

**SUBMISSION ON APPLICATION TO THE MINISTER OF TRANSPORT  
PURSUANT TO PART 9 OF THE CIVIL AVIATION ACT 1990 FOR  
AUTHORISATION OF THE AIR NEW ZEALAND AND AIR CHINA STRATEGIC  
ALLIANCE**

**31 August 2020**

**Introduction**

- 1 Christchurch International Airport Limited (*CIAL*) welcomes the opportunity to submit to the Ministry of Transport (*MOT*) on the application by Air New Zealand Limited (*Air NZ*) and Air China Limited (*Air China*) (together, the *Airlines*) for authorisation under section 88 of the Civil Aviation Act 1990 (*CAA*) of their Strategic Alliance Agreement (*SAA*) and related agreements, (the *Alliance*), for a five year term. This follows an authorisation of the SAA by the Minister of Transport on 1 September 2015 (*2015 Authorisation*)
- 2 *CIAL* submitted on the SAA on 1 May 2015 (*2015 Submission*), this submission should be read in conjunction with the 2015 Submission. As with the 2015 Submission, *CIAL*'s submission is based on our review of the Airlines' redacted application for authorisation to the *MOT*. A number of key aspects of that application remain confidential, including data in support of the Airlines' claimed public benefits. Our submission should be read in that context.

**Key points**

- 3 *CIAL* recommends the *MOT* undertake a rigorous analysis of whether the current authorisation is in the wider New Zealand public interest, having regard to:
  - 3.1 actual and demonstrable evidence as to the likelihood that the public benefits claimed by the Airlines will actually be delivered by the Alliance and that those benefits will provide a material public benefit;
  - 3.2 other options the Airlines might have to structure their relationship and whether the benefits claimed might be achieved without the need for Ministerial intervention in competitive markets;
  - 3.3 whether an otherwise anti-competitive alliance is necessary to deliver the claimed benefits;
  - 3.4 the impact of the Alliance on regional economic development as a public benefit (and interest);
  - 3.5 whether the claimed benefits outweigh the potential detriments associated with the Alliance;
  - 3.6 the New Zealand International Air Transport Policy, in particular the reestablishment of routes promoted over Christchurch to the South Island; and
  - 3.7 the impact of COVID19.
- 4 The South Island's tourism and freight industries are of both national and regional economic significance and depend on frequent, direct international air services, especially with Asian hubs to provide crucial connectivity to key Asian and other

international markets. This will be even more pronounced following the outbreak of COVID 19. Before granting a further authorisation, the MOT should be comfortable that the Alliance, whether in isolation or in conjunction with other alliances, will not have the practical effect of foreclosing the potential for such international air services to the South Island, including the return of direct air services to the South Island established prior to the outbreak of COVID 19.

- 5 If the MOT is minded to authorise the application, we recommend authorisation for the shortest period the MOT determines is necessary to allow the claimed public benefits to be more clearly evidenced in a COVID 19 environment and to ensure those benefits are distributed within New Zealand to give the best economic outcomes.

**Public benefits**

- 6 The Alliance partners point to the period since the 2015 Authorisation and claim the public benefits of the Alliance as being:

- 6.1 creation of a new direct Auckland – Beijing service and securing the sustainability of existing Auckland – Shanghai service;

- 6.2 opportunities for New Zealand suppliers;

- 6.3 premium customer handling, lounge and FFP benefits;

- 6.4 lower average fares;

- 6.5 greater connectivity;

- 6.6 competition with other carriers;

- 6.7 stimulation of tourism; and

- 6.8 continuing competition in the cargo market

- 7 CIAL supports the rebuild of Chinese demand for airline connectivity to and from New Zealand however the public version of the application for authorisation produces very little, if any:

- 7.1 insight into the necessity for a departure from the expectation of a competitive aviation market;

- 7.2 evidence to demonstrate the actual value of the claimed benefits to the New Zealand public generally. For example, it is not entirely clear from the application how helping “Air NZ maintain its competitiveness with other Chinese carriers” is, or translates to, a public benefit; or

- 7.3 evidence to demonstrate whether the claimed benefits are able to be otherwise achieved for, or by, the New Zealand public without the authorisation of an otherwise anti-competitive alliance.

- 8 The application in essence seeks to renew an existing alliance and provides limited insight into the need for this specific arrangement for a further five year period in a fundamentally changed environment. Simply expressing a belief that potential

concerns did not eventuate from the 2015 Authorisation is not sufficient in what is a *de novo* application. It does not, for example, provide any insight into the Alliance strategy over the period for which the authorisation is sought other than noting, despite the obvious material change in the operating and economic environment, the commercial rationale for the Alliance has not materially changed since the 2015 Authorisation. No other alternatives appear to have been considered.

- 9 For the reasons set out below CIAL requests the MOT conduct a rigorous examination of any claimed benefits for the period of the term sought.

***Regional Economic Benefits to the South Island unlikely***

- 10 The South Island economy depends on effective international connectivity with key international markets, like Asia, to sustain its tourism and export air freight industries.
- 11 MBIE's official tourism statistics indicate regions within the South Island derive a greater benefit from direct international connectivity than via indirect connectivity over other New Zealand ports. There is no reason to consider this will be any different following the outbreak of COVID 19, if anything this has now been brought into sharper focus.
- 12 In the absence of a direct Alliance service to Christchurch the public benefits claimed the Alliance will continue to be limited as:
- 12.1 there will be fewer, if any, direct benefits to South Island exporters;
- 12.2 the stimulation of South Island tourism will be limited to sub optimal outcomes and ultimately opportunities will be diluted;
- 12.3 due to the diluted distribution of benefits that arise when Auckland is the port of entry, the public benefits for the South Island will be significantly less than claimed; and
- 12.4 opportunities for talent attraction and export education will be diminished.

***Limited benefit to South Island exporters***

- 13 As set out in CIAL's 2015 Submission, direct services between CHC-China are crucial to the South Island's air freight reliant industries, as importers and exporters in the region depend on the belly hold freight in commercial services (wide body especially) to reach international markets efficiently and cost effectively.
- 14 As the Alliance does not propose to add a CHC – China sector it will have little, if any, noticeable positive impact on SI exporter's currently decreasing ability to efficiently access important Chinese and Asian markets. Notwithstanding the general assertion of competition in the cargo market and that shippers will continue to have better routing options, the public version of the application contains no evidence as to how South Island exporters will derive benefits from the Alliance greater than those they already enjoy. Any better routing options will be limited to those shippers whose primary route to market is Auckland to Beijing. Against that is the potential detriment of an alliance impacting on the reestablishment or enhancement of direct wide body services to the South Island.

***Limited stimulation of South Island tourism***

- 15 The South Island's tourism industry is of national importance. Growing direct volumes of visitors to and from North Asia markets is critical for growing regional South Island economies. CIAL supports initiatives which will lead not only to an actual increase in tourism numbers to New Zealand but importantly also a greater regional distribution of the economic and social benefits.
- 16 The assertion the Alliance has ensured benefits of the growth in Chinese tourism numbers have been distributed throughout the regions via Air New Zealand's domestic network applies only a passenger numbers lens. It remains the case that economic benefits of getting Chinese and North Asian visitors direct to the region are significant. For example:
- 16.1 in the most significant source market, China, surveys show that Chinese visitors to the South Island stay considerably longer in New Zealand than those who didn't visit the South Island, spent more money, and were overall more satisfied with their trip to New Zealand; and
- 16.2 approximately 70% of international arrivals to CHC will go on to visit other regions in the South Island. Only 7% of international visitors arriving in Queenstown will venture outside the region to other parts of the South Island.
- 17 South Island regional economies are best stimulated with direct international air connections. Direct travellers tend to stay longer and spend more and where the South Island has established direct services, it has been demonstrated these routes grow ahead of national growth rates.
- 18 The MOT should conduct a detailed analysis to be satisfied the Alliance (potentially together with other alliances and code sharing agreements) does not practically contribute to the reduction in opportunity for future direct air international services to destinations other than AKL, including the return of China Southern and other carriers established prior to the outbreak of COVID 19.

***Limited distribution of benefits where Auckland is the single port of entry***

- 19 The application seeks authorisation for an Alliance with two points of entry in China but a single point of entry to NZ. The NZ port of entry for direct long-haul routes is the key factor in determining which regions in New Zealand capture the benefits of connecting with these markets.
- 20 The 2015 Submission showed how the South Island suffers a significant dilution in opportunity value per visitor when the international entry point is not in the South Island. This means while there may be national benefits arising from an increase in the number of travellers originating from Beijing to New Zealand the regional distribution of those benefits through New Zealand will be significantly impacted by the port on entry. The MOT should consider not just whether passenger numbers have grown or whether distribution of those passengers has increased but rather the counterfactual of whether that increase would have occurred in that manner in the absence of an anti-competitive alliance.
- 21 We also observe that unlike other recent applications for authorisation which have directly resulted in the increases of direct air capacity to CHC, there is no evidence the Alliance has delivered any meaningful additional direct flights outside of AKL over its term.

### ***Impact on competing carriers***

- 22 It is unlikely an alliance operating with the benefit of an anti-competitive authorisation will be incentivised to deliver the claimed competitive benefit. The Alliance claims, presumably as justification for a further authorisation, that it has fulfilled its stated objectives without any detrimental impact on competition yet produces little or no evidence as what steps the Alliance put in place or will continue to put in place to ensure this occurs.
- 23 Two key features of the market (as shaped by the Alliance and the cumulative effects of other Air NZ alliances) make it difficult for competing carriers to offer alternative long-haul services to other New Zealand locations from North Asian destinations.
- 24 First, Air NZ has traditionally controlled most of the international long-haul capacity through AKL (both independently and by way of its various alliances) reinforcing AKL's fortress position as Air NZ's primary hub. This makes it difficult for an independent carrier to establish viable services that service AKL and materially more difficult to service ports in New Zealand outside Auckland.
- 25 The Alliance rely on the existence of the direct China Southern CAN-CHC service as evidence of an apparent lack of disincentives to competition on routes between China and NZ during the period of the 2015 Authorisation. The Alliance fails to acknowledge the efforts required to attract new services or that the presence of immunised anticompetitive arrangements is a disincentive to entry. No consideration appears to have been given, as it would be expected to have been, to the counterfactual of whether the absence of a level playing field has resulted in either constrained growth or as a contributing factor in the departure of carriers. Market entry and then a rapid exit or retrenchment is not an indicator of a fully functioning aviation market.
- 26 It should be noted prior to the outbreak of COVID 19 the direct services of China Southern into both CHC and AKL have been able to grow without the benefit of an immunisation. This brings into question not only the necessity for an authorisation but also reinforces the need to ensure a level playing field for all carriers through this critical next period.
- 27 MOT should give serious consideration to the impact immunised alliances will have on a return to the New Zealand market, and more particularly the South Island, by competing carriers which offer alternative long haul services to and from North Asian destinations.

### ***Lower Fares unlikely***

- 28 With a likely reduction in the intensity of competition in the markets it is highly unlikely that the Alliance will cause fares to be lower if the Alliance is authorised.

### ***COVID 19***

- 29 The Alliance responsibly acknowledges the difficulty in predicting what the competitive landscape for air services will look like following COVID 19 including when normal services will be resumed. That highlights the need for the MOT to be cautious in accepting the assertions of the likelihood of benefits made in the application and the assumptions made of market behaviour where limited precedent exists.

- 30 The application forms part of the first tranche of applications following the onset of COVID-19. Against that backdrop the MOT should carry out a higher degree of analysis to understand whether the benefits claimed by authorisations and the policy settings required to drive the economic outcomes that NZ will need will in fact be delivered by this and other applications.
- 31 Getting policy settings and decisions right is of critical importance in the recovery, not only of air services, but also in how our regions participate in that recovery process. It would be reasonable to expect to see evidence of that thinking in any decision by the Minister.

***Civil Aviation Bill***

- 32 In the same vein, these are also the first applications that follow the MOT's publication of the Civil Aviation Bill (CAB) exposure draft. CIAL has expressed reservations about the alliance authorisation framework proposed by the MOT. There is value in the MOT reflecting on how it believes this application would be assessed within the proposed CAB framework.
- 33 Of particular interest would be who, if anyone, the Minister might consult with under the proposed CAB section 186(3) to assist the Minister to determine the public benefits in a post COVID-19 environment. Consideration should also be given to how the Minister would take in to account the main and additional purposes of this Act (CAB section 189(2)) in a post COVID-19 environment. It is difficult to see, for example, which of either the main purpose and additional purposes set out in sections 3 and 4 CAB would assist consideration by the Minister of the appropriateness of an authorisation in the current circumstances.

***Term of authorisation***

- 34 In the absence of an ability to impose conditions or review the Alliance, the MOT is essentially being asked to issue a new authorisation for a further five year term and then rely on further updates from the Alliance.
- 35 CIAL is highly supportive of the recovery of connectivity to one of NZ's key markets however in the face of uncertainty facing the aviation sector over coming years and limited forward looking statements regarding the operation of the Alliance, if the MOT is minded to authorise the Alliance we recommend the MOT only authorise the Alliance for the shortest period it determines necessary to allow the claimed public benefits to be more clearly evidenced and to ensure those benefits are distributed within New Zealand to give the best social and economic outcomes.