



**MEMORANDUM TO  
THE COMMERCE COMMISSION**

**in response to  
the Air New Zealand/Qantas application for  
authorisation to enter into an alliance**

**14 August 2003**

## **Introduction**

1. This memorandum is provided by Virgin Blue in response to the Commission's invitation to interested parties to file memoranda prior to the conference. The Commission requested that the memoranda set out the following:
  - (a) an outline of further issues that have arisen since the cross-submissions that should be considered at the conference;
  - (b) a statement of the key differences between its views and those of other parties;
  - (c) an identification of those areas that ought to be pursued by the Commission by way of further examination.

## **New Issues**

2. Virgin Blue does not believe any new issues have arisen since the cross-submissions that require attention.

## **Key Differences**

### *Virgin Blue as an Effective Constraint*

3. There are a number of differences between Virgin Blue's position and those of the Applicants and the various opponents of the proposed Alliance. The difference that is of most significance relates to the ability of Virgin Blue to be an effective constraint on the Alliance, and thus significantly offset the competitive detriments that would otherwise arise.
4. In order to minimise the detriments of the proposed alliance the Applicants rely heavily on the ability for Virgin Blue to be an effective competitive constraint. In summary, Virgin Blue sees the Applicants' position as follows:
  - (a) the Applicants recognise that the Alliance will lessen competition between Air New Zealand and Qantas in the relevant markets;
  - (b) the Applicants implicitly recognise that without the entry of a new competitor, this lessening of competition would preclude the Alliance being authorised;
  - (c) the entry of Virgin Blue into the Trans-Tasman New Zealand domestic markets is the Applicants' answer. The Applicants have submitted that:
    - (i) the Alliance makes entry by Virgin Blue more likely and more successful;
    - (ii) there are no impediments to entry or expansion by Virgin Blue;
    - (iii) as a result, Virgin Blue will be an effective constraint on the Alliance.

5. Many of the other parties do not explicitly address the issue of Virgin Blue as an effective competitive constraint. A few of the opponents of the proposed Alliance mention Virgin Blue but do not consider that it can be an effective constraint (eg Bon Voyage, Origin Pacific, Gulliver's Travel). A few interested parties focus on the uncertainty of Virgin Blue's entry (eg Wellington Airport, Hospitality Association of New Zealand).
6. Virgin Blue considers that the positions taken by both the Applicants and many of the opponents of the Alliance are too extreme: they assume that either Virgin Blue will definitely be an effective competitive constraint (the Applicants) or that it definitely won't be (Origin Pacific, Gullivers Travel, among others). These positions are, in turn, based on inflexible assumptions that there are no barriers to entry (the Applicants) or that the barriers are insurmountable (various opponents).
7. Virgin Blue believes that the correct assessment of Virgin Blue's effectiveness as a constraint lies somewhere in between these two extremes:
  - (a) there are opportunities for a new entrant such as Virgin Blue;
  - (b) there are also significant barriers to entry (or constraints upon expansion once limited entry is achieved). The two principal barriers are access to facilities and the strategic response to the incumbent. Virgin Blue's position regarding these barriers is as stated in its submissions, in particular its submission of 21 July 2003. In particular, Virgin Blue maintains its position that capacity increases in response to new entry does amount to conduct designed to hinder or prevent the competitive process and cannot be described as a normal competitive response;
  - (c) the Commission must be satisfied that entry is not merely possible, but is likely, timely and of a sufficient extent. The existence of these barriers means that in the absence of conditions or undertakings, it is difficult for the Commission to be satisfied that Virgin Blue could be an effective, sustainable and sufficient competitive constraint on the Alliance; and
  - (d) however, the barriers to sufficient entry could be overcome by appropriate conditions or undertakings, thus enabling the Commission to be satisfied that Virgin Blue will be an effective competitive constraint on the Alliance.

### *Conditions*

8. The Alliance has offered certain conditions (although it claims such conditions are not really necessary). It claims these will facilitate new entry and thus reduce the competitive detriments associated with the Alliance and ensure delivery of other public benefits.
9. Most of the opponents who address the issue of conditions note that the Applicants' conditions are insufficient. Virgin Blue agrees with this as it believes that these conditions are too vague and contain too many exceptions to be either effective or workable. As a result the proposed conditions are unlikely to

adequately address the barriers that hinder Virgin Blue's sustainable and extensive entry.

- 10.** However, Virgin Blue does considers that appropriate conditions would facilitate such entry. Such conditions would include:
- (a) giving Virgin Blue a proportion of first rights of use of facilities at key airports (including peak hour use of terminals and desks); and
  - (b) capacity ceiling on relevant routes.

**Areas to be addressed by the Commission**

- 11.** Virgin Blue acknowledges that the Commission has a number of other issues it needs to consider including the counterfactual, market definition and assessment of the benefits of the Proposed Alliance. Virgin Blue does not wish to comment further on those issues (although will, of course, attempt to assist the Commission by answering any questions the Commission has).
- 12.** Virgin Blue believes the issues on which the application turn are outlined above – whether or not Virgin Blue will be an effective competitive constraint on the Alliance, and what conditions are necessary to ensure this occurs.

12 August 2003