Ronald H. Entsch

SUBMISSION NO. 11

18 Remick Street
Stafford Heights 4053

Email: entsch@eis.net.au
Phone 61 7 3353 4541
Fax 61 7 3353 4419
Mobile 0428 748 954

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Mr Ian Dundas
Committee Secretary
House of Representatives Standing Committee on Transport & Regional Services
Parliament House
Canberra ACT 2600

Dear Sir

I submit herewith for your information and consideration:

- A formula for providing financial assistance for a regional service
- A discussion on hubbing and fares
- My curriculum vitae briefly outlining my airline experience
- An extract from my book containing historical data on subsidy to remote areas

This is a private submission as I have not had nor have I made any contact with any other party regarding this subject.

Please note that I have been out of the regional airline environment for many years though I still carry the old scars of handing around the begging bowl for financial assistance to maintain outback air services in the north and west of Queensland.

The numbers mentioned in the attachment can be used as levers for deciding assistance levels, eligibility and responsibility. I'm out of date with the financial numbers which need to be aligned with a range of current air fares from with current data.

The system must be simple in all ways. Using my formula, the Federal Government is seen to be open-handed but enmeshes both the State and local interests who also have to assist. In the USA, the emerging regional airlines were usually subsidised.

The administration of subsidy payments was a real nightmare in my day and probably still is. Bureaucrats would make subjective statements like "we didn't ask them to live there" and turned the accounts upside down to ensure that government paid the absolute minimum amount, foisted upon their budget by their political masters.

In my view, the concept of "hub and spoke", as it is spoken of in Australia, is uneconomical from an optimum scheduling viewpoint. In Ansett I had looked into hubbing at Newcastle with a B737 with the NSW regionals feeding from/to the north, north-west and west. Dubbo gave a similar result.

I hope I'm not wasting the Committee's time in this matter and that you find some of the content to be useful or helpful.

Yours truly

A FORMULA FOR PROVIDING FINANCIAL ASSISTANCE FOR A REGIONAL AIR SERVICE

1. In supplying and/or receiving a subsidy, it is formally recognised by all parties that:

    a. The airline will carry totally the commercial risks to choose and operate an appropriately sized and suitably equipped aircraft on a frequency of service to suit the local market but, in any event, not less than thrice weekly to towns and communities, and weekly to remote stations. In the event of commercial failure there will no recourse to either the State or Federal Government.

    b. The affected community council declares to its State/Territory Government that such a regular air service, as proposed, is justified and that it guarantees to maintain a suitable aerodrome and terminal facilities at its own cost, with no cost to the airline.

    c. The State/Territory Government is prepared to license the airline, exclusively, to conduct such regular air services.

    d. The Federal Government receives the requests from both the community council and the State/Territory Government to establish, or to continue, the regular air service, and receives confirmation of CASA's approval to license the operator.

    e. Only towns and communities situated west of the Great Dividing Range and 400 kms from its nearest coastal commercial centre, and with a population of less than 10,000, will be eligible for a subsidised air service.

2. Subsidy payable per passenger, either adult or child, will be calculated on the basis of kilometers measured in a straight line from that coastal centre, and within the following brackets [example only]:

400 to 500 kms	$50	700 to 800 kms	$80
500 to 600 kms	$60	800 to 900 kms	$90
600 to 700 kms	$70	900 to 1000 kms	$100

3. The subsidy payment shall not exceed 50% of the published one way adult fare.

4. The subsidy will be paid to the community council by the State/Territory Transport Department and the Federal Transport Department on the basis of 50/50 [or whatever other proportion is negotiated].

5. The passenger statistics will be collected from the airline by the community council, and spot-checked by council staff at least once weekly. [The council in most cases will be the airport owner].

6. The council will send an account to the each Transport Department at the respective rate stated in 2 above, and remit the funds to the airline on a monthly basis, after withholding $1 per passenger as reimbursement of associated administrative costs.

7. If air cargo, including mail, is to be subsidised then the kilo rate applicable will be the equivalent to the weight of a passenger with baggage [say 80kgs], divided into the rate show in 2 above. Example: $50 divided by 80kgs = 63cents kg subsidy.

8. Collection of cargo weight landed will be reported and paid via the community council in conjunction with inbound passenger travel but no further payment will be deducted for administration costs.

A DISCUSSION ON HUBBING AND FARES

Creating a hub at which a large aircraft is fed by smaller aircraft seems to be a logical approach until the dynamics of schedules affecting aircraft utilisation and fixed costs, and resultant economies of scale are analysed.

Broadly speaking, large international jets are able to operate at the lowest cost per seat kilometer because they can fly over 5,000+ hours a year carrying around 400 passengers. Domestic jets costs are higher as they fly 3,000+ hours with 100-300 passengers. The larger regional airlines cost are higher still as they fly 2,000 hours with 30 passengers. The smaller feeder airlines are higher again as they strive for 1,000+ hours with 5-15 passengers.

The larger jets are more fuel efficient, have longer times between maintenance lay-ups, and benefit from long haul operations particularly during the night.

It is essential that aircraft are kept "in the air" and not sitting on the ground waiting for connections with lengthy turnarounds. That principle applies to all regular airline operations.

Southwest Airlines in the USA shuns hubbing and operates "point to point" with one aircraft type, the Boeing 737. It has been consistently expansive and profitable. Hubbing in the USA has been reasonably successful because of the spread of its population across an area the size of Australia. Our demography makes its impossible to compare Australia with the USA for hubbing opportunities.

It may be possible to hub if the smaller operator is based at the distant town [A] and is able to feed into the larger town [Z] where the larger aircraft is discharging its load and awaits the incoming load from the regional for its return to the city [Y]. Other regionals might have started out from their home bases, say B C & D so five aircraft are converging on Z to connect their loads.

For an economic operation, the large aircraft has disembarked enough passengers for each of the four regionals to make a payable load to return to their home bases. The larger aircraft likewise has expected to uplift enough passengers from the feeders to make that flight back to the city worthwhile. This sort of operation can be repeated as often as the market dictates – two or three times a day or more if required i.e. A to Z to A, B to Z to B, C to Z to C, D to Z to D.

But what if the stage lengths for these sectors are short and do not generate enough flight hours for the regionals? There are diseconomies of scale for the regionals possibly to the advantage of the larger Y to Z to Y. But, then again, the sector length for the larger aircraft might not generate sufficient utilisation either so both are disadvantaged. If the

regional was able to fly to Y that could possibly double his aircraft utilisation. However, in the case of Sydney, they might not be allowed to do this because of the landing slots permitted. This would not be a problem in the foreseeable future for any other major centre.

Furthermore, it is highly improbable that there would be a regional airline based at A, B, C & D. So it is probable that A & B or C & D could be combined and served by two regionals instead of four. However, flying A to B and C to D would add unproductive hours because there would be no interport traffic. These would thus be "dead legs" adding to the operators costs with no return.

Flying via intermediate ports is also unpopular with country travellers. East-West Airlines originally had a policy of combining only two ports on its services to Sydney e.g. Tamworth/Armidale, Glen Innis/Inverell, Grafton/Coffs Harbour etc. It had learned that passengers would not fly via two or more intermediate ports. That concept provided optimum utilisation for the F27s.

Because of the congestion at Sydney, Ansett considered hubbing a B737 at Newcastle with feeders coming from north and north-western towns of New South Wales. The regionals were not happy to have their utilisation reduced and to commit a B737 to such a short sector was not desirable. For this concept to have any measure of success, the regionals would have had to be banned from Sydney which was not on politically. They might have considered Bankstown but, at that time, it was not an option and Sydney was

seen at the perfect connection point for western travelers going further on overseas or interstate.

On a lower scale, an attempt was proposed by Air Queensland to hub at Longreach to service the surrounding towns of Muttaburra, Barcaldine, Winton, Blackall, Aramac etc. There were no acceptable small operators based at these small towns so a Longreach based operator would have had to be used to do circular routes whilst the larger aircraft sat on the ground at Longreach waiting for its incoming traffic. This was uneconomical and the concept was abandoned. Alternatively, the East-West practice was proposed with the larger towns being joined with Longreach on different services e.g. Blackall /Longreach, Barcaldine/Longreach. The other ports were dropped.

SYDNEY

Sydney has a unique problem with its cap for noise abatement. Though the Government has promised that regionals will not be squeezed out of Sydney, it is possible that the new owners of Sydney airport might consider offering an incentive for the regionals to move to a secondary airport, like Bankstown, so that Sydney might increase its earning capacity by replacing the regional slots with more jet aircraft. If that was to eventuate, there would less prospect for hubbing in New South Wales, and there probably would not need to be.

FARES

Prior to deregulation all airlines had to obtain approval from the Federal Government's Air Fares Committee before any changes could be made to tariffs. For operators, this instilled an understanding of how fixed and variable costs affected air fares.

Before an aircraft left the ground, an operator incurred costs that could only be ameliorated by increasing its flying hours e.g. depreciation and interest or lease finance costs, insurance, administration, flight crew. When the aircraft left the ground it incurred costs for fuel and engineering, and today air navigation and airport fees are variable costs.

Hence the construction of an airfare was a combination of fixed costs divided by the number of passengers, referred to as the "flagfall", plus a mileage cost for the variable costs incurred over the distance flown. Added to both was a margin for profit before tax.

Whether the sector distance was short or long, the flagfall would be the same. Hence when two carriers linked a passenger would be paying two flagfalls which made connecting flights, say via a hub, too expensive by comparison with through flight fares over a similar distance.

For example, a passenger travelling from Bundaberg to Canberra changing carriers at Brisbane, would incur two flagfalls in his fare. If the same carrier flew direct from Bundaberg to Canberra, the fare would incorporate only one flagfall.

Consequently, a major airline would negotiate with a regional feeder to either share or absorb the second flagfall. This would be done through commercial agreements such as Air Queensland had with Ansett Australia and Australian Airlines.

Though the commercial environment is now deregulated, the fixed and variable cost relationships have not disappeared and will focus in the calculations of each operator seeking to maximize its share of the passenger revenue.

Hence the prospect of hubbing introduces the argument of who is going to sacrifice what proportion of its fixed costs, and the consequent proportional loss of profit resulting from operating a shorter sector. If the major airline also owned the regional, the debate would be internal although, in these days of NCP and "user pays", even the major airline e.g. Qantas, would expect its subsidiary to operate profitably.

If, however, a regional airline was granted the subsidy assistance proposed herein, it is highly possible that its economics could be transformed and hubbing might be looked upon more favourably.

ADDITIONAL INFORMATION HELD BY THE SECRETARIAT

ATTACHMENT TO SUBMISSION NO. 11 Mr Ronald H. Entsch

3. Personal Brief, Business Experience, Appointments and Professional Associations.

4. Extract from *Bushies: A History of Bush Pilots – Air Queensland* by Ron Entsch ISBN 0 646 41241 8