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Price Regulation of Airport Services Inquiry
Productivity Commission
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Review of Price Regulation of Airport Services

Airport pricing is an issue of considerable interest to the tourism industry. As such, the Department of Industry, Tourism and Resources welcomes the Productivity Commission's review of the Price Regulation of Airport Services.

Importance of Airports to Tourism

Travellers to and from Australia are heavily reliant on efficient airports and competitive air services. Over 99 per cent of the 5.5 million short term visitors to Australia during 2005 entered through airports. This is significantly different to most other nations that often have land or ferry links to significant markets. Domestic tourism is also heavily reliant on airports and according to Tourism Research Australia, 21 per cent of Australian residents who undertook an overnight trip during 2005 used airlines as their main mode of transport. This has increased considerably from the comparative figure of 17 per cent in 2000 due to the significant growth of low cost carriers during that period.

Airports are also increasingly meeting traveller demand for a range of complementary services such as shopping and entertainment. Airports and the services provided at them create first and last impressions of Australia and therefore have an influence on Australia's image as a tourism destination. Indeed they form an integral part of the holiday experience. Similarly, the aviation industry is heavily reliant on tourism for demand.

Tourism Industry Interests in Airport Services

A critical issue for the tourism industry is whether airport infrastructure is adequate to cope with expected increases in tourism demand and aircraft operations. The Tourism Forecasting Committee predicts that inbound visitor arrivals will increase from 5.5 million in 2005 to 9.2 million in 2015, an annual average increase of 5.5 per cent. Over the same period outbound departures are forecast to increase from 4.8 million to 6.5 million and domestic visitor nights are forecast to increase from 276 million to 285 million.

Since privatisation, all price monitored airports have undertaken and/or planned significant investment in infrastructure to meet anticipated increases in demand. This will need to continue over coming years if airport infrastructure is not to impede growth in traveller numbers. Airport privatisation has also increased the commercial focus of airport operations. Airports are now required to cater to increasing traveller demands for expanded services such as entertainment and shopping, and airports are also diversifying their role through on-site non-aeronautical commercial developments.

It is important that pricing of airport services allows investment in new and improved infrastructure. To this end, it is important that airports receive a fair return on their capital and are able to fund the infrastructure developments which the airlines and the travelling public expect.

Alternatively, concerns have been raised by some tourism industry stakeholders that the past five years have seen significant increases in airport prices that are not necessarily justified. From a tourism industry perspective, it is consequently important that pricing of airport services achieves a balance between providing protection against potential abuses of market power and allowing airports to make commercially driven decisions.

Airport Market Power

In its 2002 report, *Price Regulation of Airport Services*, the Productivity Commission concluded that Sydney, Melbourne, Brisbane and Perth airports have significant market power in core aeronautical services. The report also concluded that Adelaide and Canberra airports, and to a lesser extent Darwin airport, have a moderate degree of market power.

The Department of Industry, Tourism and Resources believes that while these findings remain valid, there have been some changes in the market since the 2002 review was concluded.

The most relevant change in terms of passengers has been the introduction of Jetstar services from Avalon airport, which provides some competition for Melbourne airport in terms of price sensitive domestic travellers to and from that region. Melbourne airport still enjoys a significant advantage in terms of location and facilities for less price sensitive travellers.

Limited destination substitution

Information regarding international travellers by point of arrival and other destinations visited is provided at **Attachment A**. While this information does not elaborate on the potential for destination or mode of transport substitution in response to increases in prices, it supports the view that, for many passengers, demand for air services is still strongly linked with a particular destination. As identified in the 2002 report, this is particularly true of international travellers and domestic business travellers. A significant proportion of other categories also travel to visit one specific destination.

As also identified in the 2002 report, depending on the traveller type there can be considerable differences in the opportunities for destination or mode of transport substitution. For example, almost all international visitors must arrive by air whereas a significant proportion of domestic visitors travel by car.

Lack of competition from other forms of transport

For interstate and international travellers intending to visit one destination, there are potentially significant cost differences arising from both the actual cost from using an alternative airport or mode of travel as well as convenience costs. Given the relatively small proportion of airport charges relative to the total cost of air travel, it is likely that there remains considerable market freedom for airports to charge above marginal costs without affecting demand from a significant proportion of travellers.

The Department therefore believes that there remains a case for some form of regulatory oversight of airport charges, though the form of that oversight will naturally be dependent on the findings of the current review.

Price increases since 2002 and the impact on travellers

The ACCC report, *Price monitoring and financial reporting - price-monitored airports*, shows that prices have continued to increase in 2004-05 although to a lesser extent than those increases experienced over 2000-01 to 2002-03.

Since price monitoring was introduced, revenue from aeronautical services at the price monitored airports has increased substantially. The report also shows that total aeronautical airport costs have increased between 2002-03 and 2004-05 for all airports, with greater security requirements adding to airport costs. At the same time, increased passenger numbers have seen airport costs on a per passenger basis remain relatively constant and, combined with price rises, airport profitability has risen substantially over the period.

In determining whether these price increases are justified, it is worth noting that these price rises have occurred in an aviation environment in which airlines are seeking to reduce costs. The impact of September 11, SARS and avian flu, and high oil prices have forced airlines to seek efficiencies through a range of measures, including technological efficiencies, reducing overheads, workforce change, etc.

These developments would imply that, excluding oil prices, the cost of airport prices relative to other air travel inputs has increased over recent years, and airport prices will consequently have a greater impact on the eventual price paid by travellers. This effect will be particularly pronounced for lower cost airline products, such as low cost domestic services and discount international tickets.

These developments underline the need to ensure that airport prices are set at a level which encourages efficiency, while also providing a reasonable rate of return for investors and encouraging appropriate investment.

Concluding Remarks

The price of airport services has an important bearing on the cost of travel, which directly influences the competitiveness of Australia as a tourism destination. On the domestic front, a much larger number of tourists now travel by air due to the lower airfares on offer. Domestic air travel is somewhat more sensitive to airport prices, due to the fact that airport charges represent a much higher proportion of the total cost of air travel for domestic airfares.

The view of this Department is that the continuation of some form of regulatory oversight appears to be appropriate for the foreseeable future.

Yours sincerely



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Tourism Research Australia

International Visitor Survey

Visitors ('000)

City of arrival by Tourism Regions Visited, 2005

All Visitors	SYD	MEL	BNE	PER	ADL	DRW
Stayed a night in region of arrival airport	1,987 90%	789 88%	483 53%	436 96%	63 94%	30 85%
Stayed a night in other region in Australia	1,080 49%	504 56%	734 80%	194 43%	31 47%	25 69%
Stayed a night in other state in Australia	933 42%	410 45%	306 33%	109 24%	27 40%	23 64%
Holiday	SYD	MEL	BNE	PER	ADL	DRW
Stayed a night in region of arrival airport	1,040 94%	343 90%	247 44%	221 97%	24 94%	18 84%
Stayed a night in other region in Australia	655 59%	250 66%	500 89%	110 49%	17 65%	19 87%
Stayed a night in other state in Australia	597 54%	218 57%	207 37%	65 29%	16 62%	18 83%
VFR	SYD	MEL	BNE	PER	ADL	DRW
Stayed a night in region of arrival airport	375 83%	181 81%	122 63%	110 95%	19 94%	4 84%
Stayed a night in other region in Australia	199 44%	121 54%	127 66%	47 40%	8 39%	2 54%
Stayed a night in other state in Australia	145 32%	84 38%	47 24%	24 20%	6 31%	2 46%
Business	SYD	MEL	BNE	PER	ADL	DRW
Stayed a night in region of arrival airport	362 91%	166 89%	64 70%	55 93%	8 94%	3 81%
Stayed a night in other region in Australia	128 32%	82 44%	60 66%	21 35%	4 45%	1 33%
Stayed a night in other state in Australia	113 28%	68 37%	30 33%	12 20%	3 33%	1 25%