

## Air New Zealand/Qantas Strategic Alliance: Tourism Implications

### Purpose

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This note provides you with additional information about potential Tourism consequences related to the Air New Zealand/Qantas strategic alliance application.

<b>Date:</b>	11 December 2002	<b>Priority:</b>	Medium
<b>Security Level:</b>	Confidential	<b>File Number:</b>	TSM/6/19/1/1/1/1

### Action Sought

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	Action Sought	Deadline
Minister of Tourism	For information	

### Contact for Telephone Discussions

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File: TSM/6/19/1/1/1/1

11 December 2002

Minister of Tourism

## **Air New Zealand/Qantas Strategic Alliance: Tourism Implications**

### **Executive Summary**

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The Strategic Alliance application between Air New Zealand and Qantas has now been lodged with the Commerce Commission. We have identified three areas where the application is expected to have consequences for tourism. These are:

- Forecast international visitor arrivals over the next five years and the anticipated airline capacity on key international routes. Tourism New Zealand analysis of the proposal indicates that the main issue is undersupply on the Tasman if there are no new entrants into that market.
- Potential Global Airline Alliance changes between Air New Zealand and Qantas. Any changes to the current arrangements are likely to have significant consequences for the flow of visitors to New Zealand.
- Dual destination marketing implications. Based on past experience there is likely to be little change in expenditure on dual destination marketing as a result of the proposed alliance. In addition, the current approach of Tourism New Zealand is to promote higher yield mono destination travellers to New Zealand.

The Commerce Commission is expected to fully canvas these issues in its consideration of the application. We anticipate that the Commission will seek information from the Ministry and Tourism New Zealand during its consideration of the application.

## Air New Zealand/Qantas Strategic Alliance: Tourism Implications

### Purpose of Report

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- 1 The report provides you with information on some of the key issues from a tourism perspective that result from the Air New Zealand/ Qantas strategic Alliance application to the Commerce Commission.

### Analysis

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- 2 We have identified 3 key areas where the application is expected to have consequences for the tourism sector. These are the forecast demand from visitors over the next 5 years and capacity provision, Global airline alliance issues and dual destination marketing. We expect these aspects to receive considerable scrutiny by the Commerce Commission in its consideration of the application. This note provides you with some preliminary information about the importance of these issues from a tourism perspective.

#### Forecast growth and capacity issues

- 3 As you are aware, the Tourism Research Council (TRC) forecasts are expecting international visitor arrivals to increase by 6% on average over the next five years. The TRC also expects visitor stays to lengthen slightly and driven by this increase in stay, international tourism expenditure is expected to grow at the faster rate of 9.3% per year. Tourism New Zealand has analysed the international forecasts on a route by route basis looking at the demand for additional air capacity that these forecasts imply. This work is part of the TNZ Airline Strategy that was recently presented to the Board.
- 4 Analysis of the QF/NZ Alliance proposal in terms of Year 3 Factual schedules indicates a proposed expansion in capacity versus current schedules that is expected to meet or exceed forecast tourism demand on long-haul routes. The Tasman schedules fall around 7% short of tourism demand requirements on these routes over the three year period. The net capacity result for each route would depend on how other air carriers enter or leave the market over this period; for example if United Airlines terminated USA - New Zealand services, the proposed capacity in the QF/NZ Factual proposal would fall short of the forecast market requirement
- 5 Without further development of capacity by competing airlines or new value based airlines on Tasman routes, the proposed QF/NZ Alliance scenario is expected to constrain tourism development from Australia, our largest and most seasonally attractive tourism market. Consequently from a tourism perspective it is necessary for additional capacity to enter the Tasman market to satisfy the expected tourism demand.

	<b>TNZ Air Capacity Forecast Requirements (All Airlines) Year 3</b>	<b>Current QF/NZ Capacity Share on Direct Services to New Zealand</b>	<b>QF/NZ Alliance Capacity Proposal vs Current Schedules <i>Factual Year 3</i></b>
<b>Tasman Routes</b>	<b>10.7%</b>	<b>87%</b>	<b>4.1%</b>
<b>Los Angeles</b>	<b>19.6%</b>	<b>73%</b>	<b>23.6%</b>
<b>Japan Routes</b>	<b>1.3%</b>	<b>100%</b>	<b>9.7%</b>
<b>Singapore</b>	<b>32.8%</b>	<b>26%</b>	<b>70.0%</b>
<b>Hong Kong</b>	<b>20.9%</b>	<b>37%</b>	<b>40.0%</b>
<b>Taipei</b>	<b>17.6%</b>	<b>50%</b>	<b>50.0%</b>
<i>Note :</i> <b>TNZ Forecasts based on Tourism Research Council forecast arrivals + NZ outbound travel forecasts</b>			

It is also noted that the QF/NZ Alliance proposal does not address the direct air service development potential from either South Korea or PRC, our fifth and sixth largest inbound tourism markets that currently exhibit the highest annual growth rates of all inbound tourism markets.

- 6 Some caution also needs to be exercised in some markets as the forecasts are reliant on bilateral rights being negotiated to accommodate the predicted changes in capacity.

### Global Airline Alliances

- 7 At present New Zealand is in a very advantageous position with both Star Alliance and Oneworld members serving New Zealand. Star Alliance currently enjoys 22% global market share and Oneworld 18% global market share.
- 8 Air New Zealand's membership of Star results in the following benefits:
- Access to a feeder network from 11 other Star partners, being the broadest reach airline alliance.
  - A wider range of fares available to the travelling public to and from New Zealand
  - Access to the frequent flyer programmes of Star partners. In particular Lufthansa's "Miles and More" programme and United's "Mileage Plus" programmes generate a significant number of high yielding visitors to New Zealand.
  - Seamless distribution and interline access to 23 domestic destinations and 11 trans-tasman routes for the inbound passengers of Thai, Singapore and United.
- 9 Air New Zealand and Qantas give their respective alliances a strong presence in New Zealand. If Air New Zealand were to join Oneworld, the Star Alliance contribution to bringing passengers to New Zealand would be significantly reduced in our top five tourism markets (Australia, the United Kingdom, the USA, Japan and Korea) with consequent implications for code-share services, marketing and frequent flyer access. Star would also lose its presence in the

important outbound market of Fiji. If both airlines were to join Star, Oneworld would be all but eliminated in terms of New Zealand's top five tourism markets (the remaining Cathay Pacific plays only a small role in carrying residents from the USA, UK, Japan and Korea). The demise of Ansett and the Star Alliance connection into Australia has been seen as one of the reasons for the poor performance of Australian tourism over the last 12 months

10 Air New Zealand and Qantas becoming members of the same alliance will also have implications in the domestic market, where Air New Zealand and Qantas provide interconnect services for other carriers in their respective alliances beyond the gateway cities. It may become more difficult for carriers from the rival alliance to offer services to visitors who wish to travel beyond Auckland

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### Dual Destination Marketing

12 The proposed QF/NZ alliance is unlikely to materially change the way New Zealand is marketed internationally as both Air New Zealand and Qantas, to a lesser extent, have regularly invested with both Tourism New Zealand and the Australian Tourism Commission in mono and dual destination marketing campaigns

13 In the context of the Qantas overall marketing budget of \$A 200 million per annum, Qantas has historically been a weak investor in destination marketing of New Zealand. It has placed an average of \$NZ 1.6 million per annum in direct marketing and contra support in activities with Tourism New Zealand over the past two years. Over the same period Air New Zealand invested more than \$ 9.1 million per annum in destination marketing projects. Qantas historically has placed a greater emphasis on marketing its airline "brand" rather than the destinations it flies to, and has tended to only invest in destination focused tourism campaigns when it sees a tactical (commercial) need to do so during periods of seasonal weakness in demand.

14 A concern for Tourism New Zealand is that as contraction in the supply of international air capacity is being openly mooted in the future QF/NZ Alliance network, less marketing funding from QF/NZ would flow to destination marketing due to supply side shortage in inbound air seats.

15 Tourism New Zealand's current international marketing approach gives lower priority to promotion of dual destination holidays as such promotion diminishes the opportunity to market to higher yielding mono (New Zealand) destination visitors. Mono destination visitors are more attractive for New Zealand as they stay longer, leave economic value in more regions and spend more in absolute terms. Mono destination visitors now exceed 70 % of New Zealand's inbound

arrivals and this style of travel is increasing in popularity. But a QF/NZ alliance would provide for a broader range of Australia/New Zealand itinerary options for global travellers than the status quo.

## **Risks**

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### **Other**

- 16 There is a lot of uncertainty about the forecasts that have been used in the airline analysis and these will be tested in the Commerce Commission evaluation of the application. The Commission constructs its own counterfactual as part of the evaluation process and therefore counterfactual contained in the application may not be the same as that used by the Commerce Commission. The evaluation of the net public benefits undertaken by the Commission through its process will be a rigorous evaluation of what is likely to happen without the alliance proceeding as well as an assessment of each of the benefits and detriments claimed in the application.
- 17 We anticipate that tourism will figure prominently in the consideration of the application and the Ministry and Tourism New Zealand will be called upon as sources of information to assist the Commission in its process.

## **Recommended Action**

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This report is for noting.

Ray Salter  
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Ministry of Tourism