

Tourism Tasmania

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Professor Richard Snape
Presiding Commissioner
Productivity Commission
Airports Enquiry
LB2 Collins St East
Melbourne, VIC 8003

Dear Sir

Price Regulation of Airport Services

Thank you for your invitation to make a submission to the Commission on the need for prices regulation of airports, and the appropriate form of any prices regulation.

Air access is of critical concern giving our island status and the choice by over 80% of all visitors to use that medium to get to Tasmania. The role of pricing of regular passenger services plays an even more critical role in determining choice of holiday location for many Australians as well as being an impediment to families keeping in frequent contact.

The cost of ground services to carriers is, as a consequence, of great importance to the Tasmanian Government. Recent efforts to attract discount carriers to the State have stumbled at times due to local airport pricing (including Air Services Australia Charges).

I commend the initiative of the review and trust this input is of assistance to your deliberations.

Yours sincerely

Rob Giason
CHIEF EXECUTIVE
attachment

Price Regulation of Airport Services

**A Submission to the Productivity Commission by Tourism Tasmania
March 2001**

Background:

The Current Aviation Market and Tasmania

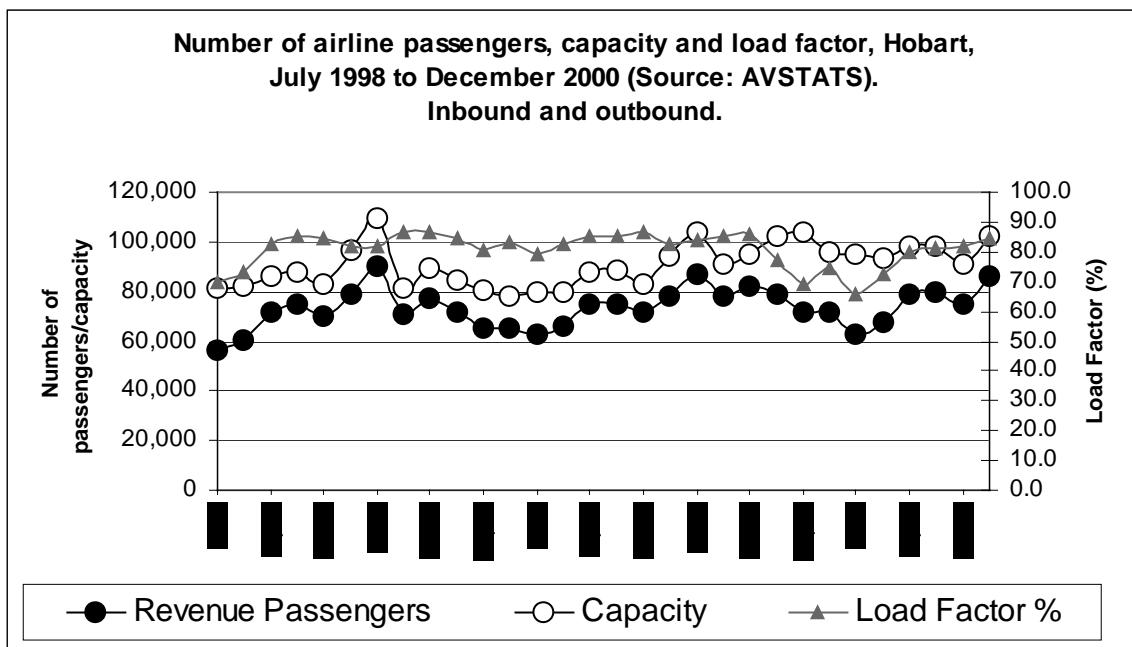
Annual domestic aviation growth in Australia is now in the 12 – 14% range with spectacular surges in the south-east triangle of Adelaide-Melbourne-Sydney-Brisbane where Impulse and Virgin services are concentrated. Comparing December 2000 with December 1999, the new competition has coincided with growth of 48.2% for the Brisbane-Sydney route (35%, 28% and 28% for Sep, Oct, Nov), 18.7% for the Sydney-Melbourne route (24%, 13% and 13% for Sep, Oct, Nov) and 33.3% for the Brisbane-Melbourne route (**AVSTATS, 2000**). Average monthly load factors for Impulse over the December and January periods for both inbound and outbound activity across all sectors ranged from a low of 73% to a high of 82%.

While early days there is every evidence available that the experience of sustainability of low cost entrants to a previously stable albeit highly priced route from overseas destinations, will be repeated in Australia.

Further evidence of the market growth potential for Tasmania is provided with Tourism Tasmania's own TVS Special Fares Survey which covered the period in September and October 2000 when \$55 fares were placed on Melb to Tasmanian ports as well as most other city pairs across the country. The survey showed that 34% of the fares to Tasmania were purchased by visitors who had no plans in the next two years or more to visit Tasmania and that the primary reason for purchasing the tickets for 92% was the price of the ticket. Visiting friends and relatives was the motivation of 53% of those travelers, with the remainder being predominately leisure focused.

Existing load factors into Hobart as evidenced in Fig 1. are continuing at the high levels that have been apparent over the past two years (other than the short period in the middle of 2000 prior to the Olympic Games and building on the back of concern over GST when all domestic travel declined)

Fig 1. Passengers, Capacity and Load factors – inbound and outbound from Hobart



In respect to demand for specific destinations, research shows there is a strong preference amongst Australians to holiday in Tasmania (25%), yet just on 3% actually get here (**RMR Holiday Tracking Study, 2000**).

While there are numerous factors which influence the choice of holiday destination, in Tasmania's case there is strong evidence that price is a major inhibiting factor (**BDA Research, 1999**). The following table gives contemporary comparisons with other destinations as at January 2001 and prior to the announcement by Impulse Airlines that it would start services to Tasmania from 2 April 2001:

Table 1 **Walk-up fare** **Cheapest fare**

Melbourne – Hobart	\$299	AN/QF	\$160 (21 day advance purchase)
Sydney – Hobart	\$428	AN/QF	\$216 (“ “ “ ”)
Sydney – Brisbane	\$169	Virgin	\$69 (Internet special)
Sydney – Brisbane	\$179	Impulse	\$72 (“ “)
Melbourne – Brisbane	\$259	Virgin	\$109 (“ “)
Melbourne – Sydney	\$167	Impulse	\$72 (“ “)

Effective 2 April the corresponding fares to Hobart and Launceston are as follows:-

Table 2	Walk-up fare	Cheapest fare
Melbourne – Hobart	\$299 AN/KN	\$69.30 (21 day advance purchase)
Melbourne – Hobart	\$299 QF/SA	\$71.50 (21 day advance purchase)
Melbourne – Hobart	\$172 Impulse	\$72 (Web Hot special)
Sydney – Hobart	\$428 AN/QF	\$145 (21 day advance purchase)
Sydney – Hobart	\$324 Impulse	\$144 (Web Hot special)
Sydney – Launceston	\$380 AN/QF	\$201 (21 day advance purchase)
Melbourne –Launceston	\$261 AN/QF	\$144 (21 day advance purchase)

Tourism Tasmania strongly believe the introduction of competitive pricing behavior onto Tasmanian routes will substantially grow visitation to the State as well as provide the means for Tasmanians to travel out of the state more frequently and enable families with relatives interstate to have more contact. While early days yet, the first week of booking activity for Impulse has seen in excess of 7,000 inbound and outbound bookings taken with increased levels of activity also being experienced by Qantas and Ansett with their competitive response fares.

A major impediment to an earlier breakthrough with either low cost carrier was seen to be the cost of terminal space and airport fees in Tasmania including the Air Services Australia (ASA) charges. As an example, under the current ASA pricing regime, it currently costs \$15.17 per landed tonne at Hobart Airport and only \$4.47 at Melbourne Airport.

Opportunities to grow aviation traffic to Tasmania also exist in the international market. Melbourne Airport (owned by APAC as is L'ton) has grown international traffic substantially over past two years and is keen to develop on-carriage to Tasmania and particularly Launceston. Tourism Victoria also keen to develop partnership marketing opportunities as further leverage to selling Melbourne (with regional highlights such as Tasmania included).

Trans Tasman opportunities also exist with the Single Aviation Market concept for Australia and New Zealand albeit the market between Australia and New Zealand currently has plenty of capacity.

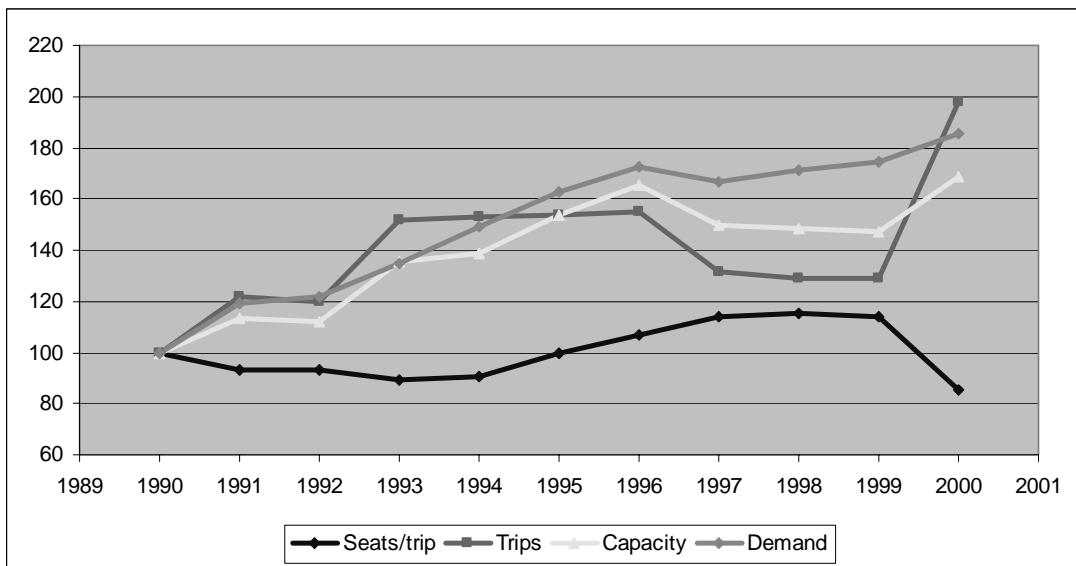
Fig 2 shows the balance of supply and demand for air travel across Bass Strait on an annual basis for the past decade. Recent trends in the balance of supply and demand are shown in more detail in Fig 1.

The analysis is extended further in Table 3 which shows trends in load factors on the main interstate routes to/from Tasmania.

Table 3**Airline Load Factors for Major Routes**

Route	Load Factor			
	2000	1999	Average 1995-1999	Average 1990-1994
HBT-MEL	0.80	0.85	0.80	0.75
HBT-SYD	0.76	0.74	0.72	0.67
LST-MEL	0.79	0.83	0.72	0.78
LST-SYD	0.82	0.80	0.77	0.77
DPO-MEL	0.72	0.68	0.68	0.66
WNY-MEL	0.67	0.64	0.64	0.66
KNS-MEL		0.65	0.63	0.50

Capacity is influenced by a number of factors but principally by aircraft size and service frequency. Therefore to more fully understand recent trends in load factors, it is necessary to examine trends in average aircraft size and frequency. Fig 2 shows these trends for the Hobart-Melbourne. Note that the time series for seats/trip, trips/day, daily capacity and demand have been indexed back to 1990 to aid comparison of the underlying trends.

Fig 2**Demand and Supply Factors – Hobart to Melbourne**

All this is provided by way of background to the Commission in respect of the fragility of the Tasmanian market to price and our total reliance on the medium of air transport as our primary connection to the world.

The Review:

As I understand it the scope of this enquiry is to report on whether there is a need for prices regulation of airports, and the appropriate form of any prices regulation having regard to:-

- The current price cap for aeronautical charges no longer operating after the first 5 years of private ownership;
- Future prices regulation only applying to those aeronautical services and airports where potential to abuse market power exists;
- Alternate approaches to prices regulation to protect users and minimize compliance costs on airport operators and government and which should promote the efficient operation of airports; and,
- Prices regulation which facilitates benchmarking between airports, competition in provision of services within airports and provides for commercially negotiated outcomes.

Further, in making recommendations the Commission will;-

- Review existing prices regulation at airports;
- Identify the rationale for any future prices regulation and relevant alternatives and benefits flowing therefrom; and,
- Identify groups likely to be affected by the current situation and alternatives identified.

My understanding of prices oversight is that it includes aircraft movement facilities and activities and passenger processing facilities and activities as well as certain aeronautical related services not including en-route navigation, terminal navigation, aeronautical information, communications and firefighting and rescue services.

Issues:

The comments provided directly relate to the experience and evidence available from the Tasmanian circumstances – some of the issues to be raised may be less relevant in major centres where new regulatory arrangements apply, they are nonetheless substantial issues in the Tasmanian market.

Location Specific Air Services Australia Charging

While airport operators do not have responsibility for those aeronautical services not covered by the price cap (en-route navigation, terminal navigation, aeronautical

information, communications and firefighting and rescue services) and are potentially outside the scope of the Commissions enquiry, Tasmania sees the need to again raise the issue of Air Services Australia (ASA) charging regimes described as location specific pricing. This policy of the Federal Government is a major impediment to the growth of air services in Tasmania as Table 4 indicates.

The cost of flying comparable aircraft to major capital cities compared to regional centres such as Hobart is discriminatory in its application and ignores the intent of recent policy initiatives designed to make regional airports more attractive for international services. The carriers generally see Tasmania as a low yield destination due to its high leisure content and cost imposts such as those brought about by ASA charging significantly increase the financial risk in flying to the State.

While not directly offering a solution to the problem – the real issue to be dealt with is the need for consistent policy by Government across the range of aviation initiatives – presently the implied benefits of one policy are undermined by another.

Proposals to seek competitive tendering of ASA charges in the near future will only exacerbate the issue in regional centres where natural monopolies for the provision of such services often exist.

Table 4. Comparative pricing of ASA charges for various aircraft types and various destinations.

Aircraft	Route	Terminal Navigation	Rescue and Fire	Air Service Charges			
				NAV En-Route	Met Service	Noise Levy	TOTAL
B737-300	MEL-HBT	\$454.37	\$474.58	\$210.29	\$9.62	\$0.00	\$1,148.86
	MEL-LST	\$454.37	\$524.18	\$151.51	\$6.93	\$0.00	\$1,136.99
	MEL-DPO	\$0.00	\$0.00	\$147.78	\$6.76	\$0.00	\$154.54
	MEL-WYN	\$0.00	\$0.00	\$137.85	\$6.31	\$0.00	\$144.16
	MEL-ADL	\$542.55	\$157.38	\$220.64	\$10.09	\$0.00	\$930.66
	MEL-SYD	\$274.34	\$39.19	\$247.13	\$11.31	\$291.05	\$863.02
	SYD-HBA	\$454.37	\$474.58	\$384.98	\$17.61	\$0.00	\$1,331.54
	SYD-LST	\$454.37	\$524.18	\$333.24	\$15.24	\$0.00	\$1,327.03
BAe 146	MEL-HBT	\$313.01	\$326.93	\$174.54	\$7.98	\$0.00	\$822.46
	MEL-LST	\$313.01	\$361.10	\$125.75	\$5.75	\$0.00	\$805.61
	MEL-DPO	\$0.00	\$0.00	\$122.66	\$5.61	\$0.00	\$128.27
	MEL-WYN	\$0.00	\$0.00	\$114.41	\$5.23	\$0.00	\$119.64
	MEL-ADL	\$373.75	\$108.41	\$183.13	\$8.38	\$0.00	\$673.67
	MEL-SYD	\$188.98	\$27.00	\$205.12	\$9.38	\$198.33	\$628.81
	SYD-HBA	\$313.01	\$326.93	\$319.53	\$14.62	\$0.00	\$974.09
	SYD-LST	\$313.01	\$361.10	\$276.58	\$12.65	\$0.00	\$963.34

Regulation of Prices for Services Provided by Airports

The Commissions brief focuses on the issue of whether regulatory imposts are required to limit the ability of airport operators to abuse market power.

In the period following the completion of long term arrangements for the Phase II airports there was frequent comment on the real market value of leases entered into. Strong opinion was voiced in this state that the new leaseholders of the local airports had paid too high a premium for those leases. The related concern was therefore that operating charges where possible would be raised to offset the increased capital outlay. The CPI-X price cap applied to aeronautical charges has effectively limited the ability of airport operators to do so.

Until recent times the users of airports services has also been limited to the two existing majors and their regional subsidiaries – a captive client group with limited scope for destination substitution.

In essence in the Tasmanian experience the evidence of market power has existed with both lumpy investments and limited price/ demand elasticity. But there is limited (if any) evidence available in the Tasmanian experience to suggest that such market power, if it really exists, has led to situations where airport charges have been levied to yield excess profits. The dilemma in this state is that the relatively low yield of carriers places airport leaseholders in the difficult position of balancing the needs for carriers to keep costs low against their own need for revenues – getting the equation wrong carries the implied threat of service reduction and thereby lost airport revenues. In other words the airlines possess significant market power themselves in response.

The arrival of a new carrier in Hobart has done little to change the situation for the local airport – the balance between charging an equitable fee for services provided still needs to be balanced by the need to attract new carriers, understanding the implied risk to other operators reducing services. This is the classic monopsonist situation where both buyers and sellers both command substantial market power.

The effect of competition is difficult to evaluate in the present small market situation – caution prevails for airport operators. It is conceivable however, that if forecast market growth occurs on Tasmanian services as a consequence of the arrival of one or more discount carriers, a new imperative may exist for the airport leaseholders in the light of increasing airline revenues and demand for airport services. That could only occur where the relative power of a single airline diminished through competition from its direct competitors.

Current pricing regimes at the airport relating to services which are under the control of the airport are at a level where it is argued that the airport is operating efficiently – understanding there is a lack of a benchmark for many of the services provided by the airport.

If price capping were removed it is unlikely that market power imperatives would see charges increase for airport users unlike the potential on the major trunk routes where volumes and therefore demand for services is substantially higher. In the case of the uncapped airports in Tasmania it could be argued that no market power opportunity exists due to the opportunity for destination substitution – regardless of this there is again no evidence of behaviour which is any different in essence from those airports where price capping exists.

Both major airports in Tasmania have been active in seeking additional users for airport facilities including new airlines – the Hobart Airport in particular has been innovative in developing a range of alternate uses for large tracts of land which are included in the leasehold with the development of services complimentary to the Airport or which provide further users for aeronautical services (freight). Price capping and implied market power has in no way influenced the intent of the leaseholders to grow their revenue base.

Conclusion

The evidence from the Tasmanian situation would seem to imply that market power has not brought with it any obvious abuses in terms of pricing and/ or inefficient behaviours. In the Tasmanian environment it would seem that continuation of the regulatory regime beyond the present sunset period would not seem warranted.