PUBLIC VERSION

REVIEW OF AUCKLAND AIRPORT'S 2022-2027 PRICE SETTING EVENT

CROSS SUBMISSION ON CONSULTATION PAPER

10 October 2024

INTRODUCTION

1. This is the New Zealand Airports Association's ("**NZ Airports**") cross-submission in response to the submissions to the Commerce Commission's ("**Commission**") consultation paper that was released as part of the review of Auckland International Airport Limited's ("**Auckland Airport**") 2022 – 2027 Price Setting Event ("**Consultation Paper**").

2. As with our previous submission on the Consultation Paper ("**Submission**"), NZ Airports has focused its comments on regulatory framework issues raised by other submissions. Auckland Airport will separately submit on the detailed aspects of its price setting event.

3. The NZ Airports contact for this submission is:

Billie Moore
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[redacted]

EXECUTIVE SUMMARY

4. Airline submissions attempt to portray an airport that is ignoring regulatory settings, which are therefore considered to be ineffectual. They argue that Auckland Airport's capital programme is too large, and the target returns are too high. They therefore seek regulatory change.

5. NZ Airports acknowledges that airlines are fully entitled to provide their views on airport performance. They have valuable insights as substantial customers. However, when it is clear that their submissions are heavily coloured by an overarching strategy to seek regulatory change, it is difficult to identify whether airlines have identified valid performance concerns or are simply aiming to make Auckland Airport, and the regulatory regime, look as bad as possible.

6. NZ Airports remains strong in its view that the information disclosure ("**ID**") regime is effective. It means that, in complex operating environments, airports and their customers are given space to engage on airport-specific approaches to investment and pricing that will promote the long-term benefit of consumers. However, it is natural that airlines and airports will not agree on some fundamental aspects of performance, for example:

   (a) airlines will seek the lowest possible WACC to reduce short-term landing charges, while airports will seek a WACC that sufficiently covers their risks of long-term investments and promotes innovation; and

   (b) airlines have incentives to reduce investment in capacity and to lower short-term costs, while airports need to ensure major investment is durable and will meet the needs of all existing and future customers and the broader New Zealand economy.

7. Resolving these differences is where the regulatory settings are particularly important. The input methodologies ("**IMs**") and other regulatory guidance provided by the Commission (including through pricing reviews) point airports (and airlines) in the right direction to achieve the Part 4 purpose of the Commerce Act 1986 ("**Act**"). Unfortunately, due to the timing of Auckland Airport's PSE4 decisions, the appropriate application of the WACC IM was uncertain, which is illustrated by the multiple scenarios analysis in the Consultation Paper. The

Commission's draft finding was that Auckland Airport was targeting excess returns. It did not find (and could not find) that Auckland Airport was *deliberately or knowingly* targeting excess returns. Auckland Airport believed it was applying the IMs in an appropriate manner. If the Commission confirms its draft view that Auckland Airport was mistaken in its approach, then Auckland Airport has indicated that it will respond. This shows the regime working effectively with the threat of further intervention effectively constraining airport decision making.

8. The Commission's other major draft finding was that Auckland Airport's investment plan was appropriate. NZ Airports endorses that finding, which if finalised, takes much of the impetus out of the airline calls for regulatory change.

9. NZ Airports continues to hold the view that while PSE reviews are core to effective regulation due to the valuable guidance provided by the Commission, they are not the appropriate forum for considering whether the right form of regulation is in place. We acknowledge that PSE reviews can identify where ID requirements could be improved. For example, airlines have raised concerns about whether sufficient information is disclosed about projected pricing and demand impacts for subsequent pricing periods. NZ Airports would be open to exploring such potential changes under an appropriate consultation process to consider amendments to the ID requirements, but for the reasons discussed in this submission has doubts whether such forecast information will prove to be useful for interested persons.

SCOPE AND PURPOSE OF REVIEW

This is not the forum for submissions on regulatory change

10. The Commission is required to provide a summary and analysis of the regulated airports' pricing disclosures for the purpose of promoting greater understanding of the performance of individual regulated suppliers, their relative performance, and changes in performance over time.[1] Pricing disclosure reviews are not processes to consider regulatory change.[2] While the Commission is permitted to include analysis of how effective ID is in promoting the Part 4 purpose in the context of considering whether the performance of a regulated entity is consistent with the Part 4 purpose, that does not invite submissions advocating for regime change.

11. Throughout this review, the airlines themselves have recognised that a pricing review is not the forum to determine what the appropriate form of airport regulation is. For example, Airlines for Australia and New Zealand ("**A4ANZ**") submitted that:[3]

> While A4ANZ acknowledges that reforms to the regulatory settings in New Zealand are not part of this review….

12. Similarly, the Board of Airline Representations New Zealand ("**BARNZ**") and the International Air Transport Association ("**IATA**") acknowledged, in their response to the Commission's issues paper for this review of Auckland Airport's PSE4 ("**Issues Paper**"), that considerations of the appropriate form of airport regulation do not fall within the scope of the review (emphasis added):

> BARNZ submits that the Information Disclosure regime is no longer an appropriate form of regulation to be applied to AIAL. **While the Review of AIAL's**

[1] Commerce Act 1986, s 53B(2)(b).

[2] For example, NZ Airports *Submission on Commerce Commission Process and Issues Paper for its review of Auckland Airport's 2022 – 2027 price setting event* (31 January 2024) at paragraphs [16]-[17].

[3] A4ANZ *Submission on Commerce Commission Consultation Paper for its review of Auckland Airports 2022 – 2027 price setting event* (3 September 2024) at page 4.

> **Pricing Decision as will be undertaken is not designed to answer this question**….[4]
>
> Although **not within the scope of this review by the Commission**, it has become increasingly evident that the current Information Disclosure (ID) regime is no longer fit for purpose or appropriate.[5]

13. Despite this awareness, airlines continue to use the review process primarily to pursue their broader agenda of regulatory change.

14. For example, A4ANZ discussed Australia's airports and corresponding regulatory regime as a comparator to Auckland Airport, indicating that the Commission should look at the repeated calls for reform of airport regulation expressed by the Australian Competition and Consumer Commission ("**ACCC**").[6]

15. A4ANZ did not note that the Australian Productivity Commission ("**APC**") reviews the regulatory framework for airports in Australia, having done so four times since the privatisation of Australia's airports in 1994.[7] As part of its review, the APC considers the need for changes to the regulatory framework.

16. Following the APC's most recent report, Commissioner Paul Lindwall rebutted the ACCC's view that light-handed regime was not working well, stating:[8]

> I would characterise the ACCC's view as the mere possession of market power being a sufficient reason for additional regulation. But that neglects the cost of regulation – direct and indirect – and the impact that it can have on investment and competition. […]
>
> Overall, it is hard to see how a negotiate-arbitrate regime would be in the interests of the flying public. To the contrary, it could lead to higher fares, less competition between airlines and restricted services. […]

17. Commissioner Lindwall's findings reflect the complexities involved in airport regulation and the risks of regulatory costs and unintended outcomes. It is for this reason that the Act separately provides for an inquiry into the form of regulation, if required. The various submissions on regime change in this forum demonstrate that airlines are consistent in their unwillingness to constructively engage with the PSE review process.

Airlines' submissions are coloured by their calls for regulatory change

18. The clear strategy to create noise around a call for regulatory change colours all the airline submissions. Airlines appear to be attempting to paint Auckland Airport in the worst possible light in an effort to achieve their broader objective. Viewed from this perspective, several of the points raised by airlines are not helpful to this review.

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[4] BARNZ *Submission on Commerce Commission Process and Issues Paper for its review of Auckland Airport's 2022 – 2027 price setting event* (31 January 2024) at paragraph [5].

[5] IATA *Submission on Commerce Commission Process and Issues Paper for its review of Auckland Airport's 2022 – 2027 price setting event* (31 January 2024) at page 5.

[6] A4ANZ *Submission on Commerce Commission Consultation Paper for its review of Auckland Airports 2022 – 2027 price setting event* (3 September 2024) at page 2.

[7] In 2002, 2007, 2012, and 2019.

[8] Productivity Commissioner Paul Lindwall's speech Economic Regulation of Airports at the Australian Airports Association National Conference (16 November 2022) at page 11-13. See https://www.pc.gov.au/media-speeches/speeches/airport-regulation/airport-regulation.pdf.

19. For example, BARNZ's submission implies that the use of confidentiality agreements has subverted Auckland Airport's consultation process and / or inhibited the disclosure of information to the Commission.[9] This is not true.

20. NZ Airports is aware that confidentiality agreements have been standard practice for pricing consultations since prior to the introduction of the ID regime and allow Auckland Airport to provide more detailed information during the consultation process than would otherwise be possible (particularly due to confidentiality concerns arising from Auckland Airport's status as a publicly listed company with continuous disclosure obligations). Nor have confidentiality agreements prohibited the flow of information to the public (via pricing disclosures) or to the Commission.

21. It is telling that no party has raised objections to the use of confidentiality agreements in the previous three price setting reviews. It is not clear why they are considered to be a problem now. The only logical explanation is that they are being used as a further mechanism to seek to portray Auckland Airport in an unfavourable light.

22. Similarly, airline submissions relating to Auckland Airport gaming the regulatory system should be considered in the context of airlines being focused on their regulatory change agenda. We note, for example, that BARNZ refers to Auckland Airport using a "self-selected" estimation date for setting the WACC.[10] This phrasing disregards the fact that BARNZ agreed to the 1 July 2022 date as part of the PSE4 consultation process (recognised by the Commission in the Consultation Paper) but changed its mind afterwards.[11] BARNZ also submits that "there is no other regulated company which is permitted to over-charge its customers so excessively and for so long",[12] which is a prominent example of its disregard for the effectiveness of regulation under the Commission's stewardship.

23. Qantas refers to Auckland Airport seeking to "cherry pick" inputs across regulatory IM periods.[13] Auckland Airport has explained in detail that it sought to apply the WACC IM in a consistent manner in accordance with accepted practice.

24. Air New Zealand raised an issue with Auckland Airport's allocation of corporate costs. Despite not raising this issue at a point where Auckland Airport could have constructively addressed it, Air New Zealand suggest this is evidence of failure of the ID regime (emphasis added):[14]

> **While we acknowledge that we did not raise this concern with AIAL during PSE4 consultation**, our resources and focus in PSE4 consultation were primarily focused on the size, adequacy and efficiency of the capital plan – that does not change the fact that it represents a material level of excess revenue. We also consider this to be one of many examples where the ID regime doesn't strike the right balance in incentivising the desired behaviour from AIAL; airports will look at multiple means to increase revenues until this is challenged by consumers, and this challenge is dependent on the resources and capabilities of consumers to identify and evidence this. This is not consistent with outcomes in a workably competitive market.

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[9] BARNZ *Submission on Commerce Commission Consultation Paper for its review of Auckland Airports 2022 – 2027 price setting event* (3 September 2024) at page 2.

[10] BARNZ *Submission on Commerce Commission Consultation Paper for its review of Auckland Airports 2022 – 2027 price setting event* (3 September 2024) at page 4.

[11] Consultation Paper, at [X20] and [2.28].

[12] BARNZ Submission on Commerce Commission Consultation Paper for its review of Auckland Airports 2022 – 2027 price setting event (3 September 2024) at page 3.

[13] Qantas Group *Submission on review of AIAL's 2022-2027 price setting event* (3 September 2024) at [4.2].

[14] Air New Zealand *Submission on Commerce Commission Consultation Paper for its review of Auckland Airports 2022 – 2027 price setting event* (3 September 2024) at [2.39].

25. Should airlines have views regarding specific airport pricing approaches, we would encourage them to raise these during the consultation process, or subsequently, directly with the relevant airport. It is unhelpful to introduce new points for the first time during a PSE review as this does not provide airports with an opportunity to engage meaningfully on the subject through the consultation process.

No new evidence in submissions

26. Airlines' opposition to Auckland Airport's capital programme and WACC has been known for some time. While their opposition might be more strongly expressed in their most recent submissions, NZ Airports has not identified new reasons or evidence for their positions.

Capex has been examined extensively already

27. Several submissions continue to make note of Auckland Airport's capex decisions, alleging in particular that the cost of the capex remains too large.[15] The Commission has already considered the airlines claims in depth.[16]

28. The Commission's careful deliberation included consideration of the alternatives put forward by airlines. In particular, in the submissions and cross-submissions on the Issues Paper, Air New Zealand and Qantas voiced their concerns regarding Auckland Airport's capex.[17] In doing so, Air New Zealand asked the Commission to consider its alternative domestic terminal design by their consultant, Arup. Qantas' submission on the Consultation Paper supported the Arup alternative.[18] After analysis of the forecasts and submissions from both airlines and Auckland Airport, the Commission's draft conclusion was that Auckland Airport's forecast capex appears to be reasonable.

29. Accordingly, the submissions on the Consultation Paper do not raise any new information that require the Commission to revisit its draft analysis or conclusions. As submitted previously, we support the manner in which the Commission has conducted its assessment of capex and urge the Commission to stay the course on its draft capex conclusions.

Auckland Airport appropriately formulated WACC

30. Auckland Airport appropriately formulated a WACC using the information available at the time of the PSE4. As the Commission recognised in its Consultation Paper, the context of PSE4 required some flexibility in the application of the IM framework.[19] Instead of using the 2016 IM as a rigid benchmark, the Commission used an adjusted 2016 IM benchmark and the 2023 IM to formulate the WACC in each its scenarios. Proposing this approach is implicit (and express)[20] acceptance that Auckland Airport's use of updated data when setting the pricing WACC under the 2016 IMs was a reasonable approach in difficult circumstances. It was

[15] BARNZ *Submission on Commerce Commission Consultation Paper for its review of Auckland Airports 2022 – 2027 price setting event* (3 September 2024) at pages 6-7; Air New Zealand *Submission on Commerce Commission Consultation Paper for its review of Auckland Airports 2022 – 2027 price setting event* (3 September 2024) at [2.73].

[16] Commerce Commissions *Review of Auckland Airport's 2022 – 2027 Price Setting Event Consultation Paper* (17 July 2024) at [4.55] – [4.72].

[17] Air New Zealand *Submission on Commerce Commission Process and Issues Paper for its review of Auckland Airport's 2022 – 2027 price setting event* (31 January 2024) at page 2, pages 13 – 14; Qantas Group *Submission on Commerce Commission Process and Issues Paper for its review of Auckland Airport's 2022 – 2027 price setting event* (31 January 2024) at page 1.

[18] Qantas Group *Submission on Commerce Commission Consultation Paper for its review of Auckland Airports 2022 – 2027 price setting event* (3 September 2024) at [2.2.2].

[19] Commerce Commissions *Review of Auckland Airport's 2022 – 2027 Price Setting Event Consultation Paper* (17 July 2024) for example at [2.46] and [2.71].

[20] For example, "We therefore accept that Auckland Airport had legitimate reasons for departing from using the 2016 IMs for their calculation of the equity beta", Commerce Commissions *Review of Auckland Airport's 2022 – 2027 Price Setting Event Consultation Paper* (17 July 2024) at [2.46].

certainly not a case of it deliberately trying to increase excess profits as alleged in some submissions.

31. The Commission has now clarified its position after the fact. That is, it is only after Auckland Airport set prices that it has become clear that the Commission has different views on how the pandemic should impact estimation of WACC. If Auckland Airport responds with pricing adjustments in those circumstances, then that is a clear indication of the strength of threat of regulatory intervention and the regime working – not regulatory failure as alleged by the airlines. Auckland Airport cannot be penalised for not complying with rules that did not exist at the time it set its prices.

32. Submissions suggesting that Auckland Airport did not engage on WACC during the consultation process are unjustified. Asserting that Auckland Airport, despite consultation, "remained committed to parameters set to target an excess profit"[21] is an unjust characterisation of Auckland Airport's approach. It appears to NZ Airports that airlines are not seeking meaningful engagement on WACC – instead, they simply want airports to apply the IMs in force at the time of the price setting event without adjustment or engagement. NZ Airports has submitted in the past that a challenge with the WACC IM is that it reduces engagement on WACC by substantial customers because airlines repeat the mantra that the IM should be applied in pricing.[22]

Tilted annuity approach to depreciation should be clarified

33. Consistent with the established IM guidance, Auckland Airport used straight line depreciation for its PSE4 price setting. Auckland Airport consulted on alternative depreciation methods with airlines however, in line with feedback received, did not adopt them.[23]

34. As NZ Airports has previously submitted, we do not consider it appropriate for any negative conclusions to be drawn on Auckland Airport's chosen method for depreciation for PSE4 when there was no clear guidance at the time that it set its prices.

35. The Commission's draft findings questioned whether a tilted annuity approach would be a better option to recover depreciation of long lived assets.[24] Air New Zealand, Qantas and BARNZ all subsequently agreed with this in their submissions.[25]

36. NZ Airports is not opposed to consideration of a tilted annuity approach to depreciation. However, its full complexities and potential implications need to be further considered if the Commission intends for it to have a more prominent role in the regulatory framework in the future. In particular, the airlines appear to support it on the basis that it will also involve long term price smoothing through a lower return on capital in early years. That is, what appears to be a relatively modest proposal by the Commission for an alternative depreciation profile to be considered, risks being converted into a heavy-handed price smoothing directive, which would not sit well under an ID regime.

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[21] BARNZ *Submission on Commerce Commission Consultation Paper for its review of Auckland Airports 2022 – 2027 price setting event* (3 September 2024) at page 2.

[22] See NZ Airports *Cross-submission on Process and Issues Paper* (21 February 2024) at [10(a)].

[23] Auckland Airport *Submission on Commerce Commission Consultation Paper for its review of Auckland Airports 2022 – 2027 price setting event* (3 September 2024) at page 48.

[24] Commerce Commissions *Review of Auckland Airport's 2022 – 2027 Price Setting Event Consultation Paper* (17 July 2024) at [3.54].

[25] BARNZ *Submission on Commerce Commission Consultation Paper for its review of Auckland Airports 2022 – 2027 price setting event* (3 September 2024) at page 4; Air New Zealand *Submission on Commerce Commission Consultation Paper for its review of Auckland Airports 2022 – 2027 price setting event* (3 September 2024) at [2.46]; Qantas Group *Submission on Commerce Commission Consultation Paper for its review of Auckland Airports 2022 – 2027 price setting event* (3 September 2024) at [4.4].

37. Should the Commission wish to further consider whether a particular approach to depreciation should be used in certain circumstances, then a separate consultation process should be followed to carefully consider how the concept can be appropriately incorporated into the ID regime without unintended consequences (assuming it is decided that the current ID requirements are not sufficient).

NZ Airports acknowledges there are cost pressures across the aviation sector

38. Local Government New Zealand ("**LGNZ**") submits that "ensuring people are able to travel around the country safely and affordably is crucial for maintaining thriving communities, and therefore of significant interest to local government".[26] NZ Airports completely agrees.

39. NZ Airports recognises that the aviation industry is under cost stress. Examples include recent announcements increasing the International Visitor Conservation and Tourism Levy (from $35 to $100), increasing visitor visa fees by 62%, increasing Civil Aviation and AvSec levies, and proposals for new charges on regional airports. All of these will impact the cost of travel for end consumers. We too are extremely concerned about these issues. However, advocating for lower prices through this review is an easy target. The outcome of this review cannot address all of the complicated cost pressures currently facing the aviation sector.

40. In various forums we have highlighted the importance of supporting the efficiency of the domestic network, of which Auckland Airport (and Wellington and Christchurch Airports) are key components. Any barriers to the viability and further development of regional routes (domestic or international) must be avoided.

41. LGNZ's concern that Auckland Airport's charges are a potential threat to affordable air travel highlights how Auckland Airport has become a scapegoat for the wider issue of upward pressure on the cost of airline travel.[27] There are many factors that determine the price consumers pay for a flight. This is reinforced by Oxford Economics Australia's price elasticity analysis provided to the Commission by BARNZ, Air New Zealand and Qantas, which highlights income, population growth and migration, competition and seasonal factors among factors influencing demand.[28] [[redacted]].[29] Airport charges are one, often small, component of prices to passengers. All of the other relevant factors make it very difficult to accurately forecast the impact of aeronautical charges on passenger demand and future aeronautical charges – especially beyond the current five-year pricing period.[30]

42. LGNZ's concern about potential adverse impacts of price increases on regional connectivity is not supported by the Oxford Economics results. The report's conclusions show [[redacted]].[31] The report finds [[redacted]

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[26] LGNZ *Submission on Commerce Commission Review of Price Setting Event 4 – Auckland Airport* (27 August 2024) at page 1.

[27] LGNZ *Submission on Commerce Commission Review of Price Setting Event 4 – Auckland Airport* (27 August 2024).

[28] Oxford Economics Australia, *Flight Price Elasticity Study: Domestic Markets* (21 May 2024), at page 6. A more detailed discussion of these factors is at section 2.2 beginning on page 13.

[29] Oxford Economics Australia, Flight Price Elasticity Study: Domestic Markets (21 May 2024), at page 18.

[30] We note that BARNZ has indicated that a lack of disclosure regarding 10 year demand and aeronautical price forecasts is a weakness of the ID regime. NZ Airports is open to consideration of relevant ID amendments via an appropriate consultation process. However, for the reasons discussed in this section, there will be challenges in providing useful forecasts, particularly in relation to the impact of prices on demand.

[31] Oxford Economics Australia, Flight Price Elasticity Study: Domestic Markets (21 May 2024), at page 7.

[redacted] highlighting the range of factors that can come into play when assessing the impact of cost increases.[32]

43. [redacted]

[redacted]

44. Skylark's review of Oxford Economics' analysis notes that income (in addition to price) elasticity impacts demand, and makes the important point that the way increased costs are distributed over all carriers is material, which is particularly relevant for Auckland Airport: [34]

> […] A further finding was that if all carriers on a route, or on multiple routes between markets experience a price increase, demand becomes less elastic due to the lack of substitutes.
>
> As a result, for a specific carrier on a given route, increasing fares will likely result in reduced demand, and vice versa. If this fare increase is implemented across all carriers on the route, the reduction in demand will be less. If all carriers on a wider number of routes increase fares by a similar proportion, the reduction in demand will be mitigated yet further. In summary, the wider the application of a price, the less elastic the demand response will be. This has obvious implications for Auckland, as the increase in charges affects all flights. […]

45. Of course, the above does not address the situation where a carrier has a monopoly on a domestic route, which is often the case for regional routes. In those circumstances, it can be expected that the unregulated carrier is already earning monopoly rents such that any (relatively small) cost increases due to aeronautical charges can (and should) be absorbed without changing prices, or prices can be increased without impacting demand.

46. The findings from Oxford Economics [[redacted]] provide reassurance that aeronautical charges are unlikely to be the cause of affordability problems on domestic network.

Demand modelling should focus on the system as it actually is

47. Oxford Economics' analysis is based on an assumption that the full cost of Auckland Airport's pricing would be applied to minimum airfares by airlines – it purposely does not look at the projected response to increases in average weighted fares. Oxford Economics takes this approach in order to identify passengers who would no longer fly at all because of price increases (i.e. they would be lost to the system), as opposed to passengers who might shift to lower cost airfare classes and still fly.[35]

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[32] Oxford Economics Australia, Flight Price Elasticity Study: Domestic Markets (21 May 2024), at page 28.
[33] Oxford Economics Australia, Flight Price Elasticity Study: Domestic Markets (21 May 2024), at page 28.
[34] Oxford Economics Australia, Flight Price Elasticity Study: Domestic Markets (21 May 2024), at page 35.
[35] Oxford Economics Australia, Flight Price Elasticity Study: Domestic Markets (21 May 2024), at page 20.

48. This approach neither represents the New Zealand context nor the real-life airline pricing model. The report itself highlights the lack of other transport modes in New Zealand which makes minimum airfare analysis less useful here.

49. Further, it would be very rare for airlines to load the full impact of any cost base increase into minimum fares. Analysis of average fares better reflects actual airline pricing behaviour. We agree with Skylark's reservations about the methodology:[36]

> While the methodological approach of deriving elasticities using changes in a single fare class may be logically consistent, typical airline pricing behaviour means increasing airport charges may not directly result in the expected loss of traffic. This is because airlines are aware that higher fare classes are relatively inelastic, and so they have a tendency to pass cost increases on to those classes in a disproportionate manner. Taken to the extreme – as a thought experiment – cost increases passed solely to the highest fare class are likely to result in higher cross-fare substitution and a lower level of aggregate traffic loss than if fares are increased uniformly across all fare classes. This will, of course, result in a reduction in average fare prices and lower airline margins.

50. We also note that, in practice, if Air New Zealand's minimum airfares prompt passengers to reconsider their flight purchase, many of those passengers would be picked up by Jetstar as the lower cost airline. This would be a perfectly acceptable market outcome. It is unclear how this has been taken into account in Oxford Economics' modelling in terms of demand impacts for Jetstar.

51. We do have some concerns, and sympathy for LGNZ's position that, in line with [redacted].[37] However, we reiterate that this outcome is a product of airline pricing models and (unregulated) market power, and not a result of increases in aeronautical charges that apply to all flights and routes equally.

52. The demand modelling also does not present an accurate counterfactual. Oxford Economics forecasts domestic demand growth of 5.5% over 8 years to FY32.[38] They admit that their elasticity estimates do not account for any suppression of demand from Auckland Airport's infrastructure investment being delayed or stopped.[39] With domestic jet gates currently full at Auckland Airport, the realisation of the baseline demand increase absolutely depends on the airport growing its capacity. Therefore, while there may be a demand impact from passing through price increases to airfares – the counterfactual is *not* higher growth, but demand suppression and congestion. Auckland Airport's charges are normalising from an extremely low base in order to address this. Reducing Auckland Airport's charges will not make domestic air travel more affordable. On the other hand, as a key domestic hub, investment in sufficient future capacity is critical for the entire network.

53. Overall, there is common ground that aeronautical price increases can have a negative impact on demand – if there is any impact. However, forecasting the likely impact on demand is extremely fraught and complicated. That is because many factors – not least airline pricing models and competition – will affect the real-world outcome.

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[36] Oxford Economics Australia, Flight Price Elasticity Study: Domestic Markets (21 May 2024), at page 37.
[37] Oxford Economics Australia, Flight Price Elasticity Study: Domestic Markets (21 May 2024), at page 43.
[38] Oxford Economics Australia, Flight Price Elasticity Study: Domestic Markets (21 May 2024), at page 29.
[39] Oxford Economics Australia, Flight Price Elasticity Study: Domestic Markets (21 May 2024), at page 6.

54. In that context, we encourage the Commission to assess the incentives of airports in relation to demand. There are absolutely no incentives in the system for airports to suppress demand. There is no scenario that exists where it would be rational for Auckland Airport to take actions that will reduce demand in the long-term. The Commission can therefore have confidence in the view that the airport has assessed potential demand impacts (including through its own disclosed studies) and has put forward a course of action focused on facilitating long term demand growth through infrastructure investment.

55. The Commission should also consider the market mechanisms that already exist for operators and consumers to respond to any cost increases that may be passed through in full or in part. Skylark's commentary highlights the fact that Auckland is competing for service provision with other airports domestically and across the Tasman, noting that, among other examples, fare differentials could motivate a passenger from Hamilton to fly via Wellington rather than taking a direct flight from Auckland.[40] All of the examples highlight how the market and network itself, and consumers, can naturally respond to any necessary cost increases. From an NZ Airports perspective, this is the healthy operation of competition in the market.

56. Despite airlines' ongoing concerns about price elasticity and costs in Auckland, Air New Zealand's network strategy of utilising Auckland Airport as a domestic hub is only intensifying. [[redacted]].[41] This week (2 October 2024), Air New Zealand made further announcements about reducing domestic flight capacity around the country – while *increasing* flights to and from Auckland.[42] This indicates that the costs Air New Zealand is concerned about are outweighed by the financial benefits of an Auckland hub model that requires passengers to arrive, depart or transfer at Auckland Airport.

[40] Oxford Economics Australia, Flight Price Elasticity Study: Domestic Markets (21 May 2024), at page 39.
[41] Analysis from OAG Traffic Analyser, January 2018-December 2023.
[42] "Air New Zealand slashes capacity on three domestic routes" Stuff.co.nz (2 October 2024) available here: https://www.stuff.co.nz/travel/350437348/air-new-zealand-slashes-capacity-3-domestic-routes.