



Australian Government

**Department of Infrastructure
and Regional Development**

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Welcome

Thank you Peter Harbison and the Centre for Aviation

The election of the Coalition Government last year has confirmed a number of Australia's policy settings.

The Coalition Government's vision for aviation in Australia is to foster aviation industry growth in an environment that is safe, competitive and productive. The Government's goal for aviation also acknowledges the importance of international aviation to our tourism industry, international trade and our broader economy.

To increase global aviation industry liberalisation the Government has confirmed it will prioritise key bilateral air services agreements to ensure we will continue to have the capacity to meet future demand. We will also protect our national interest, and strongly support sustainable industries and facilitate the expansion of the Australian industry and Australian airlines into foreign markets.

In an industry where each stakeholder often has mutually exclusive interests, it is a challenge for the Government to please everyone all of the time; which is why we try and balance the diverging views to achieve an outcome that will benefit the industry as a whole.

Regulation and Infrastructure

One of our fundamental Government objectives in support of aviation industry growth is ensuring that we have solid foundations in the form of the correct regulatory settings and appropriate infrastructure to accommodate growth.

It is important that the regulatory environment provides the right balance between ensuring compliance with relevant standards, whilst not over-burdening industry with onerous compliance regimes that impede business competitiveness and growth.

You will have no doubt seen the release by the Deputy Prime Minister of the Aviation Safety Regulation Review Report that was conducted by a panel of leading independent aviation experts headed by Mr David Forsyth. The Review commissioned by the Deputy Prime Minister confirmed Australia had an advanced aviation regulatory system, but it also identified opportunities for a range of improvements to ensure Australia remains a leading aviation state.

The Government is currently carefully considering its response to the Report's recommendations and other matters arising out of the Report.

The Government has also undertaken steps towards levelling the aviation playing field by passing legislation to remove intermediate restrictions on foreign ownership that apply to Qantas but to no other Australian international airline. The legislation removes the 35 per cent limit on ownership by foreign airlines and the 25 per cent limit on ownership by a foreign individual.

By removing these restrictions, foreign investors will be allowed to acquire the same level of ownership in Qantas as they can in other Australian international airlines regulated by the *Air Navigation Act*.

This is progress toward the Government's stated goal of harmonising the regulatory framework applying to all Australian international airlines.

In April this year, the Government confirmed that the site for Western Sydney's new airport will be Badgerys Creek, after more than 50 years of discussion about potential sites. This decision will provide an avenue for economic growth for Western Sydney and a much needed long-term capacity for the Sydney region, ensuring New South Wales does not miss out on expected growth and economic benefit due to airport congestion.

International Growth

It is no secret that our industry has enjoyed considerable growth in recent years, and that being ready for future growth is a key challenge for the future.

Since 1992, when we began to liberalise, international passenger movements into and out of Australia have more than trebled. International aircraft movements have also trebled.

In 1992, 41 international airlines flew to Australia. Today there are 54.

The mix of those airlines has changed – the rise of Asian hubs in the 1990s and Middle Eastern hubs since 2000 have caused a fundamental shift in the orientation of our industry, and an increase in global connectivity.

Growth from Middle Eastern airlines has been substantial over the past 10 years, with services trebling in just a decade.

Growth from Asia has seen the number of Asian-based airlines serving Australia increase from 14 in 1992 to 23 today.

But this growth does have side-effects. In 1992 there were eight European airlines flying to Australia – today there is only one. While it can be sad to see airlines leave our market, overall our global connectivity has increased and is now unprecedented.

The growth in the Chinese market has been a constant theme of industry discussions in recent years. The growth has been enormous: In 1992, one direct flight a week served a market of around 85,000 passengers per year. Today, 75 direct flights a week serve a market of more than 2.4 million passengers every year. And growth in the China market is predicted to continue, at around 10 per cent each year.

However the story of growth in our market is not a simple story of continued and unbroken growth. In recent months we have seen a number of airlines, particularly from Asia, slow or step back from, their previous ambitious growth plans. In some cases, we've seen airlines reduce capacity, either by operating

smaller aircraft, or reducing the number of flights they operate. This is not a cause for panic and hand-wringing. This is the market at work, and evidence that our market-driven aviation market policies are working. Liberalisation is not about guaranteeing more flights per se – liberalisation is about letting market forces operate, and letting airlines respond to supply and demand. It means both an ability to compete and to withdraw services also. The key objective is to facilitate *sustainable growth*.

Market sustainability

In order to ensure the ongoing viability of the Australian aviation industry, it is essential that all players – airlines, airports and the tourism industry - have the opportunity to make a profit. Nothing in the world is free – and someone has to pay for everything, including airline services and airport infrastructure.

The international aviation market is highly competitive and even sometimes irrational. With the recent introduction of multiple low-cost carriers serving nearby Asian markets, we have seen long-haul international airfares being offered at prices comparable to short-haul domestic airfares.

Very low airfares may be desirable for airports and the tourism industry with their ability to stimulate the market, but in the long term they damage the profitability of airlines, and the aviation industry as a whole. Extended periods of discounting and loss-making will not only impact airlines, it will also flow through to airports and the tourism industry in the longer term with airlines eventually rationalising unsustainable routes.

Sometimes, our industry is its own worst enemy, holding the belief that if they continue loss-making activities in pursuit of market share that they will eventually begin to turn a profit. Australia, with our relative economic strength in recent years, has seen international airline capacity growing in recent years well in excess of growth in passenger numbers.

In the last year, the number of international seats operated by airlines into and out of Australia grew by eight per cent. But passenger movements only rose by six per cent. You don't need to be an expert in airline economics to see that this does not look like a recipe for increasing profitability.

Indeed, the average international airline load factor for Australian services is around 75 per cent – that's a lot of empty seats coming and going from Australia every day.

In the last 12 months, Malaysian carriers have increased their capacity to Australia by around 40 per cent, but growth in passengers in the Australia – Malaysia market was only 16 per cent.

This can also be seen in both the Singapore and Indonesia markets – with modest growth in passenger numbers outstripped by airlines increasing services at a much higher rate.

Some players in the industry hold the view that anything other than constant growth means our policy settings aren't working. I disagree. The Australian

Government has set very ambitious targets for the tourism sector under its Tourism 2020 Strategy, and facilitating growth in aviation capacity is one very important aspect of that. However, it is only one aspect – and everyone involved in the tourism and aviation sectors need to remember that investment in our tourism product, and getting the right incentives for that investment, is just as important as growth in aviation capacity in delivering the goals of Tourism 2020. Growth in aviation services for its own sake is unsustainable and will not deliver those long-term goals. Growth in aviation, in step with increased capacity across the rest of the economy, is what is needed.

Bilateral System

In discussing market outlooks, it is often easy to blame any perceived impediment on the bilateral system, but there is also much that is misunderstood in the industry about the bilateral system, how it works, and what it achieves.

The bilateral system is an enabling framework: it makes it possible for airlines to operate international services. Although it is not perfect, it is here to stay for the foreseeable future. And it is important to remember that the bilateral system has delivered an effective and reliable regulatory system since the close of the Second World War and the creation of ICAO.

Australia is working through ICAO to advance the concept of multilateralism – indeed officers from my Department are leading the work of a working group developing a new multilateral aviation framework. While we will do our best to

support and develop possible solutions, it will take time, and many previous attempts have been unsuccessful.

For the Australian Government, it is not our intention that the bilateral system serve as a constraining framework, although some other countries do not share our view. Over the years, we have developed into a very liberal market, one of the most liberal in the world. Around 50 per cent of all travellers coming to Australia do so under an open skies or open capacity agreement. But open skies or open capacity agreements are not ends – they are means, aimed at delivering airlines the commercial flexibility to make their own decisions about their services. In Australia, we have largely delivered this market-driven objective, without collecting open skies trophies.

For many commentators in Australia, and some industry players, urging the Australian Government to do more to liberalise the international aviation market is a standard refrain. But unfortunately it is based on a presumption that every other government is trying to push forward on liberalising the international industry. The reality, evidenced at the last ICAO Worldwide Air Transport Conference, is that the international trend is away from liberalised, open markets. In Europe and in North America, governments are working to wind back past liberalising measures by imposing new regulation aimed at so-called ‘fair competition’, or new regulation to control consumer service standards. Against this emerging anti-competitive, pro-protectionism sentiment, Australia’s market-driven approach to liberalisation remains one of the most open in the world.

In Australia, there is a lot of unused capacity, and significant scope for growth within existing airline services. The broad-based approach we have taken to liberalisation has resulted in sufficient sixth-freedom capacity and flexibility to continue to facilitate overall market growth if a choke-point develops in one particular market.

The reality is that there are currently very few markets into or out of Australia where bilateral agreements are constraining services. There are a couple of cases, including Hong Kong, where foreign airlines are not currently able to increase services to Australia's major gateways – but we are aware of these and are working to remedy them, in consultation with those foreign governments.

This brings me to one of the most important aspects of the bilateral system: it is based on negotiation. We are not able to force bilateral partners to come to the negotiating table, nor are we able to force a particular outcome in a negotiation. Outcomes of negotiations represent a negotiated outcome, and we can only attain what the other party is willing to accept.

In my experience, Australian stakeholders' perceptions of what is required in our aviation market sometimes differ from what our bilateral partners consider necessary. There are many different approaches to aviation liberalisation amongst our bilateral partners, and we are unable to force them to accept our policy approach all of the time, even on key issues such as the concept of 'capacity to meet future demand.'

China is a good example of this. The Chinese market has been growing strongly in recent years, and continued growth in future years will be important in achieving the goals of the Government's Tourism 2020 strategy. Tourism and airport stakeholders argue strongly, and have argued for some time, that Chinese carriers need increased capacity entitlements so they can increase services to Australia. We agree – that's why we have a standing commitment with China to continue to work towards the end objective of an open skies agreement.

However, while my Department has sought numerous times over recent years to schedule talks, Chinese authorities have yet to accept our long-standing proposal to hold a new round of talks.

The reality is that no matter how much Australian stakeholders would like us to hold renewed talks with China, unless Chinese authorities also want to hold talks, talks won't happen.

Looking at the capacity available and the current utilisation, you can see why expanding the air services arrangements for the Australian market does not have the same level of priority for the Chinese.

There were just over 2 million seats available in the Australia – China market over the past year, with around 75 per cent load factor – that equates to almost half a million empty seats over the year.

Capacity available under the current bilateral arrangements to the major Australian gateways is over 22,000 seats per week, with Chinese carriers today using around 16,000 seats. In other words, there's enough capacity available for Chinese carriers to increase services by thirty per cent tomorrow, if they choose to do so.

The Chinese market is particularly seasonal with increased numbers of travellers over holiday periods such as Chinese New Year. That's why our current arrangements provide scope for Chinese carriers to operate additional seasonal services over periods of peak demand such as Chinese New Year.

As you can see there is no need for panic just yet; the current air services arrangements still contain sufficient growth potential for both Australian and Chinese airlines for the short term. Like many of our air services arrangements, there is also unlimited capacity to points other than the major Australian gateways, providing unlimited future growth opportunities to places such as Cairns, Gold Coast, Darwin and Adelaide.

In an ideal world, we would like these arrangements, and all of our arrangements, to provide growth potential for the longer term, so airlines have certainty to plan for future growth. However, as I noted earlier, we are entering a dangerous period, with protectionism creeping into some places around the world. In a government-to-government negotiation we cannot force foreign governments to adopt our policy approach. If they want to provide a short-term framework, and return to the negotiating table every couple of years, we cannot force them to accept a longer-term approach.

Conclusion

Looking to the future, it is important that we have the right policy approach to regulation and infrastructure that will ensure we can accommodate and capitalise on the predicted growth in the aviation industry, but also in the tourism, airport and trade industries.

I appreciate and share tourism and airport concerns about constrained markets; the Australian Government works to address this, and provide airlines with a market-driven framework to provide for future growth. But we cannot do it unilaterally in a system governed by negotiation. At the end of the day, the bilateral system is an enabling system that will let airlines do whatever they want to do, if they are genuinely serious about wanting to do it.

Finally, as we look to the future, it will become increasingly important that all industry participants focus on profitability throughout the value chain in order to guarantee the long-term ongoing viability of Australian airlines, airports and tourism businesses. Future growth must occur in a sensible and sustainable manner.

Thank you.