

AVIATION ECONOMICS

**Senate Committee on Rural and Regional Affairs and Transport
Parliament House
Canberra ACT 2600
Email: rrat.sen@aph.gov.au**

14 March 2014

Dear Senators,

Re: Qantas' future as a strong national carrier supporting jobs in Australia

Aviation Economics appreciates the opportunity to submit to the Senate Rural and Regional Affairs & Transport Committee a submission on the future of Qantas. Aviation Economics is a boutique private company registered to provide aviation related economic information to not for profit organisations seeking to formulate an informed opinion regarding aviation issues pertinent to their particular area of interest.

Qantas' Operating Costs

The following quote from the Securities & Investment Group CLSA, published after Qantas made its restructuring announcement on Thursday February 27th clearly sums up the costs issue:

- *The cost "light bulb" moment has come. The nature of political support is uncertain and it is difficult to believe Qantas can achieve such transformation in three years without changes to the Qantas Sale Act. It has a significant unionised workforce which, anecdotally does not appear too aligned.*

CLSA had previously stated in a prior note to its clients on the 26th of February that:

- *We cannot believe there is not a way to negotiate a win-win between staff and management (for example in the form of lower wages in exchange for equity) that would better align both parties in facing up to the challenges faced by Qantas. Both must share the burden of restructuring – why can they not share the potential upside as well?*

If Qantas cannot become capital and manpower efficient, it is our belief that Qantas will continue to contract internationally and will ultimately be forced to operate more of its existing international services using Jetstar, and/or One World code share flights; assuming it even elects to continue operating internationally.

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Employee Equity Participation

That Qantas finds itself in its current circumstances is not particularly unusual for mature legacy airlines. However, extensive recent public press suggests that 'more of the same' is unlikely to help return Qantas to its former glory.

In December 2013, in response to newspaper reporting that Qantas staff may take a stake in the airline, Alan Greig from the Employee Ownership Association publically said, "*The proposal should be given serious consideration*". Employee buy-ins have been proven to work in airlines throughout the world," Regretfully, the EOA's website also states, '*Australia lags behind the rest of the developed world in the area of employee share ownership*'.

Further, in an article entitled Total Success, by Ruth Ostrow in The Weekend Australian of 1 March 2014, Gerry Harvey of Harvey Norman Australia is reported as saying: '*the results (of employee engagement) can be way beyond even your most optimistic beliefs*'.

Overseas in the USA, a number of US Airlines, such as United Airlines have recovered from Chapter 11 bankruptcy proceedings using employee equity as the element that brought together otherwise fiercely competing stakeholders. Southwest Airlines is a particularly poignant US example of where employee equity has worked brilliantly in the aviation industry. Unlike many North American Airlines, Southwest has never made a loss. According to The National Center for Employee Ownership in the USA, "*Southwest is the most profitable airline in history. Its experience shows how dramatically positive and long-lasting employee equity can be for airlines.*"

For the reasons stated above, Aviation Economics believes that the CLSA suggestion of lowering manpower costs in return for equity would greatly assist the 'Qantas of tomorrow', reengage its workforce, manage necessary change and significantly lift productivity. Based on figures extracted from Qantas' 2013 annual accounts, a 25% employee stake in Qantas would cost around \$600 Million at the current share price of \$1.10 and 3% of Qantas' annual manpower cost is \$115 Million. Further, Qantas has announced that it intends to freeze salaries until the Company makes an underlying profit. Prima facie, this means that a three to five year pay freeze could not only dramatically improve Qantas' financial position, but also provide the basis for securing the employee equity necessary to fulfill ownership conditions necessary to keep Qantas Australian. (For further details on why this is so, the Committee should refer to Aviation Economics' submission to the Senate Economics Legislation Committee's Inquiry into the **Qantas Sale Act Amendment Bill 2014** attached thereto)

How Government can assist Qantas

Aviation Economics supports the Prime Minister's stated public view that 'Qantas is responsible for getting its house in order'. However, doing so in circumstances where confidence in leadership and strategy is so fractured, means making progress is extremely difficult.

We believe that Federal Government is well placed to kick start the transformation of Qantas by sponsoring a consultative committee that can develop the processes and procedures necessary to unleash the turnaround effect employee equity participation would bring.

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The author's recent conversation with Ron Bloom, now an investment banker with Lazards in New York and previously an advisor to Barak Obama's auto industry recovery initiatives, can be paraphrased as - '*achieving an impossible restructure requires government, management, unions and the necessary consultants to be in the same room. If you can't get them together, you have no chance*'.

Recommendation

- *Aviation Economics recommends that the Senate Rural and Regional Affairs & Transport Committee consider requesting that the Government make its support for a Qantas Sale Act Amendment Bill subject to the Government satisfying itself that Qantas has a future as a strong international carrier supporting Australia.*
- *Considerations the Rural and Regional Affairs & Transport Committee may wish to request of the Government, includes the establishment of a Government sponsored consultative committee charged with formulating and recommending to the Qantas Board, process and procedures necessary to create a Qantas Employee Share Trust.*

Aviation Economics sincerely thanks the Senate Rural and Regional Affairs & Transport Committee for the opportunity to comment on the future of Qantas. We trust that the Committee finds the information we have provided helpful.

Yours Sincerely,

Ian Woods
Executive Director

One Enclosure - *Aviation Economics' submission to the Senate Standing Committee on Economics inquiry into the **Qantas Sale Act Amendment Bill 2014**.*