

Air Niugini Limited

Submission by Air Niugini Limited to the Independent Consumer and Competition Commission in support of Authorization of the Proposed Code-share agreement with Qantas Airways Limited on services between Port Moresby and Cairns.

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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 Air Niugini purchasing seats from Qantas Airways Limited (Qantas) on Qantas Link flights between Port Moresby and Cairns. This agreement will be different to the previous code-share agreement where Qantas purchased seats on Air Niugini services over this route which ceased effective 01 July 2010.

Air Niugini's codeshare agreement with Qantas on services to Brisbane and Sydney has been in place for more than 7 years and has delivered higher quality, higher frequency wide and narrow body jet services between Papua New Guinea and Australia. This agreement continues today and governs the terms under which Qantas Airways purchases seats from Air Niugini and largely marketing these in the PNG and Australian aviation markets.

Another codeshare agreement existed between Qantas Airways and Air Niugini for flights between Port Moresby and Cairns. This agreement existed from the late 1980s until July 2010 and was the subject of approval from the ICC. This agreement ceased following advice from Qantas (see attached letter from Qantas informing Air Niugini of the cessation of this Codeshare agreement) that they intended to commence services between Cairns, Australia and Port Moresby from 1 July 2010 using Qantas Link aircraft. Since that time Air Niugini and Qantas Link have offered services independently between Port Moresby and Cairns without a code share arrangement.

Air Niugini has reached agreement with Qantas to purchase seats on some of the Qantas link flights to and from Cairns which will be offered for sale to the market as Air Niugini seats. The purchase of these seats will be on a "hard block" basis without the capacity to return unsold seats to the operating carrier except where this is requested by the operating carrier to handle over sales or manage disrupted passengers.

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 Qantas Link will provide supplementary seats for Air Niugini to market providing a far greater choice of departure times for customers. 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.

Qantas operates in a more mature and developed market than Air Niugini and yet still relies significantly on codeshare capacity. Air Niugini understands that Qantas currently participates in over 20 codesharing agreements on various routes on its network, and 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.

By contrast the code-share arrangement in this application between Air Niugini and Qantas, under BLOCK CODESHARE seats are allocated to Air Niugini on a hard block basis. This means the marketing carrier (PX) must pay the operating carrier (Qantas) whether Air Niugini sells the seats or not. Unsold hard block seats represent an absolute loss to Air Niugini. Therefore Air Niugini has a strong incentive to market these seats aggressively in competition with Qantas.

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 Airlines PNG who operate their own services between Port Moresby and Cairns. Airlines PNG are required to set fare levels independently and therefore to/from Cairns there are 3 airlines setting marketing fares. Papua New Guinea's "open skies" policy ensures that new entrants can enter the market with no barriers.

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 jet services to Australia. Air Niugini will continue to offer its own services between Port Moresby and Cairns; however the number of frequencies offered by Air Niugini would be less than we are able to offer if the codeshare application is approved.

If the application was not approved the competition would remain with each airline offering services and fares on their own services only.

Summary of benefits of the codeshare

The codeshare between Air Niugini and Qantas 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 Cairns and far North Queensland Air Passenger Market

The Market for air passenger services between Papua New Guinea and Cairns, Australia (**The Cairns and Far North Queensland Air Passenger Market**) is currently served by three operating carriers, Air Niugini, Qantas Link and Airlines PNG.

The Market between Cairns and Port Moresby 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 Qantas link not only between different flights but also on seats on the same aircraft.

- 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 Qantas 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 higher frequency of services to Cairns using high speed modern aircraft.
2. Air Niugini will be able to better meet the demand for increased services by our customers without adding further demands on the Air Niugini fleet.
3. Air Niugini customers will have more choices, being able to purchase Air Niugini seats not only on our own aircraft but also on services operated by Qantas Link flights.
4. Competition will be increased with Air Niugini marketing seats on more services and competing for sales with Qantas Link on their flights.

- 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 Qantas on Cairns services 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 Qantas Airways Limited (**Qantas**).

The New Code share Agreement replaces a previous codeshare agreement which ceased on 01 July 2010 (the **Previous Codeshare Agreement**). Together, the New Codeshare Agreement and the Previous Codeshare Agreement are 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**

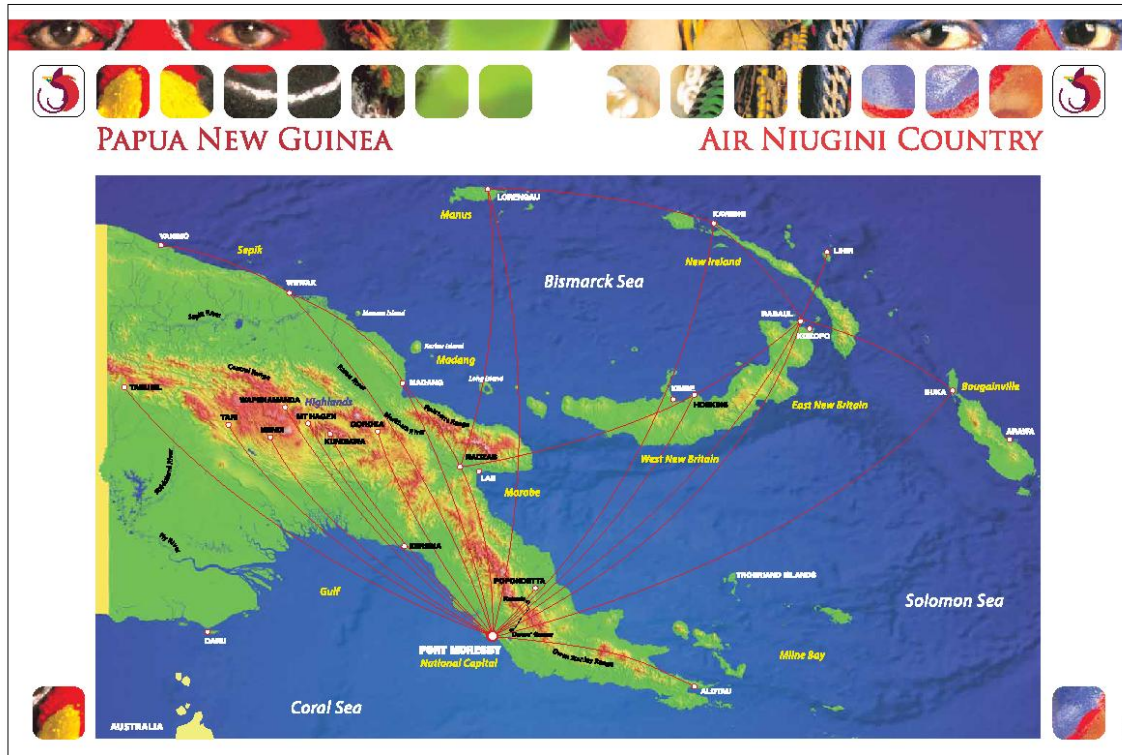
Air Niugini was incorporated and began operating in 1973 as the national airline of Papua New Guinea. The company was originally owned by the Papua New Guinean government (60%) Ansett (16%) Qantas (12%) and Trans Australia Airlines (TAA) (12%). In 1976 the Papua New Guinea government bought out the Qantas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

Qantas is the world's second oldest airline and the eleventh largest globally in terms of Revenue Passenger Kilometers. In the year ended 30 June 2010, Qantas carried approximately 41.4 million passengers, providing services to 144 destinations in 44 countries (including codeshare flights operated by other airlines) and regular passenger services to 59 destinations throughout Australia.

Qantas operates a domestic and international fleet of 252 aircraft, comprising Airbus A380s, A330s and A320s and Boeing 747s, 767s, 737s and 717s, Bombardier Dash 8s, Bombardier Q400s and British Aerospace 146s.

The Qantas Group's airline businesses include Qantas (full service domestic and international services), JetConnect (domestic New Zealand and Trans-Tasman services), QantasLink (regional Australian services) and Jetstar (Low cost domestic and international services). In addition to its airline operations, the Qantas Group operates a portfolio of airline related businesses including airport operations, freight, engineering, catering and travel and accommodation booking business. Qantas employs approximately 32,500 people worldwide.

Within Papua New Guinea, Qantas employs 19 local staff, 2 based at Jackson's Airport in Port Moresby responsible for customer service and freight operations. 17 staff based in the town office which consists of a retail travel centre, telephone sales call centre, administration and finance.

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 Qantas Link flights between Port Moresby and Cairns allows Air Niugini to compete more effectively with the largest number of seats and departure frequencies in this market.

Australia Passenger Market.

Papua New Guinea has traditionally enjoyed a close relationship with Australia. In past decades there have been strong levels of investment in Papua New Guinea by Australian businesses, particularly in the mining sector. As a result, there has been a large proportion of expatriate Australians living in Papua New Guinea and traveling to and from Australia.

In more recent years, however both the level of Australian business activity in Papua New Guinea and the number of Australian expatriates living in Papua New Guinea has reduced substantially. For example, at the beginning of the 1990's, Air Niugini believes that there were in the order of 20,000 to 25,000 expatriate Australians living in Papua New Guinea. There are now in the order of only 7,000 to 10,000. ⁽¹⁾ However, with the LNG project this number is increasing. Since Qantas Link commenced services between Cairns and Port Moresby in July 2010, Airlines of PNG has reduced services to and from Cairns; however Air Niugini after some slight rationalization has added new services to the route. Air Niugini is experiencing growth on services to Cairns and wishes to expand the available seats and frequencies we are able to offer our customers. Entering a Code-share arrangement to purchase seats on the Qantas Link flights enables Air Niugini to expand our presence in this market without putting further demands on the Air Niugini aircraft fleet.

(1)

The Australian High Commission in Port Moresby, who maintains a database of Australians registered as living in PNG, has advised that, based on current numbers registered, they estimate there are between 6,000 and 8,000 Australian expatriates currently living in PNG. Though the Australian High Commission records do not extend back to the late 1980's / early 1990's, they have confirmed that they believe an estimate of up to 25,000 Australian expatriates living in PNG at this time seems reasonable. The Australian High Commission has also advised Air Niugini that in 1995, the Consular Office issued approximately 18,000 visitor visas in PNG for entry into Australia. By 2004, this had declined to 10,500 though it recovered slightly to 13,000 in 2006.

4. SUMMARY OF THE EXISTING CODESHARE AGREEMENT

The original Codeshare Agreement 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 ICCC for the continuation of the codeshare arrangement for 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 the 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 Qantas and Air Niugini will continue to be able to offer consumers high quality, high frequency passenger services between Cairns and Papua New Guinea in accordance with the schedule outlined in Attachment C; and
- b) Qantas and Air Niugini will continue to compete in relation to both the prices and terms they offer passenger services between Cairns 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 Cairns.

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

Qantas and Air Niugini will continue to operate services in our own right between Cairns and Port Moresby, Air Niugini anticipates that these services would continue to be provided by Qantas Link Dash8 Q400 aircraft and a mixture of F100 and Dash 8 Q400 aircraft by Air Niugini.

Market expansion would most likely be met by each airline adding extra flights or increasing the aircraft size on the route. This would be more costly and expensive model adding increases to our operating costs and putting upward pressure on fares.

Air Niugini response - Short Term.

Under the previous Code-share Agreement, Air Niugini was able for the first time to provide a high frequency services to Cairns. If the new Code-share Agreement is not authorized, the frequency of this service offered by Air Niugini will be less than if the new Code-share Agreement is approved. This would result in Air Niugini offering fewer services and frequencies to customers making the Air Niugini presence in the market less viable and less competitive.

Part C- COMPETITION IN AIR PASSENGER MARKET - WITH CODESHARE

8. Overview

The previous structure in the Port Moresby/Cairns Air Passenger Market with Qantas purchasing seats On Air Niugini services was both effective and efficient. The proposed new Code-share agreement provides Air Niugini with:

- (a) the opportunity to expand our presence in the market through the purchase of seats on the Qantas Link services and the ability to sell these seats at competitive rates without adding to our operating costs.

A range of factors show that the arrangements provide effective competition for the benefit of consumers in both Papua New Guinea and Australia. 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 airfare to the consumer. Many governments entering into Air Service Agreements around the world recognize and endorse codesharing.

Qantas operates in a more mature and developed market than Air Niugini and yet still relies significantly on codesharing. Air Niugini understands that Qantas currently participates in at least 20 codesharing agreements over various routes on its network, and 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 to the ICCC 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 / QANTAS LINK BETWEEN PORT MORESBY AND CAIRNS

By contrast, under the new proposed Air Niugini/Qantas Code-share arrangements, Air Niugini is allocated blocks of seats for sale on some Qantas Link services. These seats are allocated on a 'hard block' basis. This means they must be paid for by Air Niugini whether Air Niugini sells them or not. This is recognized by competition regulators around the world as the most competitive form of codesharing arrangement.

Under the new code-share arrangements, Air Niugini and Qantas 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.

Once Air Niugini has entered into the New Code-share Agreement and committed to purchase its hard block allocations, each seat on each codeshare service sold by Air Niugini effectively has a marginal cost of zero kina. Unsold hard block seats therefore represent an absolute loss to Air Niugini.

Air Niugini therefore has the strongest possible incentive to market its seats on codeshare services aggressively in competition with Qantas.

(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. ⁽²⁾

With Qantas Link commencing services from 1 July 2010 on the route with 12 services in each direction per week on a 74 Seater Dash Q400 aircraft, capacity has clearly exceeded immediate demand.

(2) 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:

Market Growth	2008	2009	2010
POM CNS			

2010 estimate based on 9 months of data

(b) Airlines of PNG

Airlines of PNG commenced international operations between Cairns and Port Moresby in November 2005, operating 5 weekly services with a de Havilland Dash 8-100 aircraft. This was quickly increased to 6 services per week and, from November 2006, to 7 services per week.

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 from Airlines PNG and Qantas, 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 prior to APNG and Qantas Link entry to the market and continues to compete with the discounts offered by Airlines of PNG and Qantas Link. These discounted fares, however, respond to prices offered by Airlines PNG and Qantas rather than attempting to force prices down further. Air Niugini has tended to offer fares above Airlines of PNG because Air Niugini offers a full service in-flight product. Air Niugini has not engaged in conduct aimed at forcing Airlines of PNG to withdraw from the market or behave in a less competitive way.

Ability of customers to charter their own flights

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

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 and Qantas are at all times constrained in their conduct by the fact that barriers to entry to the Australian Air Passenger Services Market are low. If Air Niugini or Qantas 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 Australian Passenger Air Services Market are low is set out below:

- No regulatory barriers. There is more than adequate capacity available under the air services agreement between Papua New Guinea and Australia to allow either a new Australian or Papua New Guinean carrier to enter any or all of the codeshare routes, and both countries allow multiple carrier designation. Relevant safety certificates for operation in Australia and Papua New Guinea are available to any carrier that satisfies fair and objective safety standards.

- No slot constraints. There are no slot constraints at Port Moresby or Cairns airports that would be likely to hinder the entry of new carrier on this route.
- Ground facilities are available. Ground handling facilities and common user terminals are readily available at both Cairns 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 Australian Passenger Air Services Market is illustrated by the recent entry to the market of Virgin Airlines and the rapid expansion of Airlines PNG, which has been described in more detail above.

In addition:

- Virgin Blue has entered the Port Moresby Brisbane market commencing in November 2008 with a codeshare operation with Airlines PNG. Although Virgin and Airlines PNG have pitched their services on peak business travel days between Brisbane and Port Moresby, they have also pitched fares at the cheaper end of the market;
- 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; ⁽⁸⁾
- 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 market if Air Niugini and Qantas were to raise prices to make more than normal levels of profit.

11. COMPETITION IN AIR PASSENGER MARKET - NO AIR NIUGINI / QANTAS CODESHARE ON PORT MORESBY CAIRNS SERVICES.

If the new Codeshare Agreement between Air Niugini and Qantas for services between Port Moresby and Cairns is not authorized, Air Niugini expects that Qantas will continue its own services in the Cairns / Port Moresby Air Passenger Market. Additional demand will be met by airlines adding additional services increasing operating costs putting upward pressure on fares.

For reasons described in **section 7 Air Niugini response** this would be more likely to trigger a short term price and capacity battle as each carrier fought to attract sufficient passengers to make its services viable.

In the long term, it is probable conclusion that the result of such a battle could mean that Air Niugini would need to withdraw capacity to become a smaller, less significant operator on the route.

Air Niugini could move from having a profitable route to sustaining losses on services between Port Moresby and Cairns. 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 / Qantas 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 may result 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 than either Qantas or Air Niugini could offer on their own;

- (e) Maintaining a substantial number of airline jobs in Papua New Guinea;
- (f) Greater customer choice of available services, where customers can choose to purchase Air Niugini fares on either a dedicated Air Niugini service or on a Code-share services operated by Qantas Link.
- (g) A stronger, more capable flag carrier for the nation.
