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15/1.

12 January 2007

Mr Peter Baxter
First Assistant Secretary
North Asia Division
Department of Foreign Affairs and Trade
John McEwen Crescent
Barton ACT 0221

Peter
Dear Mr Baxter

Australia-Japan Free Trade Agreement

I refer to your letter of 20 December 2006 inviting Qantas to make a submission in relation to the Government's recently announced intention to conclude a Free Trade Agreement (FTA) with Japan.

As you may be aware, Qantas provided comments to the Department in connection with the earlier Australia-Japan FTA Feasibility Study. Our August 2005 submission (copy at Attachment 1) expressed the view that Australia's Air Services Agreement (ASA) with Japan provided an effective mechanism for growing air links, having evolved considerably over time, and (consistent with other FTAs negotiated by Australia) should continue to be developed separately from an FTA. At the same time, we indicated our support for advancing bilateral relations through the establishment of an FTA, noting that the further development of Australia's trade and economic relations with Japan could be expected to have a positive impact on the aviation sector.

While our advice is essentially unchanged, we take this opportunity to update you on developments that have taken place since our earlier submission.

Japan continues to be a market of major importance for the Qantas Group. Qantas now operates 47 services per week to four points in Japan, including seasonal flights to Sapporo. This increase reflects, in part, Qantas taking over services that had been operated by Australian Airlines until its retirement in July 2006, following which the Group has focussed flying on two main brands – Qantas and Jetstar. Jetstar, our value-based wholly owned subsidiary, will begin operating services to Osaka from March this year and to Nagoya from August.

Despite this level of activity, the profits that Qantas enjoyed on the Japan route in the 1990s have been eroded in recent years. The commercial performance of our operations has been impacted by a variety of

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considerations including the strength of the Australian dollar against the yen, a weaker Japanese economy, and shifting preferences of Japanese tourists towards short-haul destinations. The Qantas Group is working closely with Tourism Australia in an attempt to re-energise the market and attract Japanese tourists back to Australia.

In our previous submission, Qantas highlighted a particular aspect of the Australia-Japan ASA which constrains our Japan operations. Under a restrictive tariff article in the ASA, we are obliged to file fares and obtain concurrence for them from Japan Airlines, thereby impacting our competitiveness in the market.

Further background on this issue is contained in our response to the Department's request for input into Australia's 2006 submission on Japanese regulatory reform (copy at Attachment 2).

Although Qantas and Japan Airlines have recently reached in-principle agreement to provide each other with "standing concurrence" of fares, we continue to seek to have the existing tariff filing requirements (which apply in all Japan's ASAs with foreign countries) abolished or amended. However, we believe this issue can be resolved over time through the existing ASA mechanisms rather than the negotiating framework of an FTA.

We would be pleased to provide any further information that might be of assistance to the Task Force.

Yours sincerely



David Hawes
Group General Manager
Government and International Relations

26 August 2005

Japan Section
Department of Foreign Affairs and Trade
John McEwen Crescent
Barton ACT 0221

Dear Sir/Madam

Re: Australia-Japan FTA Feasibility Study

I refer to Dr Geoff Raby's letter of 8 July 2005, which invited Qantas to comment on issues relevant to the consideration of a Free Trade Agreement (FTA) between Australia and Japan, in particular interests we would wish to see pursued should negotiation of an FTA proceed.

Japan is an important market for the Qantas Group. We are the largest provider of air services between Australia and Japan, carrying predominantly Japanese tourist traffic and actively engaged in marketing Australia as a destination in Japan.

The bilateral aviation framework has provided effectively for the growth of air links over time. Although we believe this should continue to develop under these arrangements, Qantas supports conclusion of an FTA in view of the benefits it will bring to the Australia-Japan relationship more broadly.

Australia-Japan aviation market

Over 88% of Australia-Japan passengers are of Japanese origin, making Japan Australia's second largest source of visitors after New Zealand. Japanese visitors to Australia numbered more than 700,000 in the year to 31 May 2005.

Japanese visitor numbers in 2003-04 remained virtually unchanged from those recorded in 1993-94. This is partly due to the series of events that negatively impacted travel demand in Asia from the late 1990s, but also reflects the maturing of a market that experienced rapid growth in the late 1980s and early 1990s. Qantas is nonetheless encouraged by the 3.2% market growth in 2003-04, and believe that, absent unforeseen external shocks, modest growth will continue over the next three years.

The principal airlines serving the market are Qantas, our wholly owned subsidiary Australian Airlines and Japan Airlines, with a number of third party carriers, most notably Cathay Pacific and Singapore Airlines, offering services over their Asian hubs. In past years All Nippon, Ansett and Air New Zealand also operated direct Australia-Japan services, but all have withdrawn from the market.

Qantas and Japan

The Qantas Group has been directly engaged with the Japanese market for more than half a century, operating passenger air services to Japan continuously since 1949.

Qantas currently operates 31 services each week between Tokyo and Sydney, Melbourne, Perth and Cairns. Australian Airlines operates a further 21 weekly services between Cairns and Osaka, Nagoya, Fukuoka and Sapporo (Sapporo in the winter season only). Together, the Group offers approximately 62% of the direct seats between Australia and Japan.

Qantas has a longstanding partnership with Japan Airlines. Cooperation primarily revolves around code share arrangements on selected services between Australia and Japan. This has assisted in achieving greater efficiencies for the respective airlines and improved outcomes for travellers.

The Qantas Group is heavily involved in stimulating travel to Australia from Japan, and maintains a strong working relationship with Tourism Australia in the market. We also work closely with State tourism organisations to promote specific destinations in Australia.

In Australia, Qantas cooperates with the Japan National Tourist Organization to promote greater visitation by Australians to Japan. Various initiatives are being jointly evaluated to take advantage of the 2006 Year of Exchange, which will encourage increased links between the two countries.

Qantas has representative offices in five Japanese cities, which employ 76 staff, and a further 30 staff engaged in airport and freight operations.

Aviation framework

Australia-Japan air services are underpinned by a bilateral agreement concluded in 1957. These arrangements have been updated over time to reflect the needs of both countries' airlines and the expansion of the market.

Although there are some aspects of the bilateral agreement that Qantas believes would benefit from further review, in general, the existing aviation arrangements continue to serve market needs well.

Our specific concern relates to a restrictive tariff article in the agreement. There is a requirement to file published fares with the Japanese Government that restricts Qantas' ability to react quickly to changes in the marketplace. As we are required to also obtain concurrence from Japan Airlines to any changes in published fares, our primary competitor is privy to all pricing information in advance of changes.

However, as we believe that over time these issues will be resolved through the existing bilateral mechanism, we do not regard inclusion of air services within the scope of an FTA as necessary. We are confident that further liberalisation of the arrangements can continue to develop effectively within the current framework. This approach would be consistent with the treatment of aviation in the FTAs which Australia has already negotiated with the USA, Singapore and Thailand, and which we understand will be continued in the FTAs currently under negotiation with China, Malaysia and the United Arab Emirates.

Doing business in Japan

Qantas does not face any impediments of note to conducting its business in Japan that in our view might be addressed in the context of an FTA.

The Japanese wholesale and retail travel industry is highly vertically integrated, and major Japanese companies maintain substantial control over the sale of the range of travel product, from air fares to sightseeing, tours, ground transport and hotel accommodation. This is a characteristic of the travel trade with which all airlines operating out of Japan are familiar, and while different to the structure of the industry in other countries, is not considered by Qantas as a constraint on doing business.

Although the Australia-Japan aviation market is a mature one, the enhanced trade links and opportunities that will flow from an FTA are likely to stimulate aviation and tourism activity.

Qantas is therefore in favour of the negotiation of an Australia-Japan FTA. Our support is qualified, however, by an expectation that aviation market access arrangements will continue to be addressed under the bilateral treaty arrangements already in place.

We would be pleased to discuss any of the foregoing further with you.

Yours sincerely

David Hawes
Head of Government and International Relations

17 October 2006

Mr Paul Bourke
Japan Section
Department of Foreign Affairs and Trade
RG Casey Building
Barton ACT 0221

Dear Mr Bourke

Re: Australia's 2006 Regulatory Reform Submission to Japan

Thank you for your letter of 18 September inviting Qantas to submit views for consideration in developing Australia's submission to the Japanese Government in relation to regulatory reform.

Japan is a key market for Qantas. Qantas currently operates 45 return services per week to Tokyo, Osaka and Nagoya, plus seasonal services to Sapporo. In 2007, Jetstar, the Qantas Group's value-based subsidiary will enter the market. Qantas has invested heavily in marketing, product and infrastructure to support our Japan network over many years and works closely with tourism organisations to promote travel between Australia and Japan.

Air services between Australia and Japan are underpinned by a bilateral agreement concluded in 1957. These arrangements have been updated over time to reflect the needs of both countries' airlines and the expansion of the market.

There is one regulatory issue of significance, however, that is of ongoing difficulty for us. This relates to Article X in the bilateral agreement that governs the establishment of tariffs for air services (refer Attachment). The article requires that tariffs be set through the International Air Transport Association (IATA) rate-fixing machinery or agreed between the carriers concerned. This means that all tariffs require approval by the aeronautical authorities of each side – a so-called "double approval" regime.

While this article remains a feature of a number of bilateral air services agreements to which Australia is a party, in Qantas' experience, Japan is one of the few countries where the applicable aeronautical authority mandates that airlines obtain "concurrence" from the relevant home carrier before published fares can be filed.

The practice of requiring the concurrence of Japanese carriers to any changes in published fares also means that our principal competitor, Japan Airlines, is

privity to all pricing information in advance of changes, thus placing Qantas at a disadvantage.

Notwithstanding efforts by Qantas and the Australian Government, the concurrence requirement continues to be enforced by the Japanese Ministry of Land, Infrastructure and Transport (JMLIT).

The Australian Department of Transport and Regional Services (DOTARS), in contrast, does not enforce the filing of tariffs by carriers where this requirement exists under any of Australia's bilateral agreements.

Furthermore, as the bilateral obligation requires agreements between competitors on prices, it is contrary to the *Trade Practices Act 1974*. While Qantas has previously obtained authorisation from the Australian Competition and Consumer Commission (ACCC) to engage in such conduct, the ACCC is currently reviewing this approval. Qantas' strong preference is to avoid the need for any future authorisation by securing removal of the concurrence requirement.

The requirement to file published fares with the JMLIT also restricts Qantas' ability to react effectively to changes in the marketplace. The filing requirements take between two and five days to complete and airlines are charged a substantial processing fee.

As a consequence of the current environment of high fuel prices, surcharges have become an important component of airline tariffs, and flexibility in adjusting them is essential. However, fuel surcharges on airline tariffs are also required to be filed with the JMLIT. Filings for foreign carriers are handled separately to those of Japanese airlines and, in Qantas' experience, the process often takes significantly longer for foreign carriers. This aspect of the tariff filing requirements also impedes the speed to market of Qantas' fares.

Qantas would welcome the freedom to establish our published fares and surcharges between Australia and Japan independently, and introduce them expeditiously with limited intervention from the Japanese aeronautical authorities. Accordingly, we continue to seek to have the existing tariff filing requirements abolished or amended.

Despite efforts by DOTARS, air services consultations held in January 2006 between the Australian and Japanese governments failed to achieve liberalisation of the current processes.

In view of the lack of progress, Qantas and Japan Airlines have reached an in principle agreement to provide each other with "standing concurrence" of those fares that need agreement under the bilateral. Our view is that this will enhance price competition as well as commercial flexibility in the Australia-Japan market.

Nonetheless, agreement between the two governments to amend or remove the requirement would be far preferable to arrangements between individual airlines, particularly as these agreements could be terminated by either party if commercially desirable. Qantas believes Australia raising this issue in the context of its regulatory reform submission would be of value in reaffirming the importance of formal liberalisation in this area.

Japan has indicated that it views tariff regulation as a policy issue, rather than something to be negotiated with individual parties. Against this background, we note that airline tariff filing requirements have been raised by the US and the EU in their respective submissions to the Japanese Government.

We would be pleased to provide further information in relation to any of the foregoing if this would be of assistance.

Yours sincerely

David Hawes
Group General Manager
Government and International Relations

ATTACHMENT

Article X of the Australia-Japan Air Services Agreement 19 January 1956

1. The tariffs on any agreed service shall be established at reasonable levels, due regard being paid to all relevant factors including cost of operation, reasonable profit, characteristics of service (such as standards of speed and accommodation) and the tariffs of other airlines for any part of the specified route. These tariffs shall be fixed in accordance with the provisions of this Article.
2. Agreement on the tariffs shall, whenever possible, be reached by the designated airlines concerned through the rate-fixing machinery of the International Air Transport Association. When this is not possible, tariffs in respect of each of the specified routes shall be agreed upon between the designated airlines concerned. In any case the tariffs shall be subject to the approval of the aeronautical authorities of both Contracting Parties.
3. If the designated airlines concerned cannot agree on the tariffs, or if the aeronautical authorities of either Contracting Party do not approve the tariffs submitted to them, in accordance with the provisions of paragraph 2 of this Article, the aeronautical authorities of the Contracting Parties shall endeavour to reach agreement on the appropriate tariffs.
4. If the agreement under paragraph 3 of this Article cannot be reached, the dispute shall be settled in accordance with the provisions of Article XIII of the present Agreement.
5. No new or amended tariff shall come into effect if the aeronautical authorities of either Contracting Party do not approve it except under the terms of paragraph 3 of Article XIII of the present Agreement. Pending determination of the tariffs in accordance with the provisions of this Article, the tariffs already in force shall prevail.