

Air Niugini's Response to Draft
Determination on Cairns-Port
Moresby (vv) Code Share
Application
by Air Niugini and Qantas

Overview

- Need for Authorization
- Reasons for Code Share
- Capacity Issues
- Competition Issues
- Public Benefit Issues
- Clarification of Facts

Need for Authorization

- ANL accepts the position that this code share arrangement will require ICCC authorization hence ANL application for the commission's consideration.
- ANL thanks the Commission and it's staff for its effort in carrying out the review of the application

Reasons for Code Share

Code share has become a very common practice in the aviation world today. This is reflected in the number of airlines code sharing one aircraft in many routes in Australasia, Europe and North America.

The common reasons for code sharing are:

- (1) insufficient demand/passenger volume in a route to have its own service but wish to provide market presence,
- (2) demand to a destination is low and the capability of the airline (aircraft utilization) is needed in other sectors,
- (3) restrictions imposed by bilateral and airport slots availability restrictions

In the case of ANL's application, reasons (1) and (2) are relevant.

Reasons for Code Share

ANL noted the above reasons are used by various airlines around the world to enter into code share agreements. Recently Air Pacific has suspended its services to Narita and has commenced services to Hong Kong (3x wkly) and these services are understandably code shared with Cathay Pacific.

In ANL's case, there has been a significant change in circumstances causing reduction in demand in Cairns - Port Moresby sector, especially due to Japan sector impact. ANL has made a decision to suspend all flights to Japan hence the transit passengers which created major portion of demand will disappear causing the route to be a thinner route.

In addition, QF has entered the route in its own right in July 2010 providing a significant number of new services forcing **ANL and APNG** to withdraw a number of their services. The capacity drop due to this is discussed separately, however, ANL's capacity reduction has been much greater than APNG.

Capacity Issues

CHANGES IN SHARE OF CAPACITY (I.E. SEATS OFFERED) ON
CNS ROUTE FOLLOWING ENTRY OF QF IN JULY 2010

CNS	Before	After	Change
PX	68.44%	48.64%	-19.80%
QF	15.85%	47.51%	31.66%
CG	15.71%	3.85%	-11.86%
Total	100.00%	100.00%	

Capacity Issues

- As per the table above, ANL's capacity in Cairns – Port Moresby sector following QF entry reduced from 68.4% to 48.6% (19.8% reduction).
- Following QF entry, APNG capacity reduced from 15.7% to 3.8% (11.86% reduction).
- As per the above, ANL lost a larger percentage - 7.9% more than APNG.
- This is an important fact that needs attention during the review of the code share application, which **is missing**.

Capacity Issues

- While the Cairns – Port Moresby capacity issue is the only one relevant to this application, ANL wishes to highlight the total capacity between Port Moresby and Australia (i.e. Sydney, Brisbane and CNS) based on the capacity offered by each carrier before and after entry of QF to Cairns route.

	Before	After	Change
CG	14.98%	10.38%	-4.6%
PX	53.53%	47.22%	-6.3%
QF	23.71%	35.37%	11.7%
DJ	7.78%	7.03%	-0.75%
Total	100.00%	100.00%	

- Based on the above analysis, it is evident on the overall capacity wise, that ANL suffered capacity loss more than all the other carriers. **This fact is also missing in the analysis.**

Capacity Issues (Contd)

Maintaining adequate capacity in the market is important to every airline. Demand on the Cairns route is insufficient for ANL to maintain let alone increase the number of services it provides in competition to QF. The only commercially viable option for ANL to increase capacity in competition with QF on this route is for ANL to code share with QF enabling to **compete with QF similar** to the environment that existed before QF entry .

Competition Issues

The Commission has given insufficient weight to benefits to competition from the Code share.

Post QF entry, the morning and evening services are now **only done by QF and NIL Completion.**

Without the code share, the market will only be served by QF for those services as there is insufficient demand for another carrier to provide an additional service in competition.

The code share will provide additional competition between ANL and QF for those seats which would not occur without the code share. As these are hard block seats, there is a strong incentive for ANL to compete on price as unsold **seats are an absolute loss as acknowledged by the Commission..**

Competition Issues

- The Commission has also appear to have overstated alleged competitive detriments that are likely to result from the code-share.
- The Commission suggests that the code share would force the exit of APNG. There is no evidence to support this argument and it is contrary to historical evidence.
 - APNG entered the Cairns route and significantly increased market share to over 25% between 2005 to 2010 (i.e during the previous code share between ANL and QF)
 - It was the end of the previous code share and entry of QF in its own right which coincided with APNG reducing market share by cutting its services from 6 times a week to 2 times a week and ANL withdrawing its Dash 8-300 services.

Competition Issues

- The **Commission incorrectly suggests** that code share **may** harm competition in other routes which is considered as a major reason for the draft decision.
- For example, the Commission suggests that if APNG ceases to operate on the Cairns route under the code share this will impact other routes as APNG's designation under the bilateral agreement could be withdrawn, making it problematical for it to participate in Pacific Blue Code share between POM-Brisbane. This is incorrect, as confirmed in a letter from the Secretary to the Dept of Transport.
- Further, due to code share more capacity will become available enabling APNG to launch a expansion than exit.

Competition Issues

- **Commission has overstated the positive impact of "competition" without the Code-share:**
- The Commission does not provide any evidence for its assertions that competition without the Code-share will expand the market and lead to lower prices. The Commission is incorrect about the likely positive impact of competition without the code-share. As stated above there has been a change in circumstances as a result of the entry of QF and reduction in demand in this route. Under the circumstances above, the code-share will provide additional competition that will not arise without the code-share.
- The Commission's position is contrary to the historical evidence of what happened under the previous Code-share, and what Air Niugini expects to occur under the proposed Code-share:
 - As noted above, the previous Code-share ended on 1 July 2010, and Qantas entered in its own right (ie, "competition without the Code-share"), APNG significantly reduced the number of services it offered on the Cairns route as well as ANL.

Competition Issues

- The ICCC has asserted that, in the absence of a Codeshare, Air Niugini may increase the number of services it operates in competition with Qantas. **This is incorrect**, as there is insufficient demand to justify this. As a result of the changed circumstances outlined above, (i.e reduction in demand on the Cairns route and the entry of QF onto the route) the Cairns route is extremely thin.
- Between January to June 2011, ANL has lost K3.4M on the Cairns route. See next slide.
- ANL Board has resolved in July 2011 Board meeting, regardless of whether or not the proposed code share is permitted:
 - (1) to consider cutting Friday and Sunday overnight services; and
 - (2) to change equipment downgrading capacity on other services; and reducing capacity in excess of 20%
 - (3) to deploy the aircraft to more **demand driven domestic** routes.

Competition Issues

Cairns Route Profit & Loss	
January to June 2011	
Passenger No	21057
Load Factor	47%
No of Flights (Cycles)	439
Average Fare	493
Profit/(Loss)	-3,487,273

Competition Issues

- As ANL submitted in response to the Issues Paper, yields decreased over the full life of previous Codeshare. ANL considers that price (ie yields) will be more competitive under Codeshare than without Codeshare.

Competition Issues

- ANL also wishes to clarify that the reduction in prices/yields and increase in demand for services under the Code-share were not purely a result of the entry of APNG as suggested by the Commission. This is common to all international routes.
- The movement of prices is affected **SIGNIFICANTLY** by a number of things, including international exchange rates [**refer to Clarification of facts slides**]. As demonstrated in the calculation USD200 in 2003 equals PGK795 and in 2010 PGK527. This is a **33.71%** reduction due to exchange rate movement. **Lack of INDUSTRY KNOWLEDGE is seriously reflected in the COMPETITION / YIELD REDUCTION ANALYSIS.**
- ANL itself has also contributed to growth in passenger numbers on this route over the duration of the Codeshare (e.g through increased Asian services).
- Even if APNG did cause yields to decrease when it entered in 2005, this factor, together with the significant market share gained by APNG following its entry, demonstrates its ability to effectively compete while a code-share between ANL and Qantas is in place.

Competition cont.

- Commission appear to have disregarded the issue of efficiency claim ANL claimed through code-share.
- ANL has to give employment, accommodation, utility cost, security etc. Increasing operating cost and also CNS has around 5% - 10% cheaper fuel cost than POM.
- By the code-share ANL can have the access to these cost efficiencies allowing a better airfare to the public. Without the code-share such benefit and competition will be lost.

Public Benefits Issues

- **The Commission has understated the significance of public benefits that result from Code-share:**
- There is no evidence for the Commission's assertion that claimed economic benefits (eg, tourism, allocative efficiency) are likely to be greater without Code-share than with Code-share. Only passing comments.
- The Commission has given insufficient weight to the significant public benefits ANL outlined in the Application and response to Issues Papers that will occur as a direct result of the Code-share, and will be lost to the public if the Code-share is not authorised.

Public Benefits Issues

- The Commission has overstated the level of assistance from the shareholder and given insufficient weight to CSOs carried out by ANL. ANL has only received one assistance in 2008 in relation to the Japan route, which has not offset the considerable losses incurred on that route. No subsidy has been received on the other domestic loss making CSO routes. Servicing unprofitable routes also provides significant flow on effects to consumers able to travel between remote destinations.
- In its response to the Issues Paper, ANL provided a confidential estimate of the net saving to PNG economy and the ancillary revenue to various tourism related operators, as a result of the Code-share.
- The Commission appear to have **IGNORED THE suspension of services to the rural community** by the operator and still remained suspended whereas ANL has continued to serve the rural community and inter regional travel at major loss to the airline.

Public Benefits Issues

- The extent of the public benefits previously identified by ANL apply irrespective of the relative number of seats offered by each carrier on a flight (ie, the fact that the current proposed agreement only covers 5 hard block seats does not diminish the public benefit from the code share)
- In any case Air Niugini expects this seat number to increase over time, subject to sufficient demand. For example, Code-share will allow ANL to offer "add on" services to connect to a wider range of destinations, including locally within PNG, which does not depend on the number of seats. ANL can deploy resources freed by the Code-share on other routes, including loss making domestic routes.
- ANL passengers can earn Loyalty points all way to CNS and VV under code-share which is not possible without code-share.

Public Benefits Issues

- The Commission has taken into account irrelevant considerations
- ANL reiterates its earlier submissions that issues that apply equally with or without the Codeshare are not relevant to the authorisation application, e.g:
 - Historical "state aid"/subsidies (even if these were relevant, they are significantly outweighed by CSOs)
 - Designation and capacity allocation on other routes
 - Competitive neutrality
 - Government intervention in competitive markets

Public Benefits Issues

- The reason why CSOs are relevant is because they flow directly as a result of the Code-share, as the Code-share frees resources of ANL to be deployed in other areas including the provision of CSOs (eg, loss making domestic routes). Even if subsidies do need to be taken into account, they are significantly outweighed by the CSOs
- Commission appear to have **IGNORED THE PNG local conditions, community and shareholder expectations** from ANL and made an analysis in isolation as an academic exercise.

Clarification of Facts

- ANL wishes to clarify a number of facts relied upon by the Commission
 - The pie chart on page 7 of the Draft Determination could be potentially misleading as it shows passenger numbers only according to operating carrier (not marketing carrier) for the whole Australian market.
 - A more realistic representation of the passenger market on the Cairns route would show by marketing carrier that the current market share is QF 49%, ANL 47%, and APNG 4%

Clarification of Facts

- The following slides demonstrate that currency exchange rates have a significant impact on the airfares as shown by the fluctuation in the PGK value of a USD200 fare over time. This needs to be taken into account by the Commission in any analysis of the movement of airfares over time (e.g where the Commission asserts that airfare reductions were a result of the entry of APNG on the Cairns route).
- In the tables below:
 - IROE = IATA Rates of Exchange (Source: IATA Composite Resolution RADAR Database)
 - BSR = Bank Selling Rate (Source: Bank of PNG website)

Clarification of Facts

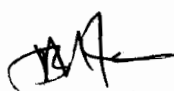
Date	PGK @ IROE	USD	Average Fare (USD)	PGK FARE
1oct-31dec02	K3.9755	\$0.2515	\$200.00	K795
1jan03-31mar03	K3.9063	\$0.2560	\$200.00	K781
1apr04-30jun04	K3.1876	\$0.3137	\$200.00	K638
1apr05-30jun05	K3.0706	\$0.3257	\$200.00	K614
1apr06-30jun06	K3.0217	\$0.3309	\$200.00	K604
1apr07-30jun07	K2.9437	\$0.3397	\$200.00	K589
1jan08-31mar08	K2.7538	\$0.3631	\$200.00	K551
1apr09-30jun09	K2.8332	\$0.3530	\$200.00	K567
1apr10-30jun10	K2.6374	\$0.3792	\$200.00	K527
1jan11-31mar11	K2.6347	\$0.3796	\$200.00	K527

Clarification of Facts

Date	AUD @ IROE	USD	Average Fare (USD)	AUD	BSR 1PGK= AUD	PGK FARE
1oct-31dec02	\$1.8320	\$0.5458	\$200.00	\$366	\$0.4578	K800
1jan03-31mar03	\$1.7794	\$0.5620	\$200.00	\$356	\$0.4396	K810
1apr04-30jun04	\$1.3226	\$0.7561	\$200.00	\$265	\$0.4044	K654
1apr05-30jun05	\$1.2634	\$0.7915	\$200.00	\$253	\$0.4158	K608
1apr06-30jun06	\$1.3565	\$0.7372	\$200.00	\$271	\$0.4532	K599
1apr07-30jun07	\$1.2871	\$0.7769	\$200.00	\$257	\$0.4056	K635
1jan08-31mar08	\$1.1439	\$0.8742	\$200.00	\$229	\$0.4006	K571
1apr09-30jun09	\$1.4052	\$0.7117	\$200.00	\$281	\$0.4940	K569
1apr10-30jun10	\$1.1008	\$0.9085	\$200.00	\$220	\$0.3995	K551
1jan11-31mar11	\$0.9892	\$1.0109	\$200.00	\$198	\$0.3704	K534

6 September 2011

Mr Bob Lowi
Independent Consumer and Competition Commission
PO Box 6394
Boroko
National Capital District

Lorna
Copy Warden, David,
Bob & Fidelis.

7/9/11

Dear Mr Lowi

SUBJECT: APPLICATION BY AIR NIUGINI (ANL) FOR CODESHARING ARRANGEMENTS WITH QANTAS (QF)

We refer to the conference held in your offices on 18 August 2011 in relation to the above matter.

Airlines PNG (APNG) wishes to respond to various statements made in the Air Niugini Response to the Draft Determination on Cairns – Port Moresby (vv) Code Share Application as follows:

1. ANL's capacity reduction has been much greater than APNG (19.8% vs 11.86%)

The percentage comparisons used by ANL are in relation to each carrier's share of capacity on the route as a whole. In July 2010 Qantas commenced operations with 888 seats per week in each direction. While since then both ANL and APNG have reduced their own capacity there has still been a significant net increase of overall capacity on the route. Accordingly, the percentage amounts used by ANL are more a reflection of the diluting effect that the introduction of Qantas services has had on the share of overall capacity for each of ANL and APNG.

In terms of capacity change APNG points out that in July 2010 the airline reduced its number of weekly services in each direction between Port Moresby and Cairns from six to two. This meant a reduction from 216 to 72 seats which represents a change of 67%.

Prior to July 2010 ANL operated 1,100 seats in each direction on the route. In the conference held on 18 August the ANL CEO commented that ANL had reduced its capacity on the route by 250 seats which accounts for 22% of its previous total.

Accordingly, in percentage terms APNG argues that its own capacity reduction is more significant than that implemented by ANL.

2. ANL has suffered capacity loss between Port Moresby and Australia more than all other carriers

Again the statistics used are more a reflection of the diluting effect of the introduction of Qantas services rather than a meaningful representation of the actual seat reductions implemented by ANL and APNG.

3. Post QF entry, the morning and evening services are now only done by QF and nil competition

This statement is factually incorrect. APNG continues to operate early evening services from Port Moresby to Cairns each Friday and Saturday and early morning services from Cairns to Port Moresby each Saturday and Monday. Consumers have a clear choice between Qantas and APNG services on the aforementioned days.

4. The Commission suggests that the code share would force the exit of APNG. There is no evidence to support this argument and it is contrary to historical evidence.

In its letter to the Commission dated 3 December 2010 APNG stated:

In the event the code share agreement was allowed it certainly follows that APNG would withdraw from the route since supply would far outweigh demand notwithstanding the projected growth in traffic.

In response to the contention that APNG entered the Cairns route and gained market share at a time when the previous code between ANL and QF was in place, this can be distinguished from the current circumstances in that QF was only a marketing carrier on the route at the time and there was substantially less overall capacity meaning less disparity between supply and demand.

5. There has been a reduction in demand on the Cairns route


On our enquiries there has been a year on year increase of 37% in traffic on the Cairns route since July 2010 when Qantas commenced its own services.

	2009-10	2010-11	% Change
July	6429	8347	29.83%
August	5600	7872	40.57%
Sept	6017	9006	49.68%
Oct	6102	8703	42.63%
Nov	5993	8353	39.38%
Dec	6163	9814	59.24%
Jan	6064	8881	46.45%
Feb	4891	6397	30.79%
March	5637	7369	30.73%
April	6193	8037	29.78%
May	5821	7184	23.42%
June	6098	7483	22.71%
Total	71008	97446	37.23%

Source: Australian Government; Department of Infrastructure and Transport; Bureau of Infrastructure, Transport and Regional Economics; Statistical Report International Airline Activity July 2009 to June 2011.

Please do not hesitate to contact me should you have any queries.

Yours sincerely,


for **SIMON SIGANTO**

GENERAL COUNSEL & COMPANY SECRETARY

OFFICE OF THE COMMISSIONER

Date: 6/09/2011

Tuesday, 6 September 2011


Email: davidolley@pngmail.net

Phone: + (675) 323 4997 or Mobile + (675) 721 88 495

From:


David WW Olley,
P.O. Box 2108,
Port Moresby NCD
Papua New Guinea

Associate Prof. Dr Billy Manoka (PhD),
Commissioner and Chief Executive Officer,
Independent Consumer and Competition Commission,
1st Floor, Garden City, Angau Drive,
PO Box 6394,
BOROKO
National Capital District.

Received by ICCC Reception Finance & Administration	
Date	06/09/11
Time	3:12pm
Sign	

Lorna
Copy Fidelis, Bob,
Winston & David.

Dear Dr Manoka,


7/9/11

Draft Determination on the Proposal by Air Niugini Limited for Code Sharing Agreement with Qantas Airways Ltd.

I have received your letter dated 24 August 2011 extending the deadline for further written submissions to 6 September 2011.

You already have received my several earlier written submissions and I was also delighted to be invited and to attend the Conference called by Air Niugini Limited and convened by the ICCC on 18 August 2011.

The previous comments and submissions I have made remain valid.

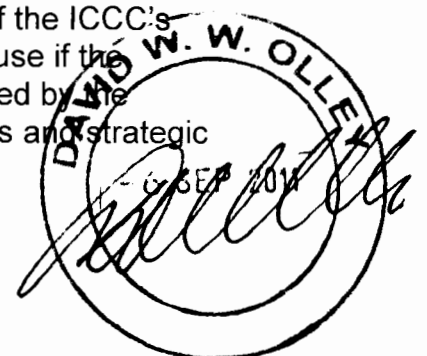
As I said briefly at the Conference on 18 August 2011, when there was some lively discussion concerning "Customer choice", it should be remembered that the market characteristics of this particular route (and probably all Australia/PNG Sectors) is that most users of the airline services are not "Price Sensitive Travellers".

This is somewhat unique and makes it difficult and dangerous for some commentators and analysts to compare (as they have tried to do to support the Code Share Proposal) the CNS/POM Sector with Sectors between Australia and Fiji, and Australia and New Zealand.

The sectors between Australia and Port Moresby including particularly the Cairns/Port Moresby Sector are totally different from Fiji and New Zealand sectors.

In my letter dated 2 May 2011 I went into some detail to express my views on the characteristics of this market. Those comments remain "on foot".

It is essential that this market characteristic remains in the forefront of the ICCC's decision-making model when reviewing its Draft Determination, because if the opportunity for Price Sensitive Travellers to use his sector is diminished by the proposed code sharing being approved, then future economic benefits and strategic



plans concerning tourism, business travel and leisure travel (in either or both directions) might be forfeited and certainly put at risk.

It is imperative that your Determination on this matter does not impede Customer Choice or National Development Opportunities.

Many of us, who live and work in Papua New Guinea, hear a lot about the PNG LNG Project and its impact and benefits.

However it is risky to have "all one's eggs in the one basket" and there must always be scope for alternative economic and development opportunities to be conceived, grow and produce benefits.

It is therefore essential that no anti-competitive arrangements be permitted on the CNS/POM/CNS sectors, and that the market be allowed to operate openly and unimpeded by improper Government Regulations and Determinations, which can lead to the risk of price gouging, cartel operations and other financial activities that can be hostile to the Users and Operators.

Users and potential Operators should not be crowded out by a Determination which permits the Code Share being proposed by Air Niugini Limited.

I remain opposed to the proposed Code Share Arrangement between Air Niugini Limited and Qantas Airways Limited.

In short your Draft Determination dated 15 July 2011 should remain and stand as it is.

With best wishes,

Yours sincerely,



David WW Olley B Bus F Fin