

PRODUCTIVITY COMMISSION INQUIRY INTO INTERNATIONAL AIR SERVICES

2nd SUBMISSION by the DEPARTMENT OF FOREIGN AFFAIRS AND TRADE

THE NATIONAL INTEREST

"Australia's well-being depends on domestic and international factors, especially the competitiveness and flexibility of the Australian economy, and the strength of international markets and their openness to our exports and investment. Australian interests therefore require action on all these fronts.

Domestic economic policies and business actions will have the greatest impact on Australia's competitiveness and productivity. The Government is committed to creating a more productive economy [including by] creating a more adaptable labour market, cutting the regulatory burden faced by business, and lifting the efficiency of infrastructure, including transport ... delivery." (*Australia's Foreign and Trade Policy White Paper, In the National Interest, August 1997*)

Australia's economic well-being has always been dependent upon international trade. As Australia becomes more integrated into the world economy, the infrastructure supporting our trade, including air transport which is becoming increasingly important must be competitive and efficient to maximise international trade's growing benefits to the Australian economy.

The increasing importance of air services to Australia's exporters and tourism and overseas educational sectors suggests that our national interests are most adequately addressed by ensuring Australians have ready access to fully competitive international air services. There is growing recognition that the longer term interests of consumers, business and the aviation industry itself would be best served by moving positively to liberalise our aviation markets further.

Significant deregulation, liberalisation and privatisation of the airline industry, as well as various forms of global alliance, have developed in the 1990s and are reshaping the competitive forces affecting its structure. Moves toward cooperative alliances in outsourcing of engineering, maintenance, information technology, yield management, catering, handling, etc, are making airlines "globally based".

This submission briefly considers the options examined by the Commission for liberalisation of the international air services framework and the implications for the Single Air Market (SAM) arrangements with New Zealand.

STRATEGIES FOR LIBERALISATION

A policy of unilateral "open skies" for Australia would be inappropriate as adjustment costs for Australian service providers, associated industries and their employees are likely to be

severe and we share the Commission's assessment that such a policy could be far from welfare enhancing.

Australia's approach to seeking bilateral "open skies" agreements should be aimed at securing particular strategic aims benefiting Australian businesses and consumers. This should also ensure that Australia is not disadvantaged by the bilateral partners' own arrangements with third countries. Careful investigation would be required of potential open skies partners' other arrangements and, if necessary, agreements would need to be negotiated with the third countries that would eliminate any risks before finalising agreements with the open skies partner.

More open and liberal bilateral Air Service Agreements (ASA) are a step in the right direction and are an integral part of progression toward bilateral - and even plurilateral - "open skies" arrangements. This is also a faster and perhaps more efficient way of achieving objectives than multilateral or other pluralistic approaches - for the immediate future, at least. Specific ASAs could be targeted in line with the strategic aims of removing market access impediments and/or developing major markets. For example, if Australia achieved the most liberal and beneficial bilateral arrangements possible with EU members, we might then be in a good position to negotiate other "bloc" (or plurilateral) agreements (eg, CER-EU) in the medium term.

WTO OPTION

The timing is opportune to gain support for a stronger multilateral approach to air services liberalisation. In the lead-up to the review of the GATS Annex on Air Transport Services, a good opportunity exists to seek broadening and strengthening of the application of GATS to the air services sector. The GATS Air Annex was initially prepared some five years ago. In the interim, the world - and the aviation industry - have changed. As stated earlier, significant deregulation, liberalisation, privatisation, and global alliances of various forms have changed not only the face of the airline industry, but also the competitive forces affecting its structure. As a result, the next GATS review will occur under a different environment.

DOTARD points out in its response to the draft report that Australia has been a leader in reforming and liberalising air services and related infrastructure, and in establishing mechanisms to enhance competition. Also, Australian airlines have established strategic alliances that give them more market power than might otherwise be expected given the size of the Australian market. Australia might therefore be in a position to participate in the possible formation of a group that could combine forces to influence the agenda for the forthcoming GATS review of the Air Transport Services Annex.

Appropriate Mechanisms

The draft report's recommendation (8.5) that Australia "promote the establishment of a working party of WTO members to determine a process for including international air services in the GATS" may not be practical in terms of "working party" involvement. Working parties have only been established as a result of Ministerial Conferences. The next conference is not until September or October 1999 - which would be too late, as the GATS (including its Air Transport Services Annex) is mandated for review in early 2000. Also, a working party might not be the most effective mechanism.

Alternative mechanisms for progressing the issue could include:

1. through the ongoing Information Exchange programme, which could be used to start discussion on issues, although this is a necessarily limited process.
2. a mandate from the Council for Trade in Services to set up a committee. Several committees exist, but they are mainly to oversee implementation or to manage negotiations and the ongoing implementation process. None manages a preparatory process, although one could ostensibly manage that and go on to manage negotiations, etc. This option would require considerable support from other WTO members.
3. the establishment of another form of grouping of WTO members.

DRAFT RECOMMENDATIONS AFFECTING NEW ZEALAND

The Department agrees with the Commission (draft section 8.5) that the sequencing of any bilateral negotiations must be considered strategically to ensure that Australia's national interest is maximised in our key external markets. Action to further enhance Australia's bilateral aviation arrangements with New Zealand should be considered carefully within this overall strategic approach.

The September 1996 Single Aviation Market Arrangements (SAM) with New Zealand builds upon the 1961 bilateral air services agreement (as amended) and the 31 July 1992 bilateral Memorandum of Understanding on air services arrangements. As the draft report notes in section 3.3.4, the SAM is Australia's most liberal bilateral aviation arrangement. It remains at the leading edge of world aviation, the EU having reached a similar accord for its internal market only in April 1997. The SAM delivers considerable benefits to both CER countries, and further liberalisation of air services arrangements within the Free Trade Area remains an active objective for governments and industry alike.

But the focus of the SAM is specifically on the internal CER market, not on each partner's external aviation linkages. These linkages are governed by a combination of each partner's bilateral agreements with third parties and the bilateral Australia/New Zealand air services agreement. There remain some important steps which could be taken to "complete" the internal CER single aviation market. Chief amongst these would be the incorporation of the SAM into a revised and extended bilateral aviation air services agreement, since the SAM is currently of less-than-treaty status.

However, it is inaccurate to refer to proposals for additional steps which are clearly external to the CER single aviation market (although building on the existing extensive SAM liberalisation) as "completion" of the SAM. For example, the draft report refers to a full Australia/New Zealand exchange of beyond rights (as canvassed in the 1 August 1992 bilateral MoU), and the multiple designation of Australian and New Zealand carriers in international markets. Such initiatives would clearly need to be placed within an overall strategy for liberalising Australia's other international aviation arrangements. The achievement of further flexibilities as between Australian and New Zealand airlines might otherwise be significantly constrained by the unwillingness of third parties to recognise or act upon bilateral agreements between Australia and New Zealand.

It follows that while completion of the SAM in the terms noted above should proceed as an independent priority, further steps to liberalise aviation arrangements external to the common aviation market with New Zealand should proceed as an integral part of a wider liberalisation package of reforms. In particular, steps such as those suggested in draft recommendation 8.6 (and incorporated in draft recommendation 8.7) would only be effective if pursued in the context of a determined strategy to achieve agreement on the part of our other key bilateral partners to more liberal bilateral arrangements with us, perhaps through the judicious and progressive implementation of "open skies" agreements.

Draft recommendations 8.6 and 8.7 could usefully be clarified and revised to reflect these complexities. In particular, the second element of draft recommendation 8.6, the multiple designation of Australasian carriers in international markets, may in fact be a much more complex issue than draft section 8.8.1 would suggest, and may warrant a more detailed analysis than that given in the draft report. In particular, the effect of such a proposal on the negotiation and renegotiation of ASAs with third parties, including its place in any overall agreed strategy to advance Australia's national interest, remains to be seen.

The Department further notes that claims that Australia "has rejected calls from New Zealand for an expansion of beyond rights on the basis that, inter alia, these rights are generally more valuable to New Zealand carriers..." (p.93), do not reflect the position of the Australian Government, nor its commitment to air services liberalisation. The timing of any further exchange of beyond rights is a matter for ongoing consultation between respective Transport Ministers. We understand in any case, however, that neither Australia nor New Zealand fully utilises its available beyond rights at present.