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DOMESTIC AVIATION 1981-1986

Frank PASCOE
Executive Director, Aviation
Ansett Transport Industries Ltd
Melbourne

ABSTRACT: *In May, 1981, the Commonwealth Government introduced a package of legislation designed to create a new environment for domestic civil aviation in Australia for the next five years.*

This legislation embraced a new Airlines Agreement, deregulation of air cargo and mail, changes to make T.A.A. a company freed of statutory constraints to function more commercially, and a new Committee to approve air fares.

The policy objective is to have T.A.A. and Ansett more competitive in the provision of efficient and economic air services over the trunk routes of Australia.

This paper looks at the situation after year one.

DOMESTIC AVIATION 1981-1986.

On July 3rd, 1977, the then Federal Minister for Transport, the Honorable P.J. Nixon, M.P., publicly announced that a review was to be undertaken of Australian domestic air transport policy having regard to, amongst other things, the fact that the Airlines Agreement Act of 1952-1972 provided that Ansett Transport Industries or the Commonwealth could terminate the Airlines Agreement by giving, at any time after 31 December, 1977, notice in writing of termination taking effect not less than five years after the giving of the notice; and the Airlines Agreements Act of 1973 was to expire in June, 1978.

The report on the desirable changes to policy, legislation and administration designed to improve air transport within Australia in so far as these related to domestic trunk route airline services and the two airline policy was completed in March, 1978.

Following Government consideration of the report, negotiations took place between the Commonwealth, the Australian National Airlines Commission and Ansett Transport Industries Ltd. on a new Airlines Agreement which was signed in its final form on May 28th, 1981.

The Government saw the principal benefits of the new two airline agreement as being:

removal of cargo from the ambit of the Agreement

new provisions which allow acquisition of large turbo jet aircraft by regional and cargo operators

recognition of the role of regional operators and provisions that foster competitive and orderly development of the industry

new far less restrictive consultation arrangements which allow either of the major operators to take unilateral action on a wide variety of issues including introduction of promotional fares

removal of mail from the Agreement thus allowing Australia Post to negotiate with all airlines without constraint.

The Minister introduced into Parliament on 28th May, 1981, four pieces of legislation to give effect to the Government's new domestic aviation policy to apply during the period 1981-1986. These Acts were:

Airlines Agreement Act 1981 (1)
Airlines Equipment Amendment Act 1981 (2)
Independent Air Fares Committee Act 1981 (3)
Australian National Airlines Repeal Act 1981 (4)

The fourth recital to the 1981 Airlines Agreement emphasises the Government's intentions that its aviation policy should result in the achievement of national competitive, efficient and economic operation of air services within Australia.(1)

The 1981 Agreement "is directed towards maintaining the two airlines policy but with the objective of increasing the level of competition within the industry in a rational and orderly manner. The two airline policy has served Australia well. On the trunk routes we have benefited greatly from the existing Boeing 727 and DC9 jet operations. As indicated earlier we are now progressing into a new era of fleet development with the two major operators acquiring different equipment. Over the next few months T.A.A. will begin to introduce the wide-bodied Airbus, the first wide-body to be used in domestic service in Australia. At much the same time Ansett Airlines of Australia will start to introduce its new B737-200s as a replacement for its DC9s. The B737-200 has the advantage of having the same fuselage size as B727. Ansett, of course, plans to introduce B767 wide-bodied aircraft. Ansett will be one of the first to introduce this new generation aircraft".(5)

The requirement of providing national air services is met by T.A.A. and Ansett in operating what is now the clearly defined trunk route system. Provision is also made that should T.A.A. and Ansett decline to provide a satisfactory passenger service over a trunk route not currently operated by them other operators will be able to serve that route.

The effect of this has been the opening of new air services by T.A.A. and Ansett during the past 12 months as follows:

Adelaide-Brisbane-Adelaide
Perth-Brisbane-Perth
Canberra-Adelaide-Canberra
Canberra-Brisbane-Canberra

Competition in domestic Australian aviation is manifesting itself in many ways not previously possible when T.A.A. and Ansett operated similar fleets. Different equipment has provided a basis for differences in scheduling and in service both on the ground and in the air.

Even at this early stage it can be said that the thrust of the legislative changes to make the industry more competitive has been successful.

In respect of the efficiency and economic performance of the Australian domestic industry all four parts of the legislative package come into play.

Firstly, under the Airlines Equipment Act 1958-1981(2) the Minister determines how much passenger aircraft capacity that is necessary to economically carry half of the estimated passenger traffic during a specified future period.

To arrive at an estimate of passenger traffic task the Minister may be assisted by the advice of the Secretary of the Department of Aviation who may consult with the industry on matters relevant to Ministerial estimates and determinations.

To determine the maximum aircraft capacity of the aircraft required by T.A.A. and Ansett, the Minister takes into account:

(a) rates of traffic increase

(b) the types, speeds and reasonable extent of utilization of the aircraft proposed to be used

(c) the revenue load factor that would be the optimum passenger revenue load factor for the operation of aircraft on each route during the period concerned, due consideration being given to the interests of the public and the maintenance of a proper relation between revenue and costs

(d) the necessity for the overhaul and maintenance of aircraft

(e) the necessity for having aircraft available to meet emergency situations

(f) aircrew training requirements

(g) any services operated otherwise than by T.A.A. or Ansett on non-competitive routes, and

(h) any other factors affecting the stability of the domestic air transport industry

Clause 13 of the Airlines Equipment Act[2] requires compliance not to provide passenger tonne kilometres in excess of those determined for the specified period, to dispose of aircraft which the Minister considers in excess to economically meet the passenger traffic task, and finally not to acquire or obtain the use of aircraft without a certificate of approval from the Minister to the effect that the acquisition "will not be detrimental to the stability of the domestic air transport industry".

Thus, in terms of economic performance of the domestic aviation industry, the functioning of this Act should at all times ensure that the industry as a whole should remain economic and not subject to the "excess" capacity problems which plague many operators overseas.

Secondly, the 1981 Airlines Agreement[1] provides for consultation to take place between T.A.A. and Ansett in three areas of importance to the economic and efficient operation of domestic air services within Australia.

(a) The 'may consult' group where the airlines can discuss issues relating to the efficiency and economic operation of air services and may reach agreement, but are not obliged to reach agreement;

(b) The 'must consult' group, restricted to only the most important issues such as aircraft utilisation and industry load factors. Any disagreement that either airline wishes to pursue may be referred directly to Sir Nigel Bowen, Chief Justice of the Federal Court, who has agreed to act as Arbitrator for the purposes of the Airlines Agreement Act 1981. The Secretary to the Department of Aviation and such other persons as Sir Nigel considers appropriate will provide information and advice to assist in the resolution of disputes.

(c) Fares, where all consultations must be in the presence of a member or representative of the Independent Air Fares Committee.

The airlines are obliged to consult on core fares and may also consult on discount fares but at the direction of the Independent Air Fares Committee. Each airline makes individual submissions on air fare variations and it is no longer necessary for them to reach agreement on the level of increases to be sought.

Thirdly, the Independent Air Fares Committee Act 1981[3] which established the Independent Air Fares Committee consisting of three part-time members, commenced functioning in November, 1981, and is responsible for the determination of air fares arising from major and minor reviews and for decisions on discount air fares covering all regular public transport (RPT) passenger air services on interstate and/or inter-territory routes and intrastate/intra-territory routes provided by incorporated bodies. The Committee also is required to undertake Cost Allocation Reviews at the request of the Minister for Aviation.

Fourthly, the Australian National Airlines Repeal Act 1981[4] was to make T.A.A. a more competitive and commercially oriented airline. The establishment of T.A.A. as a public company removed the obligations on it to consult with Government bodies in compliance with statutory responsibilities. As a public company T.A.A. would be able to participate more fully in the competitive environment created by the new legislation.

The Government will hold all of the shares initially in the new T.A.A. company but has commissioned consultants, namely, Price Waterhouse-Management-Consulting-Accounting, Potter Partners-Underwriting, Blake & Riggall-Legal, to examine the practicalities of selling the shares in T.A.A. including how this might be done in the light of the domestic air transport policy including the new 1981 Airlines Agreement. The consultant's report is expected in late November, 1982.

The Government also decided at the time of the passing of the new Airlines Agreement Act[6] to establish an inquiry into the advantages and disadvantages of deregulating the domestic aviation environment. This inquiry will take into account the developments of the different fleets of the two major operators including the introduction of wide-bodied aircraft. The inquiry's report is to be available for consideration and decision by the Government before the completion of the 5 year term of the 1981 Agreement.

Against the background of the aims of the new Two Airline Policy it is appropriate that views be advanced as to how all this is working out in practice after a year's experience on the road of a 5 year journey.

The object of the policy is to maintain firstly threshold control of capacity into the country which should, in broad terms, obviate a long term problem of over capacity applying in Australia thus avoiding one of the major problems which plagues aviation overseas. This threshold control is maintained by the procedures provided in the Airlines Equipment Act; and with depressed passenger markets with us and in prospect in the immediate future the disposal of equipment replaced by new aircraft is of real economic importance.

The Minister makes determinations of passenger aircraft capacity that may be offered by T.A.A. and Ansett to economically carry half of the estimated passenger traffic during a specified period. These determinations are arrived at by taking the actual traffic carried during the determination period of the year immediately prior, increasing this traffic expressed in millions of passenger kilometres by a traffic variation or growth factor to arrive at the estimated traffic for the determination period. This then is grossed by a passenger revenue load factor to arrive at the capacity required to economically perform the estimated passenger task. This capacity is then apportioned on a 50/50 basis on competitive routes between T.A.A. and Ansett.

Determinations of passenger capacity are also made for non-competitive routes on a similar basis.

The operators will have no problem, in my view, in observing the requirement not to provide capacity passenger tonne kilometres in excess of that determined; however, with a down-turn in traffic there could be a situation where Clause 13 (b)[2] of the Act may have to come into play. This reads as follows:-

> "(b) where, at any time during a period in relation to which the Minister has made a determination under the last preceding section, the Minister -
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> (i) notifies the Commission or Ansett Transport Industries Limited that he is satisfied that the aircraft owned, operated, or otherwise available for use, by the Commission or the Company, as the case may require, exceed the aircraft required to provide, in that period, the aircraft capacity determined in relation to the Commission or the Company, as the case may be and

(ii) directs the disposal of aircraft to a specified extent (being the extent which the Minister considers necessary to eliminate the excess),

an obligation to comply with the direction within the time specified by the Minister."

The Airlines Agreement Act 1981 Clause 7 (iv)[1] provides that there shall be consultations between the Commission and the Company with a view to reaching agreement in respect of passenger revenue load factors, aircraft utilisation and other matters approved by the Minister.

Consultations have taken place between T.A.A. and Ansett on the need for improved passenger revenue load factors to off-set the economic problems resulting from the continued decline in passenger traffic volumes in Australia during the current year 1982. Consultations have resulted in improved economic performance of the trunk route system and, to date, these have not resulted in disagreement of sufficient importance to warrant a reference by T.A.A. or Ansett to the Arbitrator, Sir Nigel Bowen.

Consultations between T.A.A. and Ansett relating to fares have been held in the presence of a representative of the Independent Air Fares Committee. The setting of core fares and variations of these are matters on which the operators must consult.

On January 18th, 1982, the Minister for Transport requested the Independent Air Fares Committee to undertake cost allocation reviews in respect of the air services provided by Ansett and T.A.A. and this was reported to the Minister for Aviation, The Hon. Wal Fife, M.P., on August 13th, 1982.

The Committee during its review received 54 submissions and conducted formal public and private hearings in all State/Territory capitals and used the services of three consultants on particular aspects of the study which under the Independent Air Fares Committee Act[3] had to have regard for:-

(a) the need to ensure that air fares charged by a passenger operator in respect of air services provided by that passenger operator over 2 or more routes having similar characteristics, being air services in the provision of which similar aircraft are used, are able to be determined by the Committee in accordance with this Act on a consistent basis;

(b) the need to ensure that the level of air fares is related as closely as practicable to the cost of providing the services for which those air fares are charged;

(c) the need to ensure that air services are operated on an efficient and economic basis;

(d) the effect of the level of air fares on the demand for the services for which those fares are charged; and

(e) the need to ensure that the air fares charged by trunk route operators in respect of air services provided over trunk routes are able to be determined in accordance with this Act on a consistent basis.

The Act requires the Committee to identify all costs incurred by the airlines in providing RPT passenger services, including the provision of profit, and then attribute (allocate) those costs/profits between the flag-fall and distance components. The allocations so determined by the Committee are subsequently used to set air fares in accordance with the Committee's determinations for major and minor air fares reviews.

The Committee is required also during Cost Allocation Reviews to determine a differential between first and economy class fares.

The quantum of airline RPT passenger service costs is a matter which the Committee considers during air fare reviews.

Thus far I see the Independent Air Fares Committee as performing well. The Cost Allocation Review just finalised did more than just establish the basis of fares to apply on and from July 1st, 1982, it established a good Committee and public understanding of the industry both as to its safety record and to its importance in maintaining a network of safe, economic and efficient air services across Australia - a country the size of the U.S.A. but only populated by 14 million people.

The Committee despite finding that the air fares charged in Australia as at May, 1982, compared favourably with those applicable in the U.S.A., still believes that a more competitive marketing approach and a greater emphasis on passenger costs are achievable.

The Committee pointed out that the maximum capacity of passenger aircraft required by T.A.A. and Ansett was a matter for the Minister for Aviation under the Airlines Equipment Act but that the cost of supplying regular public transport services is significantly affected by the level of capacity provided by T.A.A. and Ansett.

The Committee noted particularly that the use of discounts by the airlines to combat short term traffic downturns has created intense price competition on a wider and more substantial scale than ever before.

Ansett commissioned W.D. Scott & Co. Pty. Ltd., Management Consultants, to conduct a survey of passengers to advise on the economics of the Ansett July/August, 1982, Special Discount Fares.

The following information was obtained and conveyed to the Committee:

The July/August special discount fares carried conditions which attempted to limit dilution.

These fares were not well availed by the public.

Of those persons using the fares a considerable proportion were travelling for business purposes despite the conditions attaching thereto. The majority of persons were intending to travel in any event.

The number of persons in the community likely to be attracted by special discount fares is extremely limited and having travelled once a person is not likely to use these fares on a second occasion for some considerable time.

Based on revenue the survey would indicate the industry did no better than break even. When coupled with the direct costs associated with the fares the industry is in a worsened financial position as a result of these fares being approved.

The load factor improvement of 3.75% which was in our view required to offset the cost of these fares was not achieved.

The most recent survey result supports those obtained earlier by Ansett that special discounts of the type introduced thus far are highly dilutionary and have a detrimental result on the industry.

In respect of the Government's decision to establish an inquiry into he advantages and disadvantages of deregulating the domestic aviation ivironment, little yet has occurred. No terms of reference for the inquiry ve been publicised nor has any announcement been made as to who will conduct e inquiry.

It would be wrong to pre-empt the inquiry and what the findings might be, t the reasons for and the perceived benefits of deregulation must be similar r Australian administrators as they were for the Carter administration in he United States some 4 years ago.

In the United States of America the results of deregulation appear favourable for the majority of passengers, airlines, manufacturers, investors d taxpayers in general. The only short term beneficiaries have been a minority discretionary travellers. Basic air fares have doubled in three years, major rlines have posted enormous losses, orders for new aircraft have all but ased, and existing orders delayed or defaulted.

With freedom to enter markets and charge what they want under deregulation ere has been an irresistible temptation for airlines to expand their route stems. Once in the new markets carriers behave in a most predictable manner. e smallest, weakest carriers or the low cost new entrant will inevitably turn the fare weapon to try and gain market share. The larger, stronger and perhaps ss efficient carrier will inevitably match the new low fare to maintain market are with the inevitable letting of blood on all sides. The whole issue will timately be sorted out either by reregulation or by economic forces.

Reregulation will be difficult to achieve and the answer may have to come from the economic forces of route rationalisation and a reduction of competition. To achieve these economic results mergers or bankruptcies seem to be the only possibilities.

We already have the sad story of Braniff, and there are other airlines who could just as easily disappear with remaining operators mopping up the extra traffic with ease.

It is hoped that the inquiry finds against deregulation of the Australia domestic aviation system.

The present domestic aviation policy aims to create and maintain an environment in which T.A.A. and Ansett can provide over the trunk route system of Australia air services which are competitive, economic and efficient.

In respect of these important issues, it is my view that the policy is succeeding, although the outcome of the moves to make T.A.A. more commercial will have some effect on the policy for the future.

REFERENCES

1 Airlines Agreement Act 1981

2 Airlines Equipment Act 1958-1981

3 Independent Air Fares Committee Act 1981

4 Australian National Airlines Repeal Act 1981

5 Hansard P.2828 The Hon. R.J. Hunt, M.P., Airlines Agreement Bill 1981 - Second Reading Speech

6 Hansard P.2828 The Hon. R.J. Hunt, M.P., Airlines Agreement Bill 1981 - Second Reading Speech