

# VIRGIN BLUE UNDER SIEGE

## Regulatory authorities threaten Borghetti's 'new Blue' vision



Image credit: www.photolibary.com

By Ian McMahon

JUST one month ago, Virgin Blue Group's new chief executive John Borghetti rolled out the first phase of a major overhaul of the carrier's operations.

It was the first shot in what he intends to be an all-out assault on the stranglehold that Qantas exerts on Australia's corporate travel market.

A key element of his strategy for the "new Blue" is a far-reaching rationalisation of international services operated by the group under the Pacific Blue and V Australia brands.

The plan is for V Australia, flying B777s, to concentrate on international long-haul routes, offering three classes, rather than the present two classes, on major routes.

V Australia will relinquish its current Fiji services to Pacific Blue which will focus on medium haul international routes across the Tasman, the Pacific Islands and South East Asia.

Borghetti said his aim is to "provide a more attractive schedule for the business market, including better integration of our international and domestic schedules".

Underpinning the viability of the carrier's international ambitions are three proposed alliances – with Air

New Zealand across the Tasman; with Delta Airlines across the Pacific and with Etihad to provide an entrée to the kangaroo route.

The first two are in danger of being outlawed – by the Australian Competition and Consumer Commission (ACCC) in the case of the trans-Tasman pact and the US Department of Transportation in the case of trans-Pacific services.

At presstime, Virgin Blue Group has until September 24 to persuade the Australian and US regulators that they have got it wrong and should reverse their initial assessments. Borghetti is confident the airline can do this.

However Qantas has added to his problems, launching a strong attack on the Etihad proposal in a bid to persuade the ACCC to rule against it.

In the case of trans-Tasman routes, Virgin Blue has attempted to sell its proposed alliance with Air New Zealand on the grounds that it will increase competition.

Under the proposal the two carriers would co-ordinate pricing, revenue management, schedules, capacity and routes flown.

The combination of Virgin Blue and Air New Zealand, it is argued, will be able to put up a better contest against the Qantas-Jetstar monolith.

The ACCC is not buying this even though it acknowledges the alliance would provide the applicants with a broader and more integrated network.

"However, the ACCC is not convinced that this necessarily creates a dynamic in the trans-Tasman market that is fundamentally more competitive than a scenario where Virgin Blue and Air New Zealand continue to operate independently and pursue their publicly stated aims to develop their business models," the commission stated.

Explaining the commission's draft determination against the alliance, ACCC chairman Graeme Samuel said: "The ACCC believes that Virgin Blue is a significant competitor to Air New Zealand and there are a number of trans-Tasman routes where the alliance raises competition concerns.

"These routes account for around one quarter of passenger traffic in the trans-Tasman market. This means that more than one million passengers per year may be adversely affected by the removal of competition between Virgin Blue and Air New Zealand."

The ACCC said it accepts that the alliance is likely to result in some of the public benefits claimed by the applicants such as cost savings and efficiencies, but it has doubts about the

magnitude of these benefits.

Ironically the ACCC has granted approval for Virgin Blue to form a similar joint venture with Delta Airlines for trans-Pacific operations.

The difference, said the ACCC, is that the trans-Tasman proposal would bring together the first and third major competitors in the market while delivering "substantially less significant connectivity benefits for consumers" than the proposed Delta pact.

This has become a moot point, however, as the US Department of Transportation (DOT) has now issued a preliminary ruling against the proposed tie-up between Delta and Virgin Blue. The US regulator said the two airlines would improve their market share but they failed to show they would deliver lower fares or more frequencies.

Virgin Blue has signalled it will not be giving up without a fight.

In the case of the alliance with Delta, the airline said it strongly believes the partnership will be good for consumers and both airlines will be working with the DOT to respond to the concerns raised.

On the trans-Tasman, Virgin Blue said it will join Air New Zealand in efforts "to substantiate the public benefits claimed".

Blue Group's proposed tie-up with Etihad.

Borghetti is clearly pinning much of his hopes for Virgin Blue's international viability on this pact with the Middle Eastern carrier, announced late last month.

He called it "a real game changer", enabling the Australian carrier "to redefine its long-haul operation and unlock a genuine global network that would be particularly attractive to Virgin Blue's business and international leisure travellers".

The proposed commercial relationship would see V Australia mount direct services to Abu Dhabi in 2011.

But the two airlines want to offer a joint network of more than 100 destinations and integrate their frequent flyer schemes as early as October 1 and they have asked the ACCC to fast track interim authorisation.

"Together, Etihad and V Australia will move towards a total of 27 weekly services between Abu Dhabi and Australia – including double-daily services between Abu Dhabi and Sydney, daily Melbourne-Abu Dhabi flights and six frequencies per week between Abu Dhabi and Brisbane," the joint announcement said.

"V Australia will operate three Sydney-Abu Dhabi services per week from February 2011 and three Brisbane-Abu Dhabi services per week by February 2012, using its new fleet of three-class B777-300ERs."

Borghetti's pitch is that the deal will increase competition, choice and convenience for the travelling public. "Everybody wins from this partnership," he claimed.

Well, maybe not everyone. Qantas, which has its own very similar joint venture with British Airways has urged the ACCC to ignore calls to fast-track the approval process.

Claiming there is already a high degree of competition on the Australia-Europe route, Qantas argues that passengers could suffer "considerable harm and inconvenience" if they book tickets during an interim period but final authorisation is ultimately denied.

Qantas objections to the pact include that "it is not possible that the applicants will not also be co-ordinating prices between Australia and Europe when they are price fixing on the Australia-Abu-Dhabi route".

**'There is a need for a second Australian airline to operate an extensive competitive international network. That is what we are trying to achieve – that is why these strategic alliances are so important' – John Borghetti**

Apparently undaunted by the pressure, Borghetti has been publicly explaining his international strategy and outlining the arguments his airline will be putting to the Australian and US regulators.

"Our international strategy recognises that it is impossible for any airline based at this end of the world to offer a global network on its own," he told a Financial Services Council Deloitte Leadership lunch in Sydney earlier this month. "However, if you have the right alliances and partnerships you can offer hundreds of destinations with just a small fleet.

"Quite simply, there is a need for a second Australian airline to operate an extensive competitive international network. That is what we are trying to achieve – that is why these strategic alliances are so important.

"Without them, tourism, competition and our economy will be the losers."

He said the US Department of Transportation's preliminary denial of

the Virgin Blue-Delta alliance "appears to undermine the intent of the Open Skies agreement between Australia and the USA".

Asserting that a Virgin Blue-Delta combination would deliver competition and consumer benefits, he pointed out that the alliance would have a combined trans-Pacific market share of 23 per cent compared to Qantas with 54 per cent.

On the trans-Tasman he insisted: "We believe a Virgin Blue-Air New Zealand alliance would deliver greater

competition, cheaper fares, more flight options and better connections."

He said Virgin Blue's representations to the ACCC include the October 2004 decision by the Australian Competition Tribunal to approve a Qantas-Air New Zealand alliance, overruling an ACCC decision against it. (As it happened the alliance never went ahead because the New Zealand Commerce Commission ruled against it.)

"That (Qantas-Air New Zealand) alliance involved the two largest carriers on the route with a combined market share of over 80 per cent. The rationale for that alliance was to reduce capacity," Borghetti said.

"The Virgin Blue-Air New Zealand alliance does not propose any reduction in capacity..."

"Our Trans Tasman routes lose money. We need to improve our competitive position for both corporate and leisure travellers to turn them to profit – that is what the alliance is designed to deliver."

## 10th birthday celebrations: undaunted DJ looks forward to next 10 years

VIRGIN Blue was not going to let a few regulatory problems dampen its 10th birthday celebrations.

The carrier defiantly tapped its way into the next 10 years with an all-star performance featuring singer-songwriter and Australian artist of the decade Delta Goodrem and Dein Perry's Tap Dogs.

Members of the airline's staff joined them on stage inside a hangar at Melbourne Airport with a Virgin Blue B737-800 forming the backdrop.

Virgin's global figurehead Sir Richard Branson flew in to join the celebrations – and to provide rousing words of support for the direction that new chief executive John Borghetti wants to take Virgin Blue – regulators permitting.

"The airline that shook up the Australian aviation industry 10 years ago has now grown

up and I'm extremely excited about John's plans for the future," said Sir Richard.

"Our next 10 years will be just as exciting as we continue to grow our network, enhance our products and services and bring the same competition to the corporate market as we did to the leisure market 10 years ago.

"John Borghetti's vision for the evolution of Virgin Blue is simply inspiring."

Ignoring the threats posed by regulators, Borghetti said: "The Virgin Blue Group of airlines is on the threshold of new and exciting projects.

"Our first 10 years were great. The next 10 will be ground breaking."

*Right: We will not give in ... Sir Richard Branson gives a Churchillian V for victory sign at Virgin Blue's 10th birthday celebrations*

