a schedule to Haneda nor commenced any selling to Japan at all). It remains unclear whether and how VA will utilise its existing allocation. It therefore makes no economic sense for more slots to be awarded to VA. Divestment is an entirely inappropriate remedy in circumstances where overall barriers to entry are not high, and where the Proposed Conduct does not make market entry any more difficult for VA in practice than it would otherwise be.

- **VA considers that public benefits could be achieved through a codeshare.** This is not correct. The significant public benefits – outlined again below – would all *only* become possible through the ‘metal neutral’ joint business. The metal neutral nature of the joint business would give the Applicants sufficient commercial incentive to increase network access and extend customer benefits. This commercial incentive will not otherwise exist. As the Applicants have previously confirmed to the Commission, arms-length codeshare partners who do not pool revenue will always have an incentive to fill seats on flights that they operate themselves, where they will receive and retain the full fare instead of just the portion of a fare received from a codeshare sale. This limits codeshare partners’ willingness to share capacity and fails to capture integrative efficiencies that are achieved with metal neutrality.

Without the Proposed Conduct, the Applicants would have no commercial incentive to expand their existing limited codeshare. The codeshare would not expand to include direct services between Australia-Japan, any domestic services in Australia or Japan or any additional routes across the Tasman.

In addition, codeshare partners have no incentive to improve frequent flyer benefits to the maximum extent possible. It is only with a metal neutral joint business that airlines are incentivised to provide the same (highest) value to members of another carrier’s frequent flyer program.

As recently as March this year, the Commission accepted that metal neutral joint businesses facilitate material public benefits. In re-authorising the Qantas-American Airlines alliance – which has been in place since 2011, and re-assessed and re-approved by multiple regulators over time – the Commission noted the importance of metal neutrality in aligning the commercial incentives of the parties to deliver benefits which would otherwise not occur (or would only occur to a limited extent). For example, the Commission stated;

*‘The ACCC accepts that the [alliance] aligns the Applicants’ incentives in relation to `capacity, scheduling, sales and marketing. The ACCC considers that this has and is likely to continue to result in public benefit in the form of improved schedule choice, reducing travel and transit times.’<sup>4</sup>*

*‘The ACCC considers that the [alliance] has facilitated significant capacity growth and introduction of new routes by the Applicants during the previous periods of authorisation. The ACCC considers that, compared to the likely future without the [alliance], continuation of the alliance provides a greater likelihood of increased capacity and new routes in future as the airlines benefit from passenger feeds arising from their complementary networks. The ACCC considers that this constitutes a material public benefit.’<sup>5</sup>*

*The ACCC considers that the attractiveness of the Applicants’ loyalty programs is enhanced under the alliance, and that the benefits of reciprocal access to loyalty programs accrue to alliance passengers who are members of an alliance loyalty program. Given the large number of frequent flyer members and the range of benefits that might accrue to them,<sup>6</sup> the ACCC considers this is likely to result in a public benefit.’<sup>6</sup>*

These principles are the same for the Proposed Conduct in this case.

- **VA queries whether the public benefits would be passed on to consumers.** This ignores the real

<sup>4</sup> Commission [Final Determination](#) on Qantas/American Airlines alliance, para 4.43.

<sup>5</sup> Ibid, para 4.39.

<sup>6</sup> Ibid, para 4.49.

and substantiated public benefits that have been clearly put to the Commission by the Applicants, including detailed information about those benefits and a confidential comparison with the counterfactual scenario provided by each of Qantas and JAL.

To summarise, beyond the broader restorative effects for tourism and trade industries, the Proposed Conduct would deliver immediate and tangible benefits directly to consumers including:

- more sustainable capacity reinstatement on the Sydney-Tokyo route (flowing from support provided through joint sales, marketing and distribution) rather than being more susceptible to cancellation and disruption due to poor loads. In the event that loads were still poor or there are other unexpected disruptions, having a codeshare on this direct route would also at least enable the swifter and more seamless re-accommodation of passengers on to the other airline's service – thereby minimising disruption;
  - an accelerated reinstatement of daily services operated by both Qantas and JAL on the Melbourne-Tokyo route, with the ability to offer complimentary schedules giving consumers more choice;
  - diversified and accelerated capacity reinstatement including:
    - fast tracking the resumption of Qantas' services on both Sydney-Osaka and Sydney-Sapporo;
    - the introduction of new Qantas operated Cairns-Tokyo services;
  - increased schedule choice made possible by the metal neutral nature of the joint business, with Qantas customers having access to 14 new codeshare ports in Japan and JAL customers having access to 15 new codeshare ports in Australia and New Zealand. This will include expanded codesharing on the Tasman, facilitating new routings between New Zealand and Japan via Australia;
  - enhanced frequent flyer benefits again made possible through the metal neutral joint business – including increased points earn, increased status credit earn, increased top tier bonus earn and potentially reduced Qantas points required to redeem for seats on JAL marketed services. These enhanced customer benefits would not otherwise be made available; and
  - for corporate customers, additional seats, a better range of destinations, schedules, connectivity and enhanced frequent flyer benefits.
- **VA has again referred to the combined share of the Applicants, as they existed pre-Pandemic.** While pre-Pandemic share data was provided to the Commission as part of the Application, both VA and the Commission are well aware that the market conditions in which the Proposed Conduct would be implemented are going to be substantially different in the short to medium term. The impact of travel restrictions and on-going uncertainty regarding the resumption of international travel and the related impact on consumer confidence and demand for services must be appropriately accounted for in any analysis of net public benefits.

**VA states that the Proposed Conduct could adversely impact the state of competition in the domestic aviation market.** As the Applicants have previously stated, there is no basis for this argument. Competition in the domestic aviation market would remain unchanged if the Proposed Conduct was approved. This ongoing robust competition has been reflected in VA's announcement on 27 August 2021 of its acquisition of nine more 737 aircraft: *"These extra aircraft are an important part of our planning and ensure we're ready to ramp up flying and meet the pent-up demand for domestic travel as soon as the opportunity presents itself."*<sup>7</sup> The Applicants note that ANA is currently codesharing on VA's domestic Australia services (Adelaide-Sydney, Brisbane-Sydney, Cairns-Sydney, Melbourne-Sydney and Gold Coast-Sydney) through to Northern Summer 2022 and **[REDACTED JOINT CONFIDENTIAL]**

If you have any questions about the matters referred to above, please contact me on **[REDACTED]**

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<sup>7</sup> See VA media release: <https://newsroom.virginaustralia.com/release/virgin-australia-finalises-new-agreements-nine-boeing-737-800-ng-aircraft> (27 August 2021).

**CONFIDENTIAL]**

Yours sincerely



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Qantas Airways Limited