PERTH AIRPORT

WESTRALIA AIRPORTS CORPORATION

Industry Commission Inquiry: International Air Services Agreements and International Air Services Commission

SUBMISSION
Westralia Airports Corporation

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EXECUTIVE SUMMARY

Westralia Airport Corporation welcomes the opportunity to contribute to this Inquiry.

WAC believes there are three factors inhibiting competition for flights into and out of Perth:

i) lack of flexibility in existing bilateral agreements (including restrictive clauses);
ii) shortcomings in the consultation process in advance of bilateral negotiations; and
iii) existing cabotage arrangements.

WAC submits that Australia will benefit significantly from the adoption of a liberalised Air Services Agreements regime. The recommended model for liberalisation is a series of "open skies" agreements.

In addition, the current consultation and negotiation process for bilateral agreements can be significantly improved through the equal involvement of all key stakeholders.

An open, flexible approach to Air Services Agreements will encourage growth and competitiveness in Australian export and tourism industries and affiliated markets. For example, it is estimated that if the current Air Services Agreement restrictions were lifted, Perth International Airport's traffic could increase by 5 to 10 percent.

International airline activity and the passengers associated with it are a major source of regional employment throughout Australia, particularly for young people in service industries. The direct and indirect economic benefits therefore derived by local communities and their surrounding environs go far beyond the economic benefits derived by airports from traffic growth.

1. INTRODUCTION

Perth International Airport is the nation's fourth busiest airport and will serve in excess of 5 million passengers in 1998.

Westralia Airport Corporation (WAC) assumed management of Perth International Airport in July 1997 as the result of the Federal Government's Phase 1 airports privatisation program.

A focal point for business in Western Australia, Perth International Airport provides a fast, efficient service to the State's thriving export industry and a convenient point of entry for business travellers. By air, Perth is 10 hours from Tokyo, 9 hours from Hong Kong and 5 hours from Singapore and Jakarta. Perth also shares similar timezones with its Asian neighbours.

As a major enterprise centre, Perth International Airport directly and indirectly employs some 14,600 people. In financial terms a recent economic study found Perth International Airport contributes $1 billion a year to the Australian economy.

The Airport's facilities include both an international and domestic terminal complex and a three runway system with 24-hour curfew free operation. Recent commercial developments on the airport grounds include a state of the art mail centre, aviation maintenance facilities and outlets for leading retailers.

WAC's master plan and associated business strategies are designed to maximise growth opportunities in passenger and freight operations and expand the commercial and aviation activities located on the airport grounds. These strategies have been developed in close consultation with the Western Australian Government which recognises the Airport's key role in the growth of tourism and exports for Western Australia.

The Federal Government's airport privatisation program is a significant stimulus to increased competition in the Australian aviation industry. Privatised airport operators including WAC are actively investigating ways of increasing throughput and diversifying and expanding airport activities. As a result, new airport operators are investigating the establishment of regional business centres, new freight handling facilities, and importantly, working with other agencies to promote new tourism and export opportunities across Australia.

For these reasons, new airport operators such as WAC have a significant role to play in the ongoing development of Australia's aviation industry.

WAC welcomes the opportunity to contribute to this Industry Commission Inquiry and looks forward to contributing to increased competition in the aviation industry in Australia.

2. CURRENT REGULATORY MODEL: WAC EXPERIENCE

WAC acknowledges the steps taken by the Federal Government to increase flexibility within the bilateral process.

However, despite these efforts, existing Air Services Agreements are constraining new service opportunities to and from Perth International Airport. For consumers, these constraints are affecting frequency of flights, opportunities for lower pricing and alternative service options. Reduced competition is impacting on Perth International Airport's ability to expand, but also limiting the opportunities for export and tourism growth and the introduction of more competitive prices and services for consumers.

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i) lack of flexibility in existing bilateral agreements (including restrictive clauses);
ii) shortcomings in the consultation process in advance of bilateral negotiations; and
iii) existing cabotage arrangements.

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2.1 Restrictive Clauses and Lack of Flexibility

The Government is committed to negotiating capacity ahead of demand. Whilst in theory this policy can benefit all Australian markets, the system in actual application continues to provide benefits particularly to Eastern States markets.

Currently there are some 61 airlines approved to fly into Perth. However the majority of these are unlikely to take up these rights in the near future for commercial reasons. The rights have been allocated as part of a broader allocation during negotiations.

For Perth International Airport, the real challenge is in obtaining flexibility for those carriers who see a commercial return from commencing or increasing services to Perth.

Over the past twelve months, Perth has lost opportunities for increased activity as a result of restrictions in bilateral agreements. Of the 16 international carriers currently servicing Perth, either directly or through code share agreements, WAC is aware of two international carriers which have been discouraged from expansion of Perth services by existing restrictions in bilateral agreements or proposed conditions.

WAC has confirmed that in January 1997, Royal Brunei Airlines (RBA) sought extra capacity to increase its twice-weekly Perth services but was advised by the Department of Transport and Regional Development (DOTRD) that allocation of extra capacity would be conditional upon RBA also servicing one of two other smaller destinations in Australia. RBA decided against this condition on commercial grounds and therefore elected to not increase its capacity on the Perth route.

In addition, Malaysia Air Service (MAS) has held repeated discussions over the past twelve months with WAC and representatives of the Western Australian Government about their plans for expansion of services to Perth, however the existing negotiated capacity between Australia and Malaysia is insufficient to allow MAS to add any additional flights into Perth.

Finally, a number of new airlines have expressed interest in initiating service to Perth but are currently unable to do so due to restrictions in existing bilateral agreements. For example, Philippines Airlines (PAL) has indicated strong interest in initiating service into Perth, however restrictions of the existing bilateral agreement between Australia and the Philippines specifying routes, destinations and service levels prevents immediate implementation of their proposed new services. With the passing of time and the recent downturn in Asian economies, PAL may now elect not to proceed with a formal request for negotiations for access into Perth as other commercial priorities have arisen.

Were the services desired by these carriers implemented at the time the interest was first expressed, Perth International Airport would have realised a growth in International aircraft movements of between 4 - 8 services per week. On an existing base of approximately 80 services per week, this represents a foregone growth opportunity of between 5% - 10%, not to mention the loss of a new market - the Philippines - direct from Western Australia and open to travellers and exporters alike.

2.2 Consultation and Negotiation Processes for International Air Services Agreements

DOTRD is the primary agency responsible for developing a proposed negotiating position in advance of bilateral negotiations.

It is WAC’s understanding that the consultation over the negotiation process includes contact with Australia’s two international carriers (Qantas and Ansett International) and liaison with the Tourism Advisory Group (TAG) as well as other Federal Government agencies including the Department of Foreign Affairs and Trade and the Department of Industry, Science and Tourism. Membership of the TAG includes the Australian Tourism Commission, the Office of National Tourism, State representatives and peak industry representatives.

WAC has recently been advised informally that it will be offered full membership into TAG and looks forward to the opportunity of contributing formally within the group. Over the past eight months, the operators of the newly privatised airports have been given the opportunity to attend the planning segment of TAG meetings, but only as observers, not official delegates.

Of all the groups interested in the outcomes of bilateral negotiations, only the privatised airports and the airlines depend <u>directly</u> on the outcomes of those discussions. Airports and airlines alone derive their primary income from aircraft movements and all related “payload” components on board, and therefore the future of airports is dependent on the ability to expand aircraft movement activity.

Naturally, other members of TAG have a significant interest in overall tourism numbers delivered by aircraft movements. However, bilateral agreements are but one of a number of equally important factors impacting on growth in the tourism industry.

WAC believes that the operators of the newly privatised airports have a legitimate interest in the process and outcomes of the negotiating process that is in fact equal to Australia's two international carriers. **As such, WAC requests that a representative of the privatised airports be added to the government's direct negotiating team to balance the viewpoints at the table.**

WAC strongly believes that the current consultation process does not offer adequate opportunities for differing perspectives to be considered. Historically the national carriers have played a key role in the consultation process as "technical advisers". This offers them unique access to promote outcomes in the negotiating process which will be favourable to their respective competitive positions.

Airport operators have a clear interest in maximising throughput of aircraft, freight and passengers. Passenger and freight throughput increases when fares are competitive and there is a high frequency of flights. These commercial imperatives can be contrasted with the efforts of national airlines to protect their market share and maximise yields.

While WAC acknowledges and strongly supports the need for viable Australian domestic and international carriers, WAC believes the national carriers should operate under the same commercial and competitive conditions as other private industry enterprises. The regulatory regime should not afford the airlines special insulation from healthy competitive forces.

It is important to point out, however, that while both national airlines are generally regarded as "private" commercial entities, policies benefiting these companies have changed little since the time Qantas was a Commonwealth asset.

2.3 Cabotage Protection

WAC believes that the existing cabotage rules in Australia impact adversely on competition and thus reduce the opportunities for lower fares and greater capacity on domestic routes into and out of Perth.

The consumer benefits from increased competition were demonstrated in Western Australia with the introduction of Compass Airlines domestic services.

As a result of reduced air fares introduced by Compass, domestic air traffic at Perth International Airport in 1991 nearly doubled from its level the previous year. This growth was a direct result of lower domestic airfares offered by Compass. (The majority of seats between Perth and Sydney on Compass were below $400 round trip. These prices were generally matched by Qantas and Ansett.)

Following Compass' departure from the market, air fares offered by the two remaining domestic carriers again rose to pre-Compass levels and as a result, passenger and aircraft activity immediately declined to levels comparable to those prior to Compass' initiation. This point effectively illustrates the importance of and need for increased competition in the long-haul domestic air service market in Perth and across Australia.

Beyond the basic challenges of initiating a new major domestic airline, prospective candidates have faced, and will continue to face, great difficulties in gaining access to domestic terminal facilities. This point was made very clear by the recent efforts of Aussie Airlines. This highlights the need for alternative means to bring competitive forces to the Australian domestic air service market.

Cabotage, implemented in a sensible manner through case-by-case negotiations, would provide the necessary competitive impetus and offers an effective measure which could be implemented in the near term. Competition for domestic flights would be substantially improved if foreign international carriers were able to pick up domestic passengers. Cabotage would increase the availability of seats on major domestic routes and this could be expected to result in lower priced domestic fares.

International operators flying through Perth to Sydney are left with substantial passenger space once passengers have exited at Perth. For example, the South African Airways' (SAA) 747 300 regularly deposits approximately 30% of its passengers in Perth before flying on to Sydney.

If SAA were allowed to pick up domestic passengers on their continuing leg to Sydney (and returning to Perth from Sydney) there would be an immediate augmentation of between 300 - 500 seats per week in the Perth-Sydney market, the equivalent of 3 - 4 weekly 737-300 services. While this alone may not bring airfares between Perth and Sydney down to the especially attractive levels seen while Compass was flying, the additional seats would put significant downward pressure on ticket prices. It would also make Perth and the whole of Western Australia a more attractive market for additional SAA services.

3. OTHER ISSUES RELEVANT TO CURRENT REGIME

3.1 Freight

Cargo distribution, especially for perishable goods, is heavily dependent on the availability of direct and timely air services. Perishable goods exports is one of the fastest growing areas of the WA economy. It is also a very important factor in the WA air service equation because of its significant potential to contribute to airline yields, as the majority of air freight currently travels in the belly holds of passenger aircraft. Therefore, any increase in the capacity for passenger service will have a direct benefit for freight.

For any economy seeking to maximise export levels it is vital that access to air freight is not limited and that market forces are allowed to work which will in turn promote competition.

While WAC applauds the steps taken by the Government to increase the amount of dedicated freight capacity out of Australia, it is important that further steps be taken towards an open skies regime which will further enhance competition and flexibility in the air freight industry.

In all cases, dedicated air freight capacity must be negotiated apart from passenger service capacity. Combining these two results plays one off against the other, and more often than not, the users of vital air freight service lose.

Under the existing schedule (including the one existing dedicated air freighter between Perth and Singapore), WA is connected with key cargo markets, especially in Asia. WAC is seeking to increase the number of direct service destinations from Perth, especially to high-value markets in Europe.

Increasing direct air service options out of Perth to new locations can be expected to enhance export opportunities for producers in Western Australia. As many perishable goods require palletised transport, freighter capacity for palletised goods is of significant importance to the Western Australian economy.

Palletised cargo is best transported on 747’s. In a situation where the existing dedicated 747 cargo operator chose to pull out of the route and rapid responses by other operators were constrained by the need to renegotiate existing agreements, there would be a significant restriction in volume and increases in freight costs.

In addition, the current regulatory regime provides no formal mechanism for the producers of perishable goods to provide input into the bilateral negotiation process, despite the fact that on the passenger side, tourism operators are consulted through the TAG.

3.2 Beyond Rights

Access to third country markets is a key to promoting effective competition in air transport.

In addition to offering new market opportunities, the availability of beyond rights also enables international carriers to more efficiently utilise their capital resources through increased flexibility in aircraft scheduling.

WAC believes that an open skies regime which includes beyond rights for international carriers would open up substantial opportunities for expansion of services through Perth Airport and significantly contribute to increased competition in airfares for Australian travellers.

Given the current distance limitations of today’s aircraft fleets, Australia’s geographical isolation from high value markets such as the USA and Europe makes the availability of beyond rights fundamental to further expanding our own carriers’ passenger and freight activity.

While Australia’s international carriers could benefit significantly from the allocation of beyond rights for overseas target markets, the Australian tourism and export industries would benefit concurrently from reciprocal allocation of beyond rights in Australia for international carriers.

Within the current air services agreement regime, effective agreement on beyond rights requires a determined approach on the part of negotiating countries and an understanding of the wider benefits achieved through robust competition.

4. IMPROVING AUSTRALIA'S INTERNATIONAL AIR SERVICES ARRANGEMENTS

4.1 Open Skies

The development of an open skies regime for international air transport will pave the way to increased competition by opening up capacity on inter-country routes and providing access to third country markets.

WAC recognises that the Government's ultimate objective is an open skies model, however, progress in the interim is moving slowly. In addition, the small steps towards progress are benefiting primarily eastern states markets, either through insufficient capacity augmentations to allow foreign carriers to serve the markets they seek, or through negotiating agreements which exclude markets other than those in the eastern states.

WAC strongly recommends that Australia moves towards a full "open skies" policy, in line with international trends.

The movement towards open skies is being led by the United States. The US has signed open skies agreements with countries across the globe, including Germany, Netherlands, Belgium, Denmark, Norway, Brunei, Panama, Nicaragua and Sweden. In the Asia Pacific, the US now has open skies agreements with New Zealand, Singapore, Taiwan and most recently, Japan. The US has also signed liberalised agreements with Fiji, Thailand, China, Hong Kong, India, the Philippines and Macau.[1]

Liberalised air transport arrangements offer potential economic benefits to partners. For example, the liberalisation of air transport between Canada and the United States in 1995 has resulted in significant traffic growth and reductions in passenger fares. In the two years after the new agreement was signed, passenger traffic grew by 28 percent and transborder traffic flown by Canadian carriers grew by 35%. In the top 50 largest nonstop transborder markets, average fares declined 22 percent from 1994 to 1996.[2]

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[1] "USA: Open Skies - A Mid-Year Update", *World Airline News*, Vol. 7 Issue 27, 4 July 1997.
[2] "USA: Carty - Traffic Growth Under U.S. - Canadian Open Skies will Bring Big Vancouver-Asia Gains for Canadian", *World Airline News*, Vol. 7 Issue 20, 16 May 1997.

In January 1997, the US Assistant Secretary of State for Economics and Business Affairs gave the following examples of the benefits of international deregulation:

> *Though the track record is shorter, the benefits of deregulation also are evident in the international arena. Consider what happened between the U.S. and The Netherlands, our first open skies partner in Europe. Before our 1992 Open Skies agreement with the Dutch, there were 75 total weekly frequencies between the U.S. and Amsterdam. That number has now doubled to 150. Since The Netherlands and the U.S. signed up to Open Skies, there has been an astonishing 225% growth in traffic between us.*
>
> *This increase in business has accrued largely to airlines astute enough to take advantage of the opportunities for alliances created under open skies. For example, the number of passengers travelling via the KLM-Northwest alliance, a business arrangement made feasible through Open Skies, rose from 17,000 to 60,000 in only three years.*[3]

The agreements between the United States, Singapore and New Zealand are evidence of a growing liberalisation trend in the Asia Pacific. Singapore and New Zealand have their own open skies agreement and Singapore has also reached an open-skies agreement with Brunei.

While the establishment of the Australia New Zealand Single Aviation Market is a step in the right direction, Australia is still lagging behind the more proactive approaches of New Zealand and Singapore.

The liberalisation of air services is also being addressed by the Asia-Pacific Economic Cooperation forum (APEC). At the Transportation Ministerial Meeting (Victoria, Canada, June 1997), the APEC Air Services Group was reconvened to further develop options for reform of international air services.

Similarly, countries such as New Zealand are advocating a broadening of the General Agreement on Trade in Services (GATS)' application to air services.[4]

The focus on air services agreements by international trade organisations is a signal of the importance of air transport regulation in impacting on regional competitiveness.

Just as other Australian industries move towards global markets and global competition, so too Australia's international carriers must respond to intensified competition on a global scale, including in Australia. This will result in wider benefits in the transport, tourism and export industries.

Increasing reliance on market forces will ultimately offer more transparency and flexibility than the existing complex regulatory regime.

4.2 Improvements under existing bilateral system (if open skies not achievable):

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[3] "U.S.-Japan Economic Cooperation: Ready for Take-Off", Remarks by Alan P. Larson, Assistant Secretary of State for Economics and Business Affairs, at the Japan National Press Club, Tokyo, Japan, January 9, 1997.

[4] Hon Marice Williamson, Minister of Transport, *International Air Transport Policy of New Zealand*, February 1998.

Should there be no immediate move towards an open skies policy, WAC believes that improvement of the existing bilateral system should be given priority.

On a broad level, bilateral agreements should as far as possible enable the market to resolve access issues.

Bilateral agreements must be drafted to give maximum flexibility so that carriers can respond to changes in the competitive environment. Prescriptive agreements should be avoided wherever possible, either with regard to carriers or market served.

WAC welcomes the Government's support for multiple, and more importantly, unspecified destinations and carriers in Air Services Agreements, so long as sufficient capacity is incorporated to serve all markets where carriers of either country have a commercial interest. In order to further free up air services, WAC recommends that restrictive requirements such as mandated services also be abolished.

WAC recommends that the Government review the existing consultation process to ensure that it is transparent and that the priorities of States, airlines, airport operators, exporters and other industry stakeholders are given appropriate, balanced consideration. Prompt and direct feedback on the outcomes of negotiations is also critical to ensure that stakeholder interests are in fact being looked after. The "technical advisory" role provided to the government's negotiating team should be expanded to include representations from other industries capable of commenting on the "value", in a broader sense, of what may be on offer by the other country.

WAC recommends that the new airport operators be offered formal involvement in the bilateral negotiation process at four stages:

i) Pre-strategy

All existing information should be made available for stakeholders to guide DOTRD in determining agendas and priorities for the negotiating process. WAC understands that in certain cases, there may be a broader national objective at stake in the negotiations, and in these cases an acknowledgment of this fact followed by an appropriate level of briefing would suffice.

i) Strategy development

Airport operators should be formally consulted while negotiating positions are being drafted and after they are finalised. The consultation can be facilitated through full membership of TAG and a formal consultation process with DOTRD.

i) Bilateral Negotiations

Airport operators should be fully appraised of the negotiating process and able to participate directly during the formal bilateral negotiation phase.

iv) Feedback

DOTRD should be required to promptly and formally present the results of negotiations, both in writing and through face-to-face discussions, including explanations as to why desired outcomes may not have been achieved.

CONCLUSION

Australia is offered a unique opportunity to be at the forefront of the trend towards full liberalisation of air services agreements. Our geographic isolation means that we can ill afford to let others in the Asian region open up new opportunities for trade and tourism without matching or exceeding them.

The inflexibility of the existing bilateral regime impacts on our tourism, business and export opportunities. It is our firm contention that relaxation of the existing regime can offer both short term and long term benefit to passengers, exporters, businesses, regional areas and our international carriers by promoting healthy competition and a global focus.

FURTHER INFORMATION

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