

Out of scope



6 **Cabinet Notes**

Out of scope



602 POSSIBLE FAILURE OF O'CONNOR AIRLINES (Patrick Conlon) - NOTED

Out of scope



602
TO: THE PREMIER FOR CABINET TO NOTE

RE: POSSIBLE FAILURE OF O'CONNOR AIRLINES

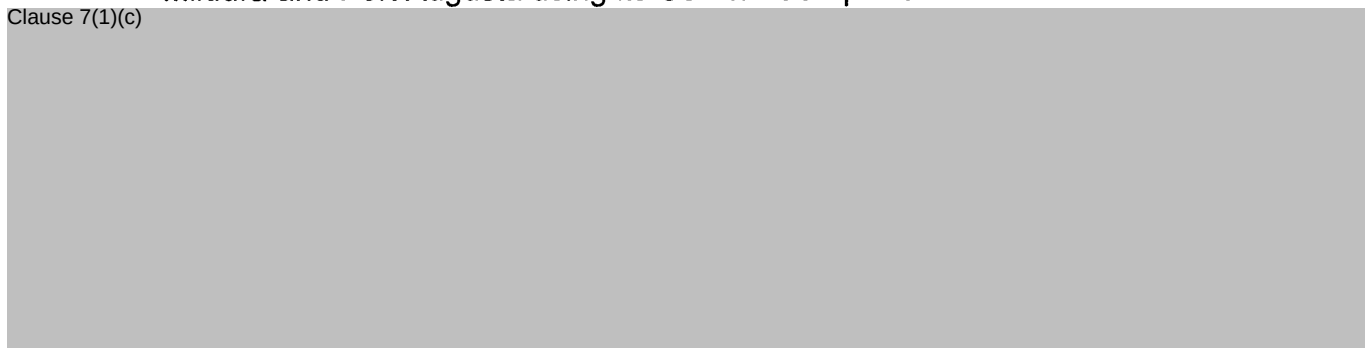
1. PROPOSAL

- 1.1. That Cabinet note the imminent possibility of failure of O'Connor Airlines and the impacts of that if it occurs.

2. BACKGROUND

- 2.1. O'Connor Airlines is a small regional airline, owned and operated by the O'Connor family since 1973, based in Mount Gambier. It undertakes ancillary aviation activities including charter, training, maintenance and search and rescue flights.
- 2.2. It operates scheduled airline services with a fleet of three 19-seat Jetstream 32 aircraft and one 9-seat Cessna Conquest. Jetstream routes are from Adelaide to Mount Gambier and Whyalla and from Mount Gambier to Melbourne, all operated in competition to Regional Express. It is the sole operator from Adelaide to Mildura and Port Augusta using its Cessna Conquest.

Clause 7(1)(c)



3. DISCUSSION

Clause 7(1)(c)



Clause 7(1)(c)



- 3.3. The immediate consequence of closure of the company would be the loss of 51 direct jobs in Mount Gambier, most of which are skilled aircrew and mechanics, with an annual payroll of \$2.553 million. Those skills are in high demand and the affected employees could be expected to regain employment quickly, but not in Mount Gambier.
- 3.4. Contractors providing ground handling at Melbourne, Adelaide, Mildura and Port Augusta would also be affected.

- 3.5. All air services from Adelaide to Port Augusta and Mildura would cease with little prospect of quick replacement. The reduction of services on the contested routes to Whyalla, Mount Gambier and Melbourne would have little impact and Regional Express could be expected quickly to replace the capacity. Regional Express would be unlikely to base aircraft in Mount Gambier, so the community would probably lose the convenience of early originating flights.
- 3.6. Mr O'Connor is making short-term aircraft rerouting plans and cancellations to cover the loss of the aircraft. He is also in negotiations with QantasLink to take over his Mount Gambier-Melbourne route, which would free up an aircraft and enable him to run the rest of his schedule more efficiently.
- 3.7. Mr Allan Scott of Scott Transport has also proposed the purchase of a replacement aircraft for leaseback to O'Connor Airlines, if that can be agreed on a fully commercial basis.
- 3.8. These measures are unlikely to be sufficient and closure of the company is possible, but it is difficult to identify how the Government could assist. Grants or subsidies would not provide long-term resolution of the problems.
- 3.9. Mr O'Connor argued strongly for the continuation of his Port Augusta route licence. The Minister for Transport has indicated that the Government will be prepared to consider re-licensing the route to O'Connor Airlines for three years on expiry of the present licence.
- 3.10. In relation to Government travel shares, the Government's travel provider is required to offer flights on a best-fare-of-the-day basis. Under that policy O'Connor Airlines provided 31.4% of seats on the Adelaide-Mount Gambier route in 2006 but achieved only 27.4% of Government fare revenue. Similarly, it provided 31.6% of seats to Whyalla but achieved only 16.6% of revenue. That might be partially redressed by more effective policing of the use of lowest fares, but Mr O'Connor acknowledges that his major problem is his inability to compete with Regional Express' aggressive fare discounting.

Clause 7(1)(c)

Clause 7(1)(c)

Airline predatory pricing is difficult to distinguish from aggressive competition and no example of it has yet been sufficient to prompt action by the ACCC.

- 3.12. Regional Express pursues a policy of volume growth through fare discounting. This has resulted in extraordinary growth on all routes in SA that it operates other than Kingscote.
- 3.13. While discounting may be to levels below cost, it is carried out under careful yield management to ensure that each route, contested or not, remains profitable. It also operates larger aircraft with lower seat/kilometre costs than O'Connor Airlines, which enables it to discount fares profitably to lower levels.
- 3.14. Regional Express claims that all its SA routes are profitable, except Ceduna and Coober Pedy. Those two routes are presently unprofitable because of the recent replacement of Metro aircraft with larger Saab 340s, which are presently oversized for the passenger volumes on the routes.
- 3.15. BHP-Billiton has provided confidential advice that it is about to award its Olympic Dam air travel tender to Queensland-based Alliance Airlines. The airline is to base two 56-seat F50 aircraft and crews in Adelaide for the contract, which will

displace Regional Express from the route. This information has not yet been publicly released or the airline advised of the award.

- 3.16. This route, while it has been highly profitable for Regional Express, is unlikely to affect its services on other routes. Since the two Alliance aircraft will be substantially underutilised in the contract, it will also provide Alliance with an opportunity to compete with Regional Express on the Whyalla and Mount Gambier high-volume routes that O'Connor Airlines may vacate, and to implement services on other routes such as Port Lincoln and Kingscote.
- 3.17. The Alliance aircraft are not suitable for use on the smaller Port Augusta and Mildura routes, should they be vacated by O'Connor Airlines. The Minister for Transport is prepared to offer sole route licences to prospective operators to Port Augusta, it is unlikely that that would be sufficient to attract new services. The Government is not empowered to licence the Mildura route since it involves an interstate destination.

4. RECOMMENDATIONS:

That Cabinet notes:

- 4.1. That O'Connor Airlines is at risk of closure, and that this would have significant regional employment and air service impacts;
- 4.2. That the causes of this primarily relate to O'Connor Airlines' inability to compete with aggressive fare discounting by Regional Express, and the loss of one of its four Jetstream aircraft;
- 4.3. That the Minister for Transport has offered to licence O'Connor Airlines on its Port Augusta route to encourage it to continue services, subject to a satisfactory business plan for the route;
- 4.4. That DTEI, in consultation with the SA Tourism Commission and the Department of Trade and Economic Development, in the event of O'Connor Airlines' withdrawal, will canvass all possible opportunities to gain replacement services on vacated routes to Port Augusta and Mildura; and
- 4.5. That O'Connor Airlines' withdrawal from its other routes would have minimal impact with the services being quickly replaced by Regional Express and possibly Alliance Airlines or other new operators.


HON PATRICK CONLON MP
MINISTER FOR TRANSPORT

6 April 2007

In Cabinet

16 APR 2007

