SUBMISSION BY

QANTAS AIRWAYS LIMITED

TO THE

INQUIRY BY THE HOUSE OF REPRESENTATIVES STANDING COMMITTEE ON PRIMARY INDUSTRIES AND REGIONAL SERVICES

INTO

"INFRASTRUCTURE AND THE DEVELOPMENT OF AUSTRALIA'S REGIONAL AREAS"

SYDNEY

14 MAY 1999

INTRODUCTION

Qantas makes this submission on behalf of its wholly-owned regional airline subsidiary companies -

Eastern Australia Airlines Pty Ltd

Southern Australia Airlines Pty Ltd

Sunstate Airlines (Qld) Pty Ltd

Airlink Pty Ltd

The purpose of the submission is to offer for the Committee's consideration several recommendations which, we believe, would enhance the viability, quality and development of regional airline services, thereby contributing further to the economic and social development of regional communities.

While some of the recommendations are affected by the policies of certain State Governments, their implementation would lie, we believe, well within the ambit of Commonwealth policy in relation to air transport, competition and regional development, and thus have relevance to the Commonwealth Government and this inquiry.

The submission is intended to make the case for limited Commonwealth assistance (including subsidies where appropriate), directly or indirectly, in respect of:

1. air passenger services between Sydney/Melbourne/Adelaide and airports in Tasmania;

2. charges at regional airports;

3. expansion of supporting technical infrastructure in regional centres, including aircraft maintenance hangars;

4. State levies on intra-state air fares (in Western Australia);

5. regulation (licensing) of intra-state air services in NSW and Queensland.

Although we are not able precisely to quantify in financial terms the end-benefits to be derived in regional centres, our belief is that the initiatives requested of the Commonwealth, while being modest in the quantum, would represent an important contribution to the efforts being made by regional airlines to provide and maintain effective linkages between regional and capital-city communities around Australia. These would come at a time when public attention is focussed on the need to reinvigorate economic and community life in regional centres and to redress in part the effects in those regions of the withdrawal of industry and services, including loss of employment and investment.

THE QANTAS "FAMILY" OF REGIONAL AIRLINES

Regional airlines in the Qantas Group make a significant impact on regional Australia. Between them, the four airlines carry more than 2.5 million passengers per annum, operate to 47 ports, employ more than 750 full time staff and some 500 contracting staff, and sustain engineering, maintenance and crew-basing services in a range of centres outside the east coast capitals, including Perth, Mackay, Rockhampton, Canberra, Cairns, Darwin, Adelaide, Tamworth, Mildura and Launceston. Attached to this submission is a map of the combined 50 routes of the Qantas regional airlines. It amply demonstrates their extensive "coverage" of regional Australia.

Membership of the Qantas Group allows the carriers to increase the range of benefits for their regional passengers. Passenger services operated by the regional airline companies are marketed through Qantas' global computerised reservations system, which effectively links regional centres around Australia with the travel industry around the world. This enhances the ability of the carriers to market their services to the tourism industry, which provides an important supplement to regional airlines' revenues generated by their primary regional and capital city-origin markets in Australia. Interstate and international tourism, promoted by Qantas, also brings added wealth to regional hospitality and transport businesses.

Passengers flying on Qantas' regional airlines, who are members of the airline's frequent flier programmes, enjoy the same access to lounge facilities at major airports as core jet-service customers. These benefits also extend to the facilities overseas provided by the airlines associated with Qantas in the **one**world group (British Airways, American Airlines, Canadian Airlines, Cathay Pacific, Iberia and Finnair).

The Qantas regional carriers offer a range of discounted air fares, both to stimulate demand in their markets and to cater to the differing needs of different market segments.

ISSUES FOR CONSIDERATION

1. Bass Strait Subsidies

Southern Australia Airlines currently operates a total of 86 round trip services per week between the mainland (Melbourne, Adelaide and Sydney) and Tasmania (Hobart, Launceston, Burnie and Devonport). These services directly compete not only against rival airline services, but also against sea transport. Under current arrangements, certain subsidies for sea operators put regional air carriers at a competitive disadvantage.

Travel on the Spirit of Tasmania from Melbourne to Devonport and return attracts a substantial Federal Government subsidy when a motor vehicle is transported. The Federal Budget provides for a passenger vehicle subsidy of $11.2 million (estimated) in 1999-2000; an estimated $13.6 million in rebates will be provided to passengers in 1998-99. At peak times a one-way fare for the accompanied motor vehicle is $190. With the subsidy the traveller pays just $40. This represents a powerful incentive to passengers to travel by sea as unaccompanied cars cost $400 each way. This not only disadvantages regional airlines, but also the vehicle rental industry in Tasmania which relies on airline passengers to provide a substantial share of business (obviously sea passengers transporting their own vehicles have no need to hire vehicles on arrival in Tasmania). Fly-drive is considered a mainstay of tourism in Tasmania and an industry segment with considerable future potential, given favourable competitive circumstances.

The Tasmanian Government also has subsidised sea travel from Melbourne to Georgetown on the Seacat catamaran. In this case the subsidy is indirect, being not a discount on the passenger's ticket but financial relief for the Seacat operator who lost $3.7 million in 1997/98 and may have lost more in the 1998/99 Christmas/New Year peak period (when it operates). If there were no subsidy, ticket prices would be higher to offset the operating losses of the vessel.

Already there is a shortage of airline capacity across Bass Strait at certain periods. However, airlines cannot be expected to increase capacity at their own cost if Governments subsidise the operations of their competitors - i.e. the ship operators. This committee may wish to consider recommending some incentives to regional airlines to increase capacity across Bass Strait, perhaps in the form of some reductions (as subsidies) in landing charges at Tasmanian airports and/or as lower charges for air traffic control services provided by Airservices Australia. Other options could also be considered.

2. **Airport Charges at Regional Centres**

Regional airports in Australia are virtually entirely individually-owned - often by local Government councils, sometimes by private companies or consortia. User (landing) charges at varying levels are imposed using a variety of formulae, including aircraft weight and passenger count. Only in South Australia is there a Government standard charging rate.

It is not always the case that fees collected from regional aviation are used solely for the maintenance and improvement of the airport services provided, with the result that end-users sometimes have to be charged an unnecessary increment on the air fare. A further issue is that regional airport charges can sometimes be comparatively excessive when compared against ticket prices. For instance at Armidale, the landing fee and passenger head taxes of $26 represent nearly 10 per cent of the cost of a round trip ticket to Sydney.

Given the policy and legislation attached to its airport privatisation agenda, the Commonwealth Government appears not to have any wish to intervene in specific pricing arrangements at Australian airports. Nor does it appear to want to change the ownership status of regional airports, and their attendant pricing policies. Nonetheless, there are significant anomalies in regional airport service pricing which, in the interests of efficiency and cost reduction, need urgent attention and, in our view, warrant some action at the Commonwealth level in the context of assisting regional development. This could extend to carrier subsidies at locally-owned regional airports where they are justified, including in those instances where landing fees were not consistent with the national average.

3. **Technical Infrastructure Development**

Eastern Airlines currently operates engineering and maintenance facilities in Tamworth for the purpose of supporting the technical operations of its fleet of 11 aircraft. These facilities represent a capital investment of $5.5 million and generate ongoing operating costs of more than $8 million per annum, including manpower costs. Included in these costs are State payroll taxes of some $140,000.

While Eastern has no plans to close or relocate its Tamworth technical facilities, there must always be an ongoing evaluation of the economic efficiency of current arrangements compared to alternatives, such as relocation to Sydney or another capital where the benefits of synergies, cost savings or other changes might possibly be realised, thus improving profitability without compromising safety or other technical requirements.

Similarly, Southern Airlines has an investment of some $1 million in hangar facilities in Mildura and an additional $3.5 million in aircraft spares. In Launceston, the airline employs eight engineering staff and holds another $1.5 million worth of spare parts. Southern also has an interest in principle in setting up a second hangar facility in Launceston provided the necessary financial support, possibly in the form of a capital-investment subsidy, can be found.

The Committee may wish to consider whether, under Commonwealth Regional Development policy, targeted financial assistance could be directed towards offsetting at least some of the relatively large capital expenditures required to expand and/or improve regional airline engineering and maintenance facilities located in specific regional centres. This would have the double benefit of maintaining and enhancing employment opportunities for skilled tradesmen and women locally, while freeing-up financial resources of the airlines for other purposes, such as market development.

4. **State Taxes**

In Western Australia a transportation levy is imposed on scheduled carriers for intra state travel. A charge of 1.5 per cent of all intrastate revenue is collected and used for regional airport development. In Airlink's case the amount is over $650,000 per annum. As far as we know, no airport to which Airlink flies in the State benefits from this charge. It is an additional cost of doing business for scheduled carriers while charter carriers, which account for 40 per cent of air travel within Western Australia, are exempt from the levy.

5. **Regulation - Competition vs Licensing**

In most of Australia, regional airlines operate in a commercially de-regulated environment in which any and all airline companies, provided they meet the safety standards laid down by the Commonwealth safety regulator, CASA, are free to offer their services on any intra-State route as they see fit. The exceptions are NSW and Queensland, both having decentralised populations, in many cases located long distances from capitals and other major traffic-generating centres. While these demographics help to create demand for air services within those States as a whole there are few instances where traffic flows at similar levels, leading to the need for different types of air services across the range of routes.

Traditionally, these States have used route licensing, rather than open competition, as the foundation for commercial operations in certain regional markets. In NSW, all intrastate regional routes (at least for the moment) are regulated - i.e. licensed to specific operators. In Queensland, a mix of regimes is used, ranging from full competition on coastal routes from Coolangatta to Cairns, through non-subsidised, monopoly licensing on Cairns-Horn Island (Torres Strait) and Cairns-Weipa, to subsidised monopoly routes between isolated, smaller centres of Western Queensland (Birdsville, Bedourie, Boulia, Charleville, Winton, Longreach, Thargomindah etc).

The use of licensing (v market competition) is based on the well-founded belief that in small, virtually mature markets which have little if any growth potential, the best way to ensure continuation of safe and reliable service, at reasonable prices, is to create a "partnership" between Government, acting of behalf of the communities, and business, in which all available revenue is directed exclusively to the one carrier that successfully bids for the licence at the time of its renewal. Without this, continuing service and investment is put at what the Governments believe is an unacceptable risk that communities may become isolated when competing operators downsize or withdraw when price competition renders their operations unviable.

Experience by Eastern in NSW and Sunstate in Queensland leads Qantas to believe that intrastate markets which generate fewer than 100,000 passengers per annum probably would not sustain open competition over the long term. These markets should therefore continue to be served under licensing arrangements as best defined by the Governments concerned as meeting their respective tests of public (State) interest.

The 100,000 passenger-breakpoint figure is calculated simply by dividing the traffic between two operators, each flying 36-seat aircraft, such as the Dash-8, three times a day each way (and possibly four times) at an average passenger seat factor of 60 per cent. This arrangement has the advantage of offering the public direct price/service competition between Australia's two major airline groups (Kendell, Hazelton, Flight West etc are affiliated with Ansett; Eastern, Southern, Sunstate and Airlink with Qantas) using advanced, safe and comfortable aircraft designed for regional/commuter operations, with two pilots and in-cabin services. It should be noted that each operator in this environment would need to acquire at least one Dash-8 aircraft per route, necessitating considerable capital investment, including a $16 million purchase cost per aircraft.

The issue is relevant to this inquiry because the States and the Commonwealth entered into the Competition Principles Agreement (the Hilmer Agreement) in 1995. This Agreement, one of three making up the National Competition Policy, imposes on the States an obligation to open their licensed intrastate air routes to competition by the year 2000 unless compelling public-interest arguments can be sustained which demonstrate that:

- the benefits of restriction to the community as a whole outweigh the costs; and

- the objectives of State legislation can only be achieved by restricting competition.

In NSW, the Independent Pricing and Regulatory Tribunal recommended in July 1997, after considerable public consultation, that all air routes within the State be deregulated simultaneously. Eastern Airlines supported deregulation, on the basis that public benefit would be enhanced by allowing major carriers to compete in the bigger (100,000 passengers-plus) markets. In doing so, Eastern indicated it had no plans to enter smaller markets on a competitive basis, and was in any event intending to phase out all of its aircraft with fewer than 36 seats, leaving routes servicing the more isolated communities to (monopoly) operators of small aircraft. A final State Government decision on licensing in NSW is still awaited. Meanwhile current licences are due to expire in the near future, leaving all operators and communities in some continuing uncertainty.

In Queensland, the State Government is currently reviewing State transport legislation in accordance with requirements under National Competition policy. Sunstate has informed this review that it seeks no change to current arrangements in which it operates in competition on the coastal routes, does not participate in the Western Queensland subsidised routes and provides service on one (Cairns-Horn Island) route under exclusive licence. The Torres Strait route generates considerably fewer than 100,000 passengers - just over 42,000 in 1997/98 with no forecast growth in 1998/99.

In these circumstances, Qantas suggests the Committee consider recommending that the Commonwealth and the States agree on a joint regulatory policy framework for regional aviation which, based on the Qantas model, would allow the States to continue to licence intrastate routes with passenger volumes up to 100,000 per annum, using arrangements that best suit the needs of regional communities within their borders. Routes generating more than 100,000 passengers should be opened to competition, as per the State's obligations under Hilmer.

CONCLUSION

Qantas accepts that the Commonwealth is limited in the extent to which it can provide financial assistance to industry, even to the industry of aviation which has an important strategic role to play in regional development across Australia. It also recognises that this Committee will most likely be asked to recommend financial and other forms of assistance to a vast range of activities, many of which may well be able to make a convincing case, at least for some qualified support.

For these reasons we have confined this submission to a short discussion of a limited number of areas where we believe some assistance is not only justified in the short term, as a means to address fairness questions and remove anomalies, but would contribute in the longer term to industry competitiveness, with shared benefits for regional Australia.

We would welcome the opportunity to discuss our proposals with the Committee in more detail at public hearings, or with any expert independent advisers which the Committee may appoint to assist it with the current inquiry.

14 May 1999