

Air Niugini Limited

Submission by Air Niugini Limited to the Independent Consumer and Competition Commission in support of the Authorization of a Proposed Code-share agreement with Philippine Airlines Inc. on services between Port Moresby and Manila.

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Executive Summary

Application for Authorization

This submission is made by Air Niugini Limited (Air Niugini) in support of an application for authorization of a new codeshare agreement (New Codeshare Agreement) to cover Philippine Airlines (PAL) purchasing seats from Air Niugini Limited on Air Niugini flights between Port Moresby and Manila. This is a new agreement which will coincide with an expansion of the Air Services Agreement between PNG and the Philippines allowing for Air Niugini to increase services to 3 per week.

Air Niugini's has had successful codeshare agreements covering Australian services for some years with Qantas on services to Brisbane and Sydney and separately to Cairns. These have both been subject to ICCC approval and re-approval and a new agreement is proposed to allow Air Niugini to purchase seats from Qantas Link on the Port Moresby Cairns route and this is the subject of a separate application before the ICCC.

Air Niugini is experiencing growth broadly across most markets and our international traffic has grown as a result of increased economic activity in PNG. We have expanded our fleet to meet this increasing demand leasing new and additional aircraft to meet these demands.

Having a new codeshare with Philippine Airlines will enable PNG to gain agreement to extend the Air Services Agreement allowing for an extra weekly flight. It will enhance the available Air Niugini product in this market expanding our brand and market presence.

Pro- competitive structure of the codeshare

A codeshare is an arrangement where one airline (the marketing carrier) buys seats on a flight operated by another airline (the operating carrier) to sell to the marketing carrier's customers. Codesharing is an important form of airline competition. In the modern aviation industry, codesharing has become common, with recognized potential for delivering a lower seat cost to the operator and lower airfare to the traveling public. Many governments entering into Air Service Agreements around the world recognize and endorse codesharing. Further, international developments provide evidence of more than two airlines code-sharing services, in some cases as many as four airlines code-sharing one aircraft service.

There are over two hundred code-sharing agreements between the world's airlines.

Codeshare arrangements typically fall into two broad types:

- (a) 'free sale' or
- (b) 'hard block'

Under a free sale codeshare, the marketing carrier only pays the operating carrier for seats if it actually sells them.

It is proposed that the agreement with Philippine Airlines will be on a "Free Sale" basis. Philippine Airlines has indicated that they would purchase up to 20 economy seats and 4 business class seats on services between Port Moresby and Manila. These seats would be marketed as Philippine Airlines seats and the flight would have an Air Niugini flight number as well as a Philippine Airlines flight number. Under this agreement any unsold seats will be handed back from the Marketing carrier (PAL) to the operating carrier at -48 hours before departure. Any seats not sold at that point by the marketing carrier (PAL) would not be paid for by the marketing carrier (PAL). However once returned these seats could be sold by the operating carrier, Air Niugini.

Under the codeshare arrangements, each carrier, independently from the other:

- (a) sets its own prices;
- (b) determines its own fare classes and rules;
- (c) operates its own independent yield management systems; and
- (d) sells its products through its respective independent sales networks including Websites.

This results in high level of competition between the carriers. In addition, both carriers face effective competition from other combining services from the Philippines to other with connections to PNG.

However, under this new agreement Philippine Airlines will become a new entrant marketing and selling seats between Port Moresby and Manila in competition with Air Niugini.

Results if this code share application was unsuccessful.

Consumers in Papua New Guinea have become used to the Current Codeshare Agreements and high frequency of services to Australia. If the codeshare agreement with Philippine Airlines is not approved, its unlikely the aeronautical authorities of the Philippines will approve extra services under the Air Services Agreement between PNG and the Philippines. Although Air Niugini would continue to market and sell 2 services per week, the route is growing and at peak times is likely to experience capacity constraints. This would lead to upward pressure on prices as the market struggled to secure seats.

If the application was not approved new competition would not be introduced and only one carrier (Air Niugini) would be operating the route.

Summary of benefits of the codeshare

The codeshare between Air Niugini and Philippine Airlines provides a wide range of benefits for both Air Niugini and the nation of Papua New Guinea as a whole. These can be summarized as:

- Competition in the Port Moresby and Philippine Air Passenger Market

The Market for air passenger services between Papua New Guinea and Manila, Philippines is currently only served by one operating carrier, Air Niugini.

The Market between Port Moresby and Manila has grown since 2009. This year Air Niugini alone has experienced in excess of growth in passengers compared to last year. This growth allows for far greater competition between carriers as new and additional passengers are entering the market.

If the application is approved there will be price competition between Air Niugini and Philippine Airlines for the sale of seats on these codeshare flights.

- Employment

Although employment levels would not be dramatically effected if this code share application was not approved, it would in a small way have the effect of limiting Air Niugini's expansion of sales options. This, Air Niugini contends would have the effect of stifling competition rather than enhancing it and could have a negative impact on the growth and development, reducing employment and opportunity for PNG citizens in the aviation industry.

- Improvements to services

If the proposed codeshare agreement with Philippine Airlines is approved it will allow Air Niugini to offer a higher standard of services to Papua New Guinean consumers in a range of ways:

1. Air Niugini will be able to offer greater frequency of services to Manila using high speed modern aircraft.
2. Air Niugini will be able to better meet the demand for increased services by our customers.

3. Air Niugini customers will have more choices, being able to purchase Air Niugini seats on flights operated on 3 days of the week rather than 2 as is currently the case.
4. Competition will be increased with Air Niugini marketing seats on more services and competing for sales with Philippine Airlines.

- National flag air carrier

Having a flag air carrier with the strength and service capability of Air Niugini provides important benefits to the people of Papua New Guinea. For example, having a strong national air carrier is important from a security and safety perspective. In times of national crisis or emergency, a national carrier is a valuable resource. For example after the Bali bombing on 12 October 2002, many injured Australians required evacuation to Darwin, and then to burns units around Australia. In response, Qantas was able to transport approximately 1,700 people from Bali to Sydney on six special flights from Bali to Australia, as well as transport medical staff and supplies to Bali. Similarly, in the wake of the earthquake and series of tsunamis that devastated South East Asia in 2004, Qantas operated special flights to Phuket, the Maldives and Colombo in Sri Lanka to bring travelers home to Australia. When the Ansett Australia Group collapsed in 2001, Qantas leased extra aircraft and withdrew aircraft from a number of services (including its Papua New Guinea service) in order to add hundreds of special domestic flights to assist stranded Ansett passengers.

The maintenance of Air Niugini as a strong national airline means that similar resources are available to the people of Papua New Guinea should they ever be required.

Conclusions

Air Niugini believes that its proposed codeshare arrangements with Philippine Airlines on Port Moresby Manila services will lead to very substantial public benefits, whilst not resulting in a lessening of competition.

Air Niugini therefore requests that the Independent Competition and Consumer Commission authorize these arrangements pursuant to section 70 (1) of the *Independent Consumer and Competition Commission Act 2002*

Part A – Introduction

1. APPLICATION FOR AUTHORISATION

This submission is made by Air Niugini Limited (**Air Niugini**) in support of an application for authorization pursuant to section 70 (1) of the *Independent Consumer and Competition Commission Act 2002 (ICCC Act)* to enter into and give effect to a new code share agreement (**New Codeshare Agreement**) with Philippine Airlines (PAL).

The New Code share Agreement is a new agreement enabling an expansion of services to Manila. This agreement is referred to in this submission as the **codeshare arrangements**.

This submission and its annexures include certain commercially confidential information. Disclosure of this information could result in material financial loss and prejudice the competitive position of Air Niugini. Air Niugini requests that this information be kept in strict confidence by the Commission and excluded from the register kept by the Commission in accordance with section 131 of the *ICCC Act*. For convenience, the confidential information is indicated by the use of bold **red font** for confidential text for a heading of a confidential table, figure or Annexure in the confidential versions of the submission. This information has been deleted and replaced with **(CONFIDENTIAL INFORMATION DELETED)** in the non-confidential version of the submission provided to the Commission.

Air Niugini requests that the ICCC raise any issues or questions it may have in relation to the proposed codeshare arrangement or this submission with Air Niugini through its Mr Colin Lyttle, General Manager Marketing for Air Niugini.

2. DESCRIPTION OF THE PARTIES

2.1 **Air Niugini**

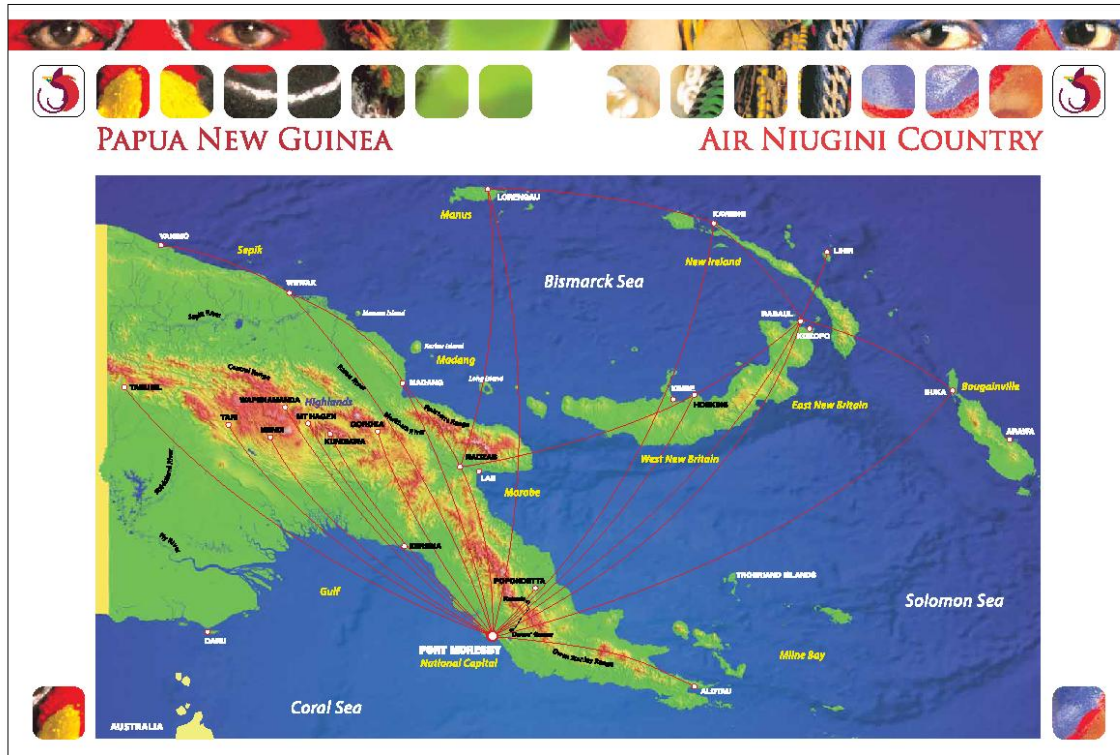
Air Niugini was incorporated and began operating in 1973 as the national airline of Papua New Guinea. The company was originally owned by the Papua New Guinean government (60%) Ansett (16%) Qantas (12%) and Trans Australia Airlines (TAA) (12%). In 1976 the Papua New Guinea government bought out the Qantas and TAA holdings and in 1980 acquired the Ansett shares to make the airline wholly government owned. Air Niugini is still 100% owned by the Papua New Guinea government.

Air Niugini is one of Papua New Guinea's largest and most respected companies. Air Niugini employs approximately 1725 people worldwide and is Papua New Guinea's largest airline. In the last two years the airline has grown thanks to the approval of the precious code-share agreement and has added a further wide body long range aircraft B767 to the fleet to provide more reliability and travel choices to the travelling public.

Air Niugini's gross turnover in financial year 2009 was .

Air Niugini's main business is the transportation of passengers and air freight domestically and internationally. In addition to the core business of transporting passengers and air freight, Air Niugini maintains 22 retail sales offices throughout Papua New Guinea, provides in-flight catering for its own operations, operates a tours division packaging holidays for its customers and travel agent's customers around Papua New Guinea, and maintains offices in Brisbane, Cairns, Sydney, Manila and Tokyo. These overseas offices not only sell tickets to the traveling public, but they also service the needs of the Papua New Guineans who travel overseas and (in many ways) act as de facto Papua New Guinean tourism offices. Additionally, Air Niugini has appointed General Sales Agents who represent its and Papua New Guinea's interests in Singapore, UK, Scandinavia, Germany, Italy, Malaysia, Indonesia, Hong Kong, China, Taiwan, the USA, Fiji, Solomon Islands, New Zealand and South Korea. Air Niugini provides its own ground handling throughout PNG employing over 1700 staff. Further, it also maintains an engineering facility covering up to "C" check level service for Fokker 100 and Dash 8 Aircraft types and provides line check services to B767 and B757 aircraft types.

Air Niugini Operates Domestic services between Port Moresby and 21 Ports throughout Papua New Guinea as shown in Figure 1 below:



In addition to domestic air services as displayed here, Air Niugini operates international services between Port Moresby and 10 ports around the world as follows:

- Sydney, Brisbane and Cairns International Airports, Australia;
- Narita International Airport, Tokyo, Japan;
- Changi International Airport, Singapore;
- Kuala Lumpur International Airport (KLAS) in Kuala Lumpur, Malaysia;
- Hong Kong International Airport, Hong Kong;
- Honiara Henderson International Airport, Solomon Islands;
- Nadi International Airport, Fiji; and
- Ninoy Aquino International Airport, Manila, Philippines.

Air Niugini's domestic and international fleet consists of nineteen aircraft, 2 x B767 aircraft, 1 x B757, 6 x Fokker F-100 jets, 2 x Dash 8 Q400 aircraft modern turbo prop aircraft and 8 Dash 8 turboprop aircraft.

2.2 Philippine Airlines (PAL)

A PROUD HERITAGE, A PROMISING FUTURE

Philippine Airlines (PAL) began life with a noble mission: to serve as a partner in nation-building. With this in mind, PAL took to the skies on 15 March 1941, using a Beech Model 18 aircraft amid the specter of a global war. It became Asia's first airline.

PAL through the years

Since then, PAL deeply involved itself in shaping the course of historic events. With its every takeoff and touchdown, PAL planted the seed of growth.

PAL has become one of the most respected airlines around the world with a young and modern fleet of aircraft and a route network that spans 33 foreign cities and 29 domestic points.

Service excellence

PAL's excellent service has won the hearts of travelers worldwide. This trademark has distinguished it from the pack and has stood guard in an environment that has grown more competitive by the day.

But PAL does not sit on its laurels. Realizing that it owes its success to its loyal passengers, PAL launched a campaign called "Call for excellence" to serve its market better.

Embracing e-business

PAL began embracing electronic commerce with the introduction of its Online Booking service that accepts ticket purchases and credit card payments for all flights. A new, improved website was also launched to serve the customers' needs more quickly and efficiently.

In 1992, the Philippine Airlines Foundation (PALF) was founded as the community relations arm of Asia's First Airline and an accredited disaster relief, crisis intervention and welfare organization.

PAL Medical Travel Grants are PALF's main program for humanitarian and social development assistance. These enable indigent Filipinos to go for medical treatment as charity or service patients for serious health conditions.

The PAL Foundation has a preferential option for the poorest and the weakest members of society - the children, the differently abled and the elderly.

3. RATIONALE FOR THE NEW CODESHARE AGREEMENT

Air Niugini assesses demand for services across its routes and on potential new routes regularly. In making such assessments, Air Niugini considers how best to meet market demands and offer the greatest choices to our customers.

Code-share agreements are an established way for two or more airlines to be able to share the cost of operations whilst continuing to compete for sales on a given route.

Air Niugini believes that with the approval of the code-share arrangement on the Port Moresby / Manila services will allow Air Niugini to grow operating 3 weekly services rather than 2 and compete more effectively with the largest number of seats and departure frequencies in this market.

Philippine Passenger Market.

Papua New Guinea enjoys a close relationship with the Philippines.

The Filipino community in PNG is growing and increasingly become part of the fabric of life in PNG. The Filipinos are involved in PNG are involved in businesses, charity work, sports and drama. Their children attend PNG schools and they travel to and from their homeland. With employment opportunities expanding in PNG, more Filipino workers are finding work in PNG.

This is reflected in the increasing growth on the air route to Manila.

According to 2007 embassy figures, there were around 10,000 Filipinos living in PNG, and 2,850 undocumented workers. As these Filipinos become more integrated into PNG society they are increasingly engaged in business and family life. They travel frequently and their friends and relatives travel to visit them.

Passenger traffic between PNG and Manila is increasing on an annual basis and this year has grown significantly.

4. SUMMARY OF OTHER EXISTING CODESHARE AGREEMENTS

Other Codeshare Agreements covering services to Australia have existed for many years. The current agreement covering services to Brisbane and Sydney between Air Niugini and Qantas Airways commenced on 1 September 2002 for a term of five years, expiring on 31 August 2007. Essentially this agreement was granted conditional authorization by the ICCA for the continuation of the codeshare arrangement for a further two (2) years and was due to expire on 31 December 2009. This was further extended in 2009 for another two years until 30 June 2012.

Key terms of this existing Current Codeshare Agreement are as follows:

- (a) Air Niugini operates services between Papua New Guinea and Australia on the following routes:
 - i. Port Moresby – Brisbane vv (**Brisbane Route**)
 - ii. Port Moresby – Sydney vv (**Sydney Route**)
 - iii. Port Moresby - Sydney - Melbourne (potential new route)

Changes in routes may be negotiated between the parties from time to time in response to customer demand and capacity available.

These services above are referred to collectively in this submission as the **current code-share services**.

- (b) Qantas is allocated blocks of seats for sale to Qantas passengers on each codeshare service. Most of these seats are allocated on the basis that they must be paid for by Qantas whether Qantas sells them to a passenger or not (the **Hard Block** allocation). The hard block allocation that Qantas is required to purchase under the codeshare arrangements is significantly higher than the number on average that it sells. Unsold hard block seats represent an absolute loss to Qantas. Qantas therefore has a strong incentive to market these seats aggressively in competition with Air Niugini.
- (c) If Qantas sells all its hard block allocation on any particular flight, it has an option to purchase a certain number of additional seats. This is referred to as the **Soft Block** allocation.
- (d) Air Niugini and Qantas each sells and markets fares on each codeshare service independently through its respective sales networks in full competition with the other. Each carrier has complete freedom in relation to the fare classes it offers, the rules it sets for each class and the price it charges for fares.

Part B - THE FUTURE WITH AND WITHOUT THE NEW CODESHARE AGREEMENT.

5. OVERVIEW

When assessing the effect on competition and the public benefits associated with the new Code-share Agreement, it is necessary to consider and compare the likely outcomes if authorization is granted and the new Code-share Agreement proceeds with the likely outcomes if authorization is not granted and the new Code-share Agreement does not proceed.

6. IF AUTHORISATION IS GRANTED

- a) Both Philippine Airlines and Air Niugini will be able to offer consumers high quality, higher frequency passenger services between Manila and Papua New Guinea in accordance with the schedule outlined in Attachment C; and
- b) Philippine Airlines and Air Niugini will compete in relation to both the prices and terms they offer passenger services between Manila and Papua New Guinea; and
- c) Air Niugini will be able to offer an increased number of seats and frequency of services between Port Moresby and Manila.
- d) Philippine Airlines have had no presence in the PNG market for more than two decades will reenter the market as a marketing carrier offering codeshare seats to their customers.
- e) Passengers in PNG and the Philippines will have a choice of booking seats with Air Niugini or Philippine Airlines.

7. IF AUTHORISATION IS NOT GRANTED - AIR PASSENGER SERVICES.

Air Niugini will continue to operate services in our own right between Port Moresby and Manila, however Air Niugini anticipates the Philippine aeronautical authorities will not agree to increase the capacity under the Air Services Agreement and therefore Air Niugini will be limited to 2 x weekly services.

Market expansion will be restricted as flights during busy periods will be constrained and customers will have to look for less convenient routes. This will have a negative impact on prices putting upward pressure on prices as customers compete for seats.

Its unlikely Philippine Airlines would enter the market in its own right, given that they have not been in this market for many years and the risk of committing an aircraft to the route would be cost prohibitive.

Air Niugini response – Short Term.

Air Niugini would continue to lobby for an increase in services but would expect to encounter resistance from the Philippine aeronautical authorities.

As seats become more difficult to secure, prices will rise and possibly attract the interest of more predatory airlines. Air Niugini strongly advocates a measured and managed approach to expansion of routes to enable the industry to evolve to new levels ensuring operations are sustainable.

Part C- COMPETITION IN AIR PASSENGER MARKET - WITH CODESHARE

8. Overview

The proposed new Code-share agreement provides Air Niugini with:

- (a) the opportunity to expand our presence in the market through the increased services and the introduction to the market of a new airline to this market.
- (b) Philippine Airlines will be marketing and selling seats in both the Philippines and PNG giving customers a choice of airlines and fares.

A range of factors show that the arrangements provide effective competition for the benefit of consumers in both Papua New Guinea and the Philippines. These are described in more detail below.

9. Pro-competitive codeshare structure

A codeshare is an arrangement where one airline (the **marketing carrier**) buys seats on a flight operated by another airline (the **operating carrier**) to sell to the marketing carrier's customers. Codesharing is an important airline activity and is widespread in the industry. It allows airlines to maintain a presence in a market where their own operation would not be sustainable. In the modern aviation industry, codesharing is common and recognizes the potential for delivering a lower seat cost to the operator and lower airfares to the consumer. Many governments entering into Air Service Agreements around the world recognize and endorse codesharing.

There are currently hundreds of codesharing agreements among the world's airlines. A survey of the myriad of codesharing and alliance arrangements implemented around the world is set out in Airline Business 'Airline Alliance Survey 2006', a copy of which was attached as an Annexure to an earlier submission on the Australian services to the ICCA in 2007.

Codeshare arrangements typically fall into two broad types:

- (a) 'free sale'. or
- (b) 'hard block';

Under a free sale codeshare, the marketing carrier only pays the operating carrier for seats if it actually sells them. This is a less competitive arrangement as the marketing carrier has less incentive to sell and be competitive.

10. SUMMARY OF PROPOSED CODESHARE AIR NIUGINI / PHILIPPINE AIRLINES BETWEEN PORT MORESBY AND MANILA

Despite "free sale" codeshare agreements being less competitive than "hard block" agreements, under the new proposed Air Niugini/Philippine Airlines Codeshare arrangements, Philippine Airlines will take seats to sell to the market that it currently doesn't have. This will effectively mean there is a new marketing carrier in the market and is an easier way for an airline to enter a new market without having to endure the much higher risks of committing a regular passenger aircraft to the route immediately.

Under these proposed new codeshare arrangements, Air Niugini and Philippine Airlines each sells and markets fares on codeshare services independently, in full competition with the other.

Each carrier, independently from the other:

- (a) sets its own price;
- (b) determines its own fare classes and rules;
- (c) operates its own independent yield management systems: and
- (d) sells its products through its respective independent sales networks.

(a) No Constraining of Capacity

As with many markets, competition in airline markets is driven substantially by capacity. The higher level of capacity relative to demand, the higher the pressure on prices. Competition regulators have therefore raised concerns where codeshare arrangements have the effect of constraining capacity on a route. ⁽¹⁾

⁽¹⁾ No official market share data is available in Papua New Guinea. Market share is therefore calculated on the basis of Air Niugini estimates of passengers carried by Airlines of PNG and Qantas.

Figure 7:

Philippines Passenger Growth

	2008	2009	2010
POM MNL			

(b) Anti-competitive body comments

When approving the proposed Trans-Tasman alliance between Qantas and Air New Zealand, the Australian Competition Tribunal summarized the ability of a small but vigorous competitor to constrain the conduct of a much larger competitor as follows:

“Although market share can be a significant factor in determining the extent of competition in a market, we believe that prime attention must be paid to market conduct. A structuralist approach that focuses heavily on an increase of market power by using market shares as a proxy to assess market power fails to assess the whole picture...”

and

“Market shares, by themselves, in the absence of barriers to entry or expansion, do not guarantee that the firms holding such market positions will be able to act to the detriment of the competitive process. A high market share indicates only that at a point of time the firm in question has been able to command the patronage of many customers in the market. Such patronage may be due to the fact that the firm has been able to offer the right “price-product-service package” to customers...”

and

“...When entry barriers are low or non-existent, in the sense that there exist no impediment to competitively significant entry – entry that will serve to constrain the firm in question – then if the firm currently enjoys a high share of the market, this will not of itself signal that the firm can be expected in the future to behave in an anti-competitive manner.”

Although Air Niugini has responded to competition in various markets, it is important to note that, in doing so, it has been careful not to engage in conduct that may be considered predatory. When the new CEO was appointed to Air Niugini in May 2006 the Board of Air Niugini required as part of the KPI, CEO to make the airfares more competitive and introduce new fares in both domestic and international sectors and allow passenger growth. Air Niugini has introduced new discounted fares over the last several years and continues to

compete with the discounts offered by other airlines. These discounted fares, however, respond to prices offered by other airlines rather than attempting to force prices down further. Air Niugini has tended to offer fares above some airlines as Air Niugini offers a full service in-flight product. Air Niugini has not engaged in conduct aimed at forcing other airlines to withdraw from the market or behave in a less competitive way.

Ability of customers to charter their own flights

Air Niugini is also constrained by the ability of major customers to impose price pressure by threatening to or actually chartering or operating their own services to Papua New Guinea.

For example Lihir Gold Ltd recently sought airline proposals for Cairns / Lihir / Cairns charters to operate 6 flights per week to cater for between 55-70 passengers per week in each direction. Airlines of PNG were awarded the contract on the basis of using a Dash 8 - 100 aircraft which they have reconfigured especially to 12 Business class seats only.

(c) Low barriers to entry and potential competitors ready to enter.

In addition to being constrained by existing competition, Air Niugini is at all times constrained in their conduct by the fact that barriers to entry to the PNG Air Passenger Services Market are low. If Air Niugini were to raise prices or reduce service levels, it would be easy for a new entrant to take advantage of this to enter the market.

A summary of the reasons why barriers for entry to the PNG Passenger Air Services Market are low is set out below:

- Limited regulatory barriers. Although there is limited capacity available under the Air Services Agreement (ASA) from the PNG side no Philippines airlines have taken up the option of operating to PNG. Relevant safety certificates for operation in the Philippines and Papua New Guinea are available to any carrier that satisfies fair and objective safety standards.
- Slot constraints. There are no slot constraints at Port Moresby and these would not be expected to be a problem in the Philippines.
- Ground facilities are available. Ground handling facilities and common user terminals are readily available at both Manila and Port Moresby.

- Aircraft are available. There is an active international market for appropriate aircraft. This means that a new entrant could acquire appropriate aircraft at competitive prices. Sunk costs are minimal, as aircraft can be readily resold. Alternatively, if a new entrant wanted to minimize start up capital requirements, active markets exist to enable them to lease appropriate aircraft with minimal capital outlay.

This ability for new carriers to enter the PNG Passenger Air Services Market is illustrated by the recent entry to the market of Virgin Airlines and the rapid expansion of Airlines PNG.

In addition:

- The Commission noted in September 2006 in its report entitled *Papua New Guinea Tourism Sector Review and Masterplan 2007 - 2017* that there were then suggestions of a further new entrant on the Port Moresby and Cairns route. This presumes that there would be little impediment to a new entrant into the PNG markets;
- A range of other companies, such as Tiger Airways Australia (which has financial backing from the Singapore government and has been investigating potential routes in the north of Australia), may also be well positioned to enter the PNG market if Air Niugini were to raise prices to make more than normal levels of profit.

11. COMPETITION IN AIR PASSENGER MARKET - NO AIR NIUGINI / PHILIPPINE AIRLINES CODESHARE ON PORT MORESBY MANILA SERVICES.

If the new Codeshare Agreement between Air Niugini and Philippine Airlines for services between Port Moresby and Manila is not authorized, Air Niugini expects to continue its own services in the Manila / Port Moresby Air Passenger Market. Capacity limitations will result as demand for seats will exceed supply in peak periods. Additional demand will be met by airlines operating from Manila to other countries to meet passenger demand to seats to Port Moresby.

The collective outcome will be upward pressure on prices as customers compete for scarce seats. It would be unlikely that Philippine Airlines would be prepared to take the risk of committing aircraft and personnel to the route at this time, given the global fragility of the aviation industry.

If Philippine airlines did enter the market in their own right, Air Niugini could move from having a profitable route to sustaining losses on services between Port Moresby and Manila. As a national airline, those losses represent a direct loss to the people of Papua New Guinea.

It is also possible that the no authorization of the new Code-share Agreement could result in the carriers chasing sales seeking to cover extra operating costs and may lead to a less efficient and, ultimately, less competitive market structure than authorization of the new Code-share Agreement.

Part D - PUBLIC BENEFITS.

12. OVERVIEW

The Air Niugini / Philippine Airlines code-share arrangements provide a wide range of public benefits. These include the following:

- (a) Benefits to the Papua New Guinean economy through increasing Air Niugini's foreign earnings;
- (b) Benefits to the Papua New Guinea economy through enabling Air Niugini to earn profits on code-share routes (rather than the losses that could occur from the introduction of a different scenario without the code-share) which can be returned to the people of Papua New Guinea through the payment of dividends to the government;
- (c) More efficient use of resources through sharing the operating aircraft on code-share flights and therefore lowering per passenger costs and lowering greenhouse emissions than a more duplicated model of services that could result without the code share;
- (d) Provision of more frequent services;
- (e) The introduction of a new airline marketing their products and setting fares in the PNG market. Philippine Airlines offer easy connections to the USA, China and Japan amongst other Asian and Middle East destinations. Effectively opening new markets for easy sales and purchase in PNG.
- (f) Maintaining a substantial number of airline jobs in Papua New Guinea;
- (g) Greater customer choice of available services, where customers can choose to purchase Air Niugini fares or Philippine Airline fares competing in the market for passengers between Port Moresby and Manila.
- (h) A stronger, more capable flag carrier for the nation.