

AVIATION ECONOMICS

**Senate Economics Legislation Committee
Parliament House
Canberra ACT 2600**

Email: economics.sen@aph.gov.au

14 March 2014

Dear Senators,

Re: Qantas Sale Act Amendment Bill 2014

Aviation Economics appreciates the Senate Economics Legislation Committee's invitation to make a submission to its inquiry into Qantas Sale Act Amendment Bill 2014. Aviation Economics is a boutique private company registered to provide aviation related economic information to not for profit organisations seeking to formulate an informed opinion regarding aviation issues pertinent to their particular area of interest.

This submission will be confined to macro comment on the likely impact the legislation will have on the future prosperity of Qantas and its expected reduction in its manpower costs.

We appreciate that the Qantas Sale Act Amendment Bill, if passed in the Senate, would:

- Repeal Part 3 of the *Qantas Sale Act 1992*, and
- Amend the *Air Navigation Act 1920*, to allow Qantas to be included in the definition of an Australian international airline.

In broad terms, we recognise this means Qantas Airways Limited would then be directed and managed in accordance with legislation and regulations applicable to all Australian airlines providing regular public transport and Qantas would no longer be required to comply with obligations that make it unique.

Public reporting of the Parliamentary and Community debate around the Qantas Sale Act Amendment Bill indicates that the proposed legislative changes are, inter alia, likely to:

- Make Qantas more attractive to partner investor(s), and
- Make many thousands of Qantas employees redundant and ultimately lead to a significant reduction in Qantas' manpower costs.

Stakeholder views on the costs and benefits flowing from the Qantas Sale Act Amendment Bill are polarised and Aviation Economics endorses the public statement by the president of the Australian & International Pilots Association *that 'debate around the Qantas Sale Act is unnecessarily absolutist'*. The Bill does not enjoy majority support in the Senate and we believe that the expected lengthy delay in passing the Bill as it is, will mean Qantas will unnecessarily continue to operate unprofitably and put at increased risk the Qantas workforce.

In our opinion, we believe a more generally acceptable legislative solution can be found if Part 3 of the Qantas Sale Act is appropriately amended rather than repealed in its entirety.

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Ownership Restrictions

Majority foreign ownership does not in itself seemingly pose insurmountable challenges to how Qantas operates, where it flies and who it employs. I.e. 35% foreign ownership by two foreign airlines would mean that Qantas is 70% foreign owned, but not controlled by either one.

That the Virgin Australia share registry includes three foreign airlines should indicate that majority foreign ownership in itself will not change the Australian character of Qantas, provided one single foreign entity does not own more than 49%.

Nevertheless, there are control risks associated with allowing a single foreign entity to own 49% of Qantas and Aviation Economics contends that ameliorating considerations need to be put in place if the Qantas Sale Act Amendment Bill is amended to ultimately allow Qantas to be majority foreign owned, but also prohibiting one single foreign entity from owning more than 49% of the company.

We understand that the biggest risk to Qantas, (as the public knows it and to its future Australian character), arises from a decision by shareholders to delist the company to take it private. This risk exists, whether or not Qantas is allowed to be majority foreign owned.

It is our understanding, that the delisting risk posed by one or more large foreign Qantas owners, who together control more than 50% of Qantas' shares, can be effectively negated. Ownership of at least 25% of Qantas shares, if held in perpetuity by Australian interests such as a Qantas Employee Share Trust, would remove this risk.

Reduction in Operating Costs

The following quote from the Securities & Investment Group CLSA, published after Qantas made its restructuring announcement on Thursday February 27th clearly sums up the costs issue:

- *The cost "light bulb" moment has come. The nature of political support is uncertain and it is difficult to believe Qantas can achieve such transformation in three years without changes to the Qantas Sale Act. It has a significant unionised workforce which, anecdotally does not appear too aligned.*

CLSA had previously stated in a prior note to its clients on the 26th of February that:

- *We cannot believe there is not a way to negotiate a win-win between staff and management (for example in the form of lower wages in exchange for equity) that would better align both parties in facing up to the challenges faced by Qantas. Both must share the burden of restructuring – why can they not share the potential upside as well?*

Aviation Economics accepts the prima facie assertion that irrespective of any restrictions imposed on the Qantas share register by the Qantas Sale Act, and/or future Qantas investment by a partner airline(s), that the advent of global open skies means Qantas has to be both capital and manpower efficient if it is to ever be able to purchase next generation cost efficient aircraft it needs to compete internationally.

If Qantas cannot become capital and manpower efficient, it is our belief that Qantas will continue to contract internationally and will ultimately be forced to operate more of its

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existing international services using Jetstar, and/or One World code share flights; assuming it even elects to continue operating internationally.

Air Navigation Act 1920

The decision to also amend the Air Navigation Act of 1920 'to allow Qantas to be included in the definition of an Australian international airline,' is somewhat perplexing to us. This is especially so given the recent announcement by Alan Joyce that:

- *Qantas has decided to put on hold our application to obtain a separate AOC for Qantas Domestic, but maintain separate business structures for Qantas International and Domestic due to the unique strategic challenges we all know these businesses continue to face.'*

On the face of it, it seems to us that the proposed amendment to the Air Navigation Act is only necessary if another Qantas Airline is created by Qantas Airways Limited; the entity that presently conducts all Qantas' International and Domestic operations.

If the Qantas Sale Act Amendment Bill 2014 is passed by the Senate and the Air Navigation Act of 1920 amended as is presently proposed, we believe that intended and unintended consequences are a real possibility. We are not able to say with any degree of certainty what the consequences of amending the Air Navigation Act could be and can only respectfully suggest that the Senate Economics Legislation Committee seek expert advice from restructure specialists and employment lawyers on issues that may arise from a splitting of Qantas Airways Limited.

Employee Equity Participation

Given that Qantas is a service provider, it is our firm view that Qantas should negotiate the necessary reduction in manpower costs in good faith. We believe that the CLSA suggestion of lowering manpower costs in return for equity will greatly assist the passage of the Qantas Sale Act Amendment Bill through the Senate. In the USA, a number of US Airlines recovered from Chapter 11 bankruptcy proceedings using employee equity as the element that brought together otherwise fiercely competing stakeholders.

We understand that employee equity can make possible ownership structures and cost reductions otherwise difficult, if not impossible to achieve if a Qantas Sale Act Amendment Bill is not ultimately passed by the Senate. The economic impact of not eventually passing a Qantas Sale Act Amendment Bill, is, in our opinion, an economic cost neither Australia nor Qantas can afford.

In Summary:

1. Foreign ownership is necessary for capital raising,
2. Cost reductions are necessary if Qantas International is to be reequipped,

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3. Amending the Qantas Sale Act is likely to unleash economic reform sooner than seeking to repeal Part 3 of the Act in its entirety can.
4. Amending the Air Navigation Act of 1920 requires careful consideration if it is the Governments' intention to apply the proposed amendment generically to Qantas and not specifically to Qantas Airways Limited.
5. Employee equity participation has real potential to drive the change, engagement and the economic productivity Qantas needs regain international competitiveness.

For the sake of completeness, attached is our submission to the Senate Rural and Regional Affairs & Transport Committee on **Qantas' future as a strong national carrier supporting jobs in Australia**

Aviation Economics sincerely thanks the Senate Economics Legislation Committee for the invitation to comment on the economic impact the Qantas Sale Act Amendment Bill 2014 is likely to have on Australia and Qantas. We trust that the Committee finds the information we have provided helpful.

Yours Sincerely,

Ian Woods
Executive Director

One Attachment - *Aviation Economics' submission to the Senate Rural and Regional Affairs & Transport Committee on **Qantas' future as a strong national carrier supporting jobs in Australia.***