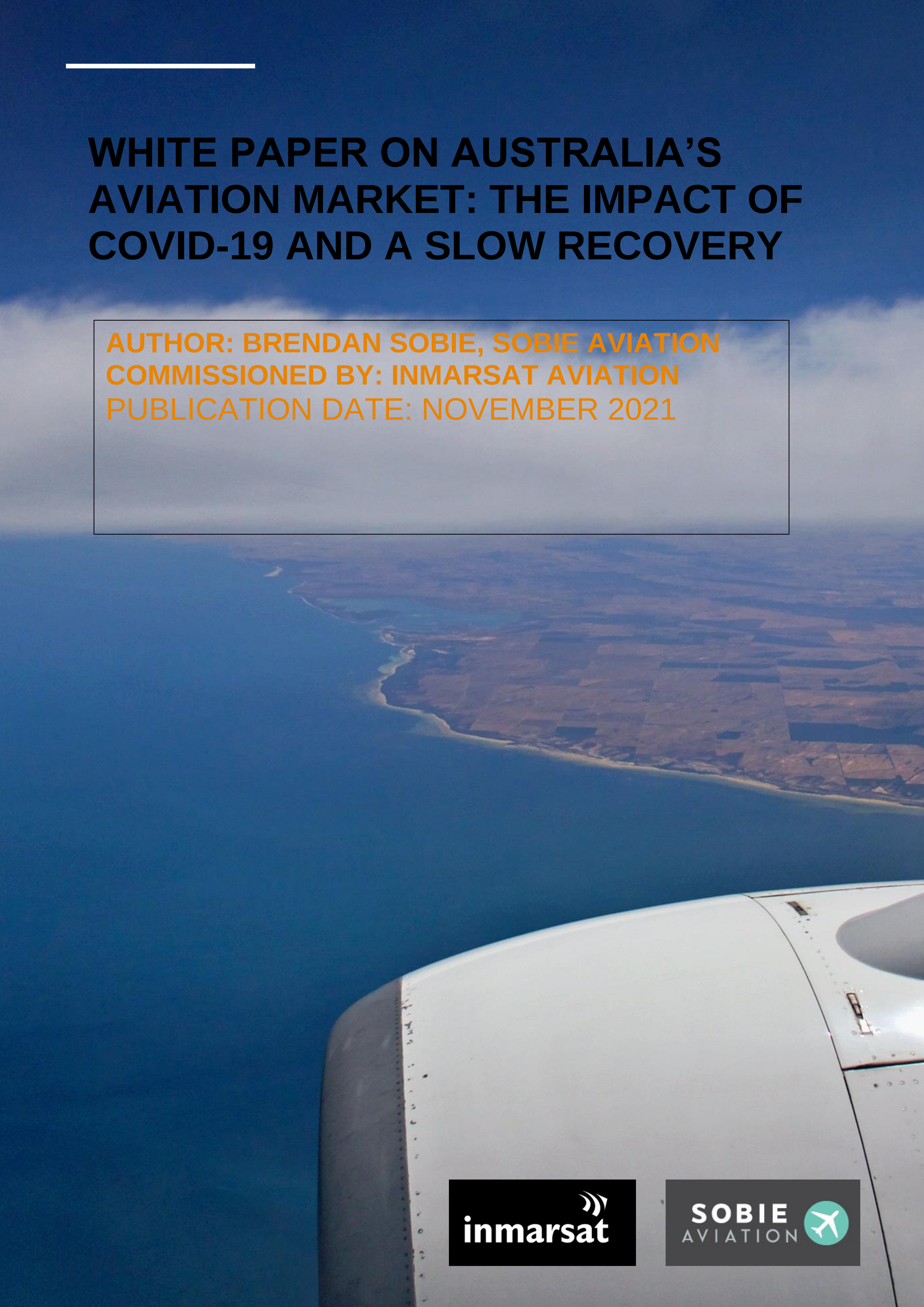

# WHITE PAPER ON AUSTRALIA'S AVIATION MARKET: THE IMPACT OF COVID-19 AND A SLOW RECOVERY

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**COMMISSIONED BY: INMARSAT AVIATION**
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# EXECUTIVE SUMMARY

While Covid-19 has significantly impacted all markets, Australia has been particularly impacted despite having very successful virus containment. Due to a slow vaccination rollout (particularly for developed nations) and a zero-COVID policy Australia is now in the unenviable position of becoming one of the last markets to recover.

Australia has already been the most impacted of the major domestic air transport market in the world, dragged down by internal border closures that has prevented most interstate travel during most of the pandemic. In the first 19 months of the pandemic (April 2020 to October 2021), scheduled domestic passenger traffic in Australia declined by about 73%.

Australian carriers have already lost about AUD16 billion in domestic revenues in the first 19 months of the pandemic due to a loss of 71 million domestic passengers.

On the Melbourne-Sydney route alone there has been a reduction of nearly 13 million passengers or 87%. The top 10 domestic routes combined have experienced a reduction of 84% or about 43 million passengers. Intrastate routes have fared much better but are smaller and also have declined more than the global domestic average.

The domestic market is now starting to recover again and by the end of December 2021 domestic traffic could reach 70% of pre-COVID levels. However, a full recovery could take several more months and occur later than most other major domestic markets.

Internal border issues continue to be an impediment, resulting in a scenario where essentially Australia is divided into two with domestic travel within each portion but not between. This is unfortunate as it separates families and results in substantial economic damage. It is an issue and challenge that is unique to Australia. While the government has provided significant support to airlines and the overall aviation industry, the political environment has been unfavorable and needs to improve for the domestic market to finally recover.

The international market is also starting to recover in November 2021. But the initial recovery will be modest as it will be limited to select states and, with a few exceptions, to Australian residents or their immediate families. A meaningful recovery cannot be achieved until all states reopen their international borders, quarantine is waived in all of Australia and all international visitors are again permitted to enter.

Prior to the pandemic, visitors from overseas accounted for more than 40% of international passenger traffic and about 3% of GDP. Australia's attractiveness as a destination has declined significantly during the pandemic and could fall even further as the rest of the world rapidly reopens.

Australia needs to quickly reopen to visitors and provide a blanket no quarantine option. If there is any uncertainty, potential visitors will continue to travel elsewhere.

Uncertainty is also an impediment to outbound travel as it is not clear when some states or territories will reopen borders and waive quarantine requirements. Consensus and uniformity with regulations and policies is critical as otherwise it erodes passenger confidence.

In the first 19 months of the pandemic, scheduled international passenger traffic declined by almost 98%. Even during the three months the Trans-Tasman bubble was in place the decline was 94%. The pandemic has so far cost Australian carriers about AUD13 billion in international revenues and about 21 million passengers. The economic impact of having virtually no visitors over the past 19 months exceeds AUD60 billion.

There are now opportunities to put in place policies to facilitate both the international and domestic recoveries. Australia has significantly accelerated its vaccination program in recent months, resulting in one of the world's highest vaccination rates and potentially enabling passenger traffic to catch up with other developed countries. But a recovery of the aviation and travel sectors is hardly assured.

First and foremost, the current lack of consensus between states needs to be resolved. With a divided Australia, neither the domestic nor international market will be able to fully recover. Australia will continue to fall behind the rest of the world with huge long-term implications on the aviation and travel sectors. Hundreds and potentially thousands of companies will not be able survive. Thousands of highly qualified industry professionals, including pilots, will be lost to other industries or countries.

*Note:* This paper assesses the impact of the pandemic on Australia's aviation industry so far and examines the outlook for the remainder of this year as well as 2022 and beyond. The current situation is very dynamic. While this paper incorporates recent developments through the end of October 2021, including the removal of quarantine requirements for New South Wales and Victoria from 1 November, there could be other major developments in the coming weeks that will impact the outlook for the end-of-the-year holiday season and 2022.

This paper incorporates available data as of the end of October 2021, including Bureau of Infrastructure and Transport Research Economics (BITRE) and International Air Transport Association (IATA) data through August 2021.

This paper has been commissioned by Inmarsat Aviation and written independently by Brendan Sobie with an international perspective, analyzing how Australia's aviation industry has performed and is now positioned in the global context. Feedback and queries are welcome by contacting Brendan Sobie, independent aviation analyst, at brendan@sobieaviation.com.

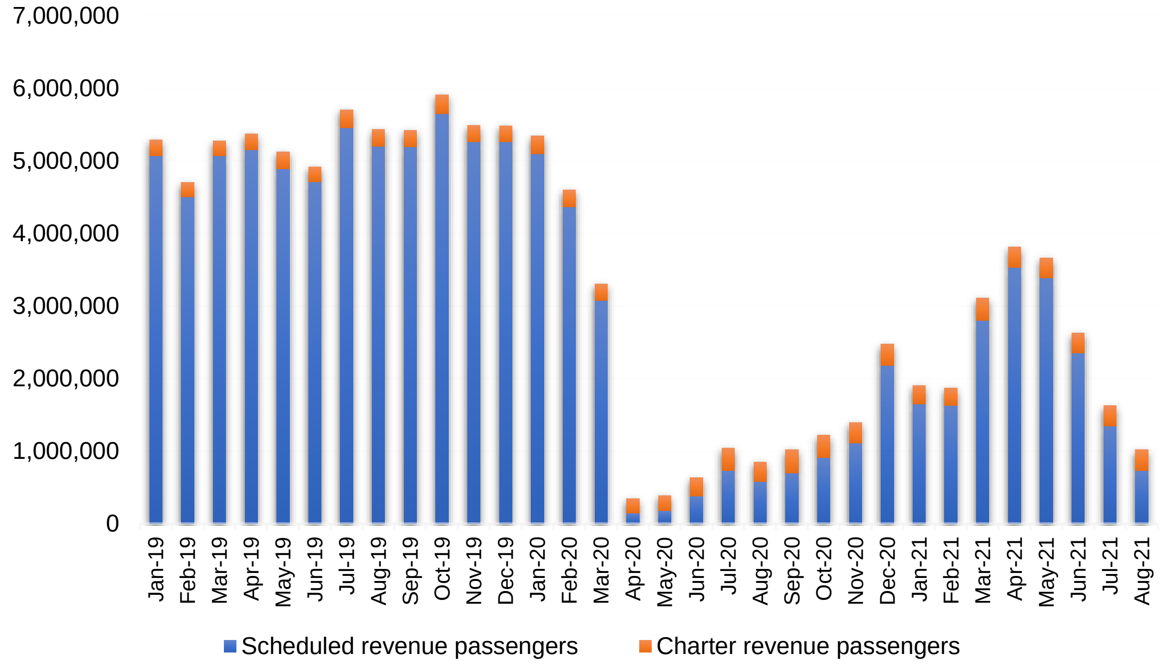
# IMPACT ON THE DOMESTIC MARKET

So far during the pandemic Australia has been the most impacted of the world's main domestic markets despite very low COVID-19 cases and deaths.

In the first 17 months of the pandemic (April 2020 to August 2021), there were 28.4 million domestic passengers in Australia. This represents a decline of 69% compared with the equivalent 17 months prior to the pandemic, according to BITRE data.

Scheduled or regular public transport (RPT) domestic traffic dropped 72% to 24.3 million while the smaller charter segment grew 9% to 4.1 million. The latter reflects the increased demand for charters during the pandemic, particularly from companies in the resources sector, due to the reduction in scheduled domestic services.

**Monthly domestic passenger traffic in Australia: January 2019 to August 2021**




*Source: Sobie Aviation, BITRE*

On a revenue passenger kilometer (RPK) basis, scheduled domestic traffic dropped 72% in the first 17 months of the pandemic to 28 billion. BITRE does not provide RPK data for the charter segment.

Total domestic passenger traffic was 64.1 million in 2019, including 61.4 million RPT passengers and 2.7 million charter passengers. International passengers connecting to domestic flights are counted under RPT.

Australia exceeded 50 million scheduled domestic passengers for the first time in 2008 and exceeded 60 million for the first time in 2018. New records were achieved for five consecutive years, from 2015 to 2019, although the growth rate was very modest. In the five years prior to the pandemic total growth was only 7%.

## Comparing Australia with other domestic markets

In 2020, the total domestic market dropped by 65% to 22.6 million passengers, including a 68% drop in RPT passengers to 19.4 million and a 16% growth in domestic charter passengers to 3.2 million passengers. RPT RPKs dropped 69% to 22.3 billion. This represented the lowest RPT passenger figure since 1992 and the lowest RPT RPK figure since 1993.

In 2020, Australia recorded the largest decline in scheduled domestic traffic among the world's 10 main domestic markets. Australia was the eighth largest domestic market in 2019, ahead of Mexico and Canada and behind the United States, China, India, Japan, Brazil, Indonesia and Russia.

**2019 and 2020 domestic passenger traffic for top 10 domestic markets**

| RANK | COUNTRY | 2019 PASSENGERS (MILLIONS) | 2020 PASSENGERS (MILLIONS) | Y-O-Y CHANGE | COVID-19 DEATHS PER MILLION (AS OF OCT-2021) |
|---|---|---|---|---|---|
| 1. | United States | 812 | 335 | -59% | 2242 |
| 2. | China | 575 | 407 | -29% | 4 |
| 3. | India | 144 | 63 | -56% | 333 |
| 4. | Japan | 107 | 47 | -33% | 144 |
| 5. | Brazil | 95 | 45 | -53% | 2869 |
| 6. | Indonesia | 79 | 35 | -55% | 529 |
| 7. | Russia | 73 | 56 | -23% | 1561 |
| 8. | Australia | 61 | 19 | -68% | 65 |
| 9. | Mexico | 54 | 28 | -47% | 2244 |
| 10. | Canada | 49 | 16 | -67% | 766 |
| | *TOTAL* | *2049* | *1051* | *-49%* | |

*Notes: China domestic figures are for mainland China only; Hong Kong, Macau and Taiwan are excluded*
*Charter passengers generally excluded; a few countries do not separate charter but charters in these countries are limited*

*Sources: Sobie Aviation, US DoT, China CAAC, India DGAC, Japan MLITT, Brazil ANAC, Indonesia DGCA, Russia Federal Air Transport Agency, Mexico SCT, Statistics Canada, John Hopkins University (as of 25 October 2021)*

As the table above indicates, the average decline in scheduled domestic passenger traffic among the top 10 domestic markets was 49%. Australia was 19 percentage points below this figure.

IATA also reported a 49% decline in global scheduled domestic RPKs for 2020. Of the seven domestic markets IATA tracks, Australia had by the largest RPK decline in 2020. Based on IATA data, Australia domestic RPKs declined by just under 70%, which was 20 percentage points below the global decline.

For the first eight months of 2021, IATA reported a 31% decline in global scheduled domestic RPKs. Australia had the second largest decline after Japan over the eight-month period. However, Australia has again been at the back of the pack in recent months and will almost certainly again have the largest decline for the full year.

**Scheduled domestic RPK growth for 2020 and 2021 (vs 2019) for select countries**

| COUNTRY | 2020 | 8M2021 | AUG-2021 | COVID-19 DEATHS PER MILLION (AS OF OCT-2021) |
|---|---|---|---|---|
| Russia | -23.5% | +20.5% | +31.9% | 1561 |
| China | -30.8% | -18.9% | -57.0% | 4 |
| Brazil | -49.0% | -36.6% | -20.7% | 2869 |
| Japan | -53.6% | -63.4% | -59.8% | 144 |
| India | -55.6% | -51.2% | -44.8% | 333 |
| United States | -59.6% | -29.6% | -13.2% | 2242 |
| Australia | -69.5% | -58.7% | -83.3% | 65 |
| *GLOBAL* | *-48.8%* | *-30.5%* | *-32.2%* | |

*Notes: declines are calculated using 2019 as the baseline*
*These seven countries accounted for 84% of global domestic RPKs in 2020*
*Source: Sobie Aviation, IATA, John Hopkins University (as of 25 October 2021)*

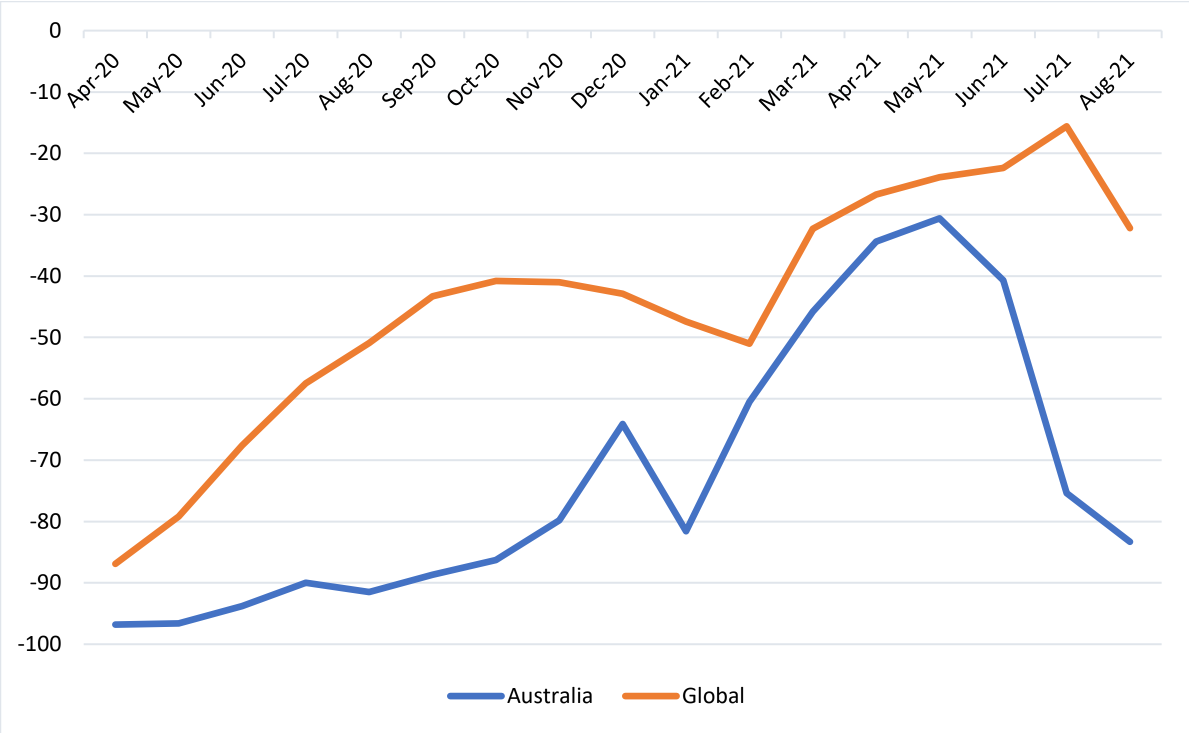
The 2020 figures are skewed as domestic traffic was relatively strong for most of the first quarter and only started to decline in February 2020 for China and late March 2020 for the other markets including Australia.

Monthly domestic RPK declines in Australia have ranged from a high of 97% in the first two full months of the pandemic, April and May 2020, to a low of 31% in May 2021 when all internal borders were open. Domestic RPKs were down by at least 80% every month until March 2021, when the internal border situation started to improve, but have dropped sharply since July 2021 as several borders reclosed.

Not surprisingly the gap between the Australia decline and the global average decline was the least in May 2021 – at a relatively modest 7 percentage points. The gap was also relatively modest in February, March, April and May before widening again in June as local travel restrictions started to tighten again. Sydney and Melbourne implemented a full lockdown in July which was not lifted until October.

The gap between the Australia decline and the global average decline reached 60 percentage points in July 2021, when global domestic RPKs was down only 15% while the decline in Australia was 75%. In August 2021 the gap was 51 percentage points, with a larger 83% decline for Australia but also a larger 32% decline for global domestic RPKs as China experienced a setback.

**Monthly scheduled domestic RPK growth (%) during pandemic: Australia vs global average**




*Note: Year-over-year growth is based on same month from 2019*
*Source: Sobie Aviation, IATA*

Australia was behind all five top global domestic markets (US, China, India, Japan and Brazil) every month from June 2020 to January 2021. During this eight-month period Australia had much better COVID containment than all these markets except China.

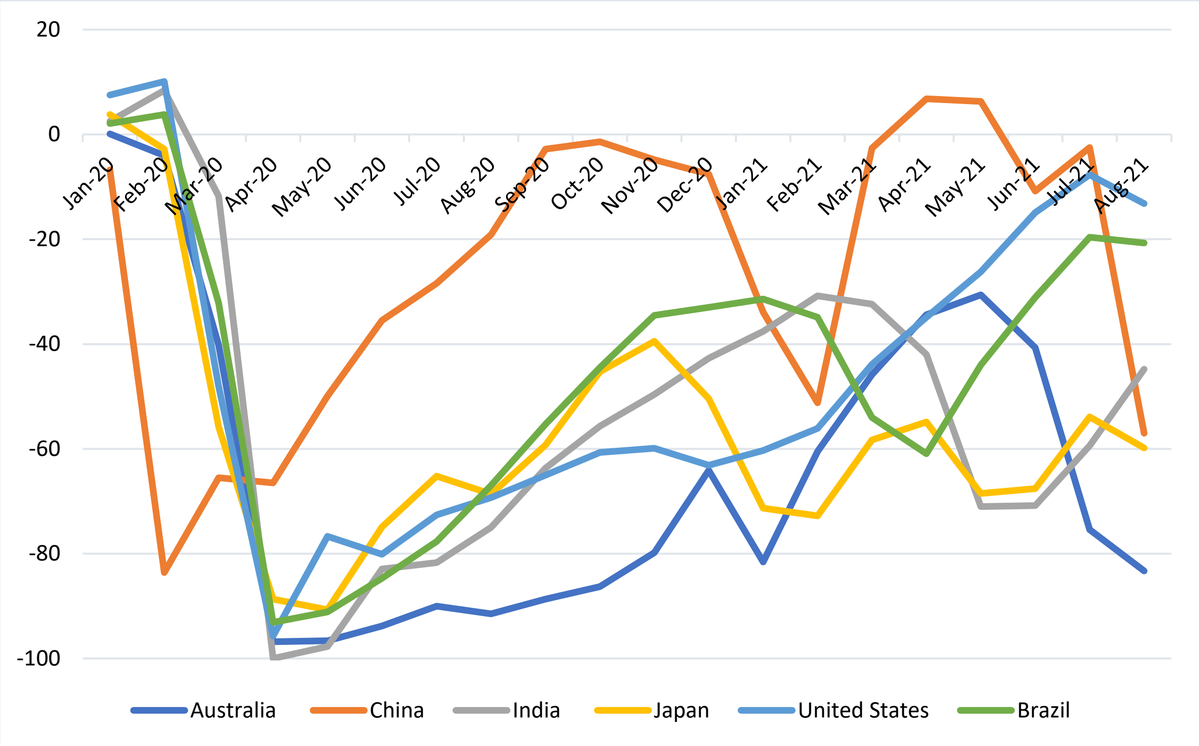
Australia was ahead of Brazil, India and Japan for a few months earlier this year. Australia has been behind the US every month except December 2020 and April 2021, when they had similar declines. Australia has been behind China every month since April 2020.

India has been a very resilient market despite high case numbers and has outperformed Australia every month except April and May 2021, when India was devastated by a record wave. Brazil has outperformed Australia every month except March, April and May 2021 while Japan has outperformed Australia every month except April, May and June 2021. All three of these markets again outperformed Australia in July 2021 and August 2021. This trend continued in September and October 2021 as Australia domestic traffic remained at roughly similar levels as August 2021 (although BITRE has not yet reported figures for the last two months).

The US has recovered rapidly in recent months and came close to reaching pre-COVID levels in the northern summer. The US also had a stronger initial recovery last year than Australia although it only reached 50% of pre-COVID levels for the first time in April 2021 – similar to Australia. The two markets have since diverged significantly.

China experienced a larger decline than Australia in February and March 2020 as the virus started in China, significantly impacting Chinese domestic traffic before COVID-19 was declared a global pandemic. China's domestic market has since recovered well despite some setbacks. China domestic traffic was close to pre-COVID levels in the fourth quarter of last year and exceeded 2019 levels in April and May 2021. Australia could have potentially achieved a similar trajectory if were not for internal politics and domestic border issues.

**Monthly domestic RPK growth (%): Australia vs top 5 domestic markets**



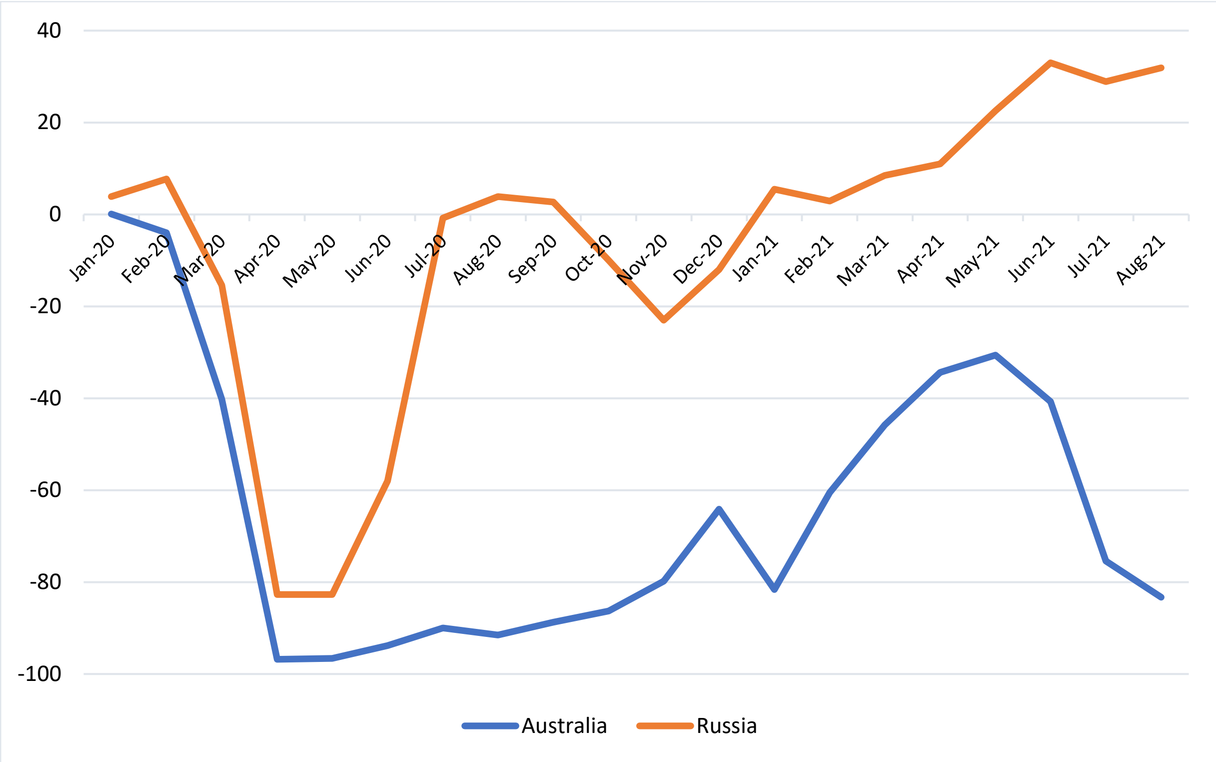

*Note: Year-over-year growth is based on same month from 2019*
*Source: Sobie Aviation, IATA*

Another relevant domestic market for comparison is Russia, which prior to the pandemic was similar in size to Australia. In the first 19 months of the pandemic Russia had about 24 times as many deaths per capita. But Russia's domestic market recovered rapidly and total scheduled passenger numbers in the first 19 months of the pandemic were down less than 10% compared to 73% for Australia.

Russia's domestic market was back to 2019 levels in the third quarter of 2020 and after a slight setback in the fourth quarter of 2020 it has been above 2019 levels every month so far in 2021. In recent months domestic RPKs in Russia were about 30% above 2019 levels.

The domestic growth in Russia is driven partially by more residents holidaying domestically as some borders have remained closed. Australia could have achieved similar domestic growth as Russia for the same reason, particularly in late 2020 and early 2021, if it were not for internal border closures.

**Monthly domestic RPK growth (%): Australia vs Russia**




*Note: Year-over-year growth is based on same month from 2019*
*Source: Sobie Aviation, IATA*

## Impact on interstate air travel

Domestic traffic in Australia was set back from late June 2021 through October 2021 by a new wave of cases driven by the more contagious Delta variant, which led to long lockdowns initially in Sydney and subsequently Melbourne and Canberra. All borders with Australia's two most populous states, New South Wales and Victoria, as well as with the Australian Capital Territory, were closed during this period. These closures and the resulting huge decline in domestic passenger traffic could have potentially been avoided with a faster vaccination rollout.

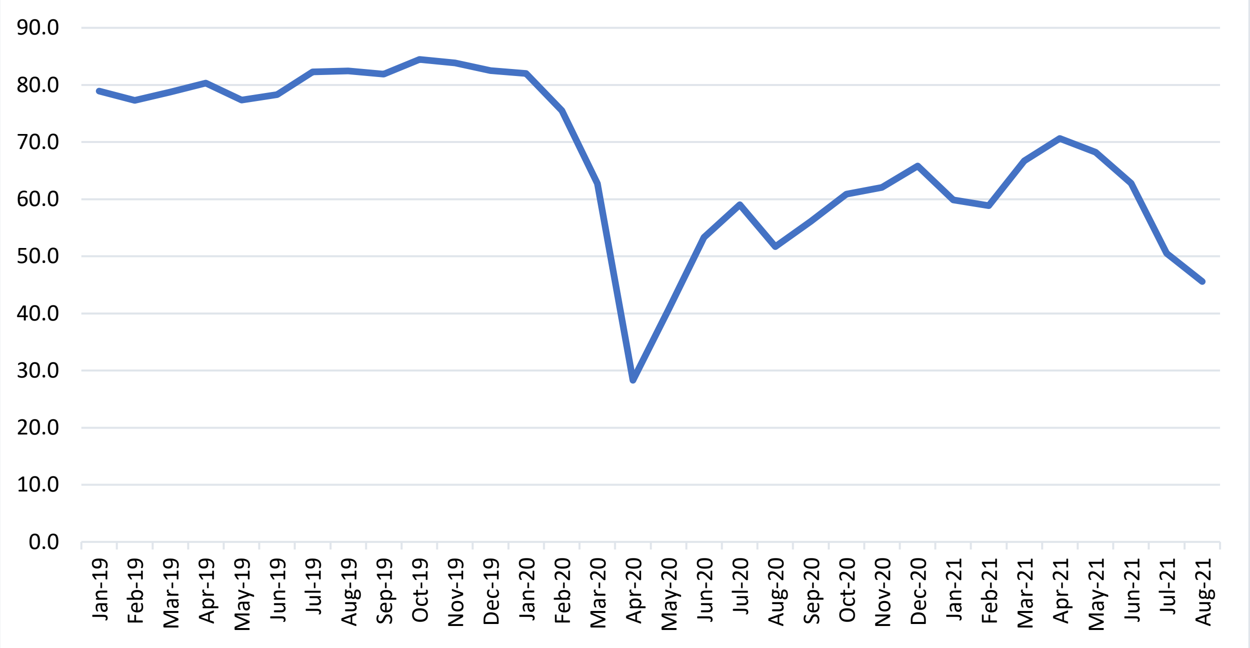
While Australia's vaccination rate has recently caught up with most developing countries and is now exceeding many developing countries, for several months it had one of the lowest vaccination rates in the developed world. With a faster vaccination rollout Australia could have potentially avoided the recent setback in domestic recovery or, at least, recovered much faster from the setback that began in late June. Other developed countries – such as the US and Canada – experienced a rapid domestic recovery earlier this year after successful vaccination rollouts.

In April and May 2021, Australia was on a track to achieve a full domestic recovery in the third quarter of 2021. Australia's carriers flew 5.685 billion scheduled domestic available seat kilometers (ASKs) in April 2021 and 5.756 billion scheduled domestic ASKs in May 2021, representing 79% and 80% of 2019 capacity respectively. All internal borders were open and demand was recovering with the average load factor exceeding 70% in May for the first time since the start of the pandemic. Airlines were bullish and planning to continue adding back domestic ASKs, which were projected to reach 2019 levels in the third quarter of 2021.

Instead ASKs instead plummeted in the third quarter and Australia will now have to wait until at least 2022 for domestic capacity to fully recover. Domestic capacity was at about one quarter of 2019 levels for most of the third quarter of 2021 as well as in October 2021. Traffic was even lower as all services touching New South Wales, Victoria or the Australian Capital Territory operated at very low load factors, carrying only essential traffic and supported with government subsidies.

The average domestic load factor slipped to only 45.6% in August 2021 (based on BITRE data), representing the lowest load factor since May 2020. The monthly domestic load factor has exceeded 70% only once since the start of the pandemic – in April 2021, when it was 70.7%. It has exceeded 60% on only six occasions.

**Monthly domestic passenger load factor: January 2019 to August 2021**




*Source: Sobie Aviation, BITRE*

Traffic within Queensland and Western Australia was relatively much stronger in the third quarter and in October as there was only brief lockdowns in parts of these states during this period. The border between Queensland and Western Australia was closed for most of this period but Western Australia kept its borders with the Northern Territory, South Australia and Tasmania open for most of this period, enabling travel with these states and territories. All the borders between Queensland and these three states also remained open during most of this period. However, these are all relatively small markets and demand was subdued as there was always the risk any state border could quickly shut.

With New South Wales and Victoria closed, all of Australia's largest routes have been limited to only essential traffic in recent months. Melbourne-Sydney was Australia's largest route and the world's second largest route (behind Seoul-Jeju) with 9.2 million RPT passengers in 2019. Brisbane-Sydney and Brisbane-Melbourne generated another 4.8 million and 3.6 million RPT passengers in 2019 respectively. The Brisbane-Melbourne-Sydney triangle alone accounts for 29% of total domestic traffic in Australia during normal times.

The remaining seven top 10 domestic routes (during normal times), all seven also touch New South Wales or Victoria: Sydney-Gold Coast, Melbourne-Adelaide, Melbourne-Gold Coast, Melbourne-Perth, Sydney-Adelaide, Sydney-Perth and Hobart-Melbourne. These seven routes account for another 24% of the market, resulting in a 53% share for the top 10.

All 10 of these routes have experienced RPT traffic declines above the market average in the first 17 full months of the pandemic (April 2020 to August 2021). The total decline was 82%, which is 10 percentage points higher than the market average of 72%. The Melbourne-Perth route had the largest decline, 89%, while the Melbourne-Gold Coast route had the smallest decline, 74%.

**Australia top 10 domestic routes based on RPT passenger traffic (millions): 17 months before the pandemic vs first 17 months of the pandemic**

| RANK | ROUTE | PRE-PANDEMIC | PANDEMIC | DECLINE |
|---|---|---|---|---|
| 1. | Sydney-Melbourne | 13.0 | 1.8 | 86% |
| 2. | Sydney-Brisbane | 6.8 | 1.3 | 81% |
| 3. | Melbourne-Brisbane | 5.1 | 0.9 | 83% |
| 4. | Sydney-Gold Coast | 3.8 | 0.8 | 80% |
| 5. | Melbourne-Adelaide | 3.6 | 0.6 | 83% |
| 6. | Melbourne-Gold Coast | 3.0 | 0.8 | 74% |
| 7. | Melbourne-Perth | 3.0 | 0.3 | 89% |
| 8. | Sydney-Adelaide | 2.7 | 0.6 | 77% |
| 9. | Sydney-Perth | 2.4 | 0.4 | 85% |
| 10. | Melbourne-Hobart | 2.3 | 0.5 | 80% |
| | ***TOTAL*** | ***45.6*** | ***8.0*** | ***82%*** |

*Notes: Rank is based on pre-pandemic passenger traffic*
*Decline is calculated using 2019 and five months of 2018 (April to August) as a baseline*
*Source: Sobie Aviation, BITRE*

The table above show the total decline rate for each route over the entire period. The monthly decline rates were particularly steep in the first eight months of the pandemic (April 2020 to November 2020) when state borders were mainly closed. The declines were generally more modest from December 2020 to March 2021 as borders were partially open although fragile with several snap lockdowns. The declines were the smallest in April 2021 to June 2021 when borders were fully open. In recent months, traffic on all 10 of these routes tumbled back to anemic levels similar to the first few months of the crisis due to closure of all borders with New South Wales, Victoria and the Australian Capital Territory.

## Impact on intrastate air travel

Intrastate routes have had much lower decline rates during the pandemic as they have not been impacted by state border closures although they are also obviously impacted when a state imposes a lockdown, leading to local travel restrictions.

Queensland and Western Australia intrastate routes have been particularly strong. These states generally have more and bigger intrastate routes than the other states or territories given their large geography. During the pandemic these states also have been under lockdown for significantly less time overall than New South Wales, Victoria or the Australian Capital Territory.

South Australia, Northern Territory and Tasmania also have had significantly less time under lockdown but have limited intrastate markets. These three states and territories are all small and combined account for only 10% of Australia's total population. New South Wales, Victoria and the Australian Capital Territory account for 60% of Australia's population while Queensland and Western Australia account for 30%.

Prior to the pandemic only three of Australia's top 20 domestic routes were intrastate: Brisbane-Cairns (number 11 overall), Brisbane-Townsville (number 14 overall) and Brisbane-Mackay (number 20 overall). These are all within Queensland.

The largest route within Western Australia, Perth-Karratha, was 29th overall prior to the pandemic. The largest route within New South Wales, Sydney-Ballina was 30th overall.

The largest route within Victoria, Melbourne-Mildura, was the 43rd largest domestic route in 2019. The largest route within South Australia, Adelaide-Port Lincoln, was 56th overall. These two routes are not among the top 10 intrastate routes in all of Australia.

The top 10 intrastate routes include four routes within Queensland, three within Western Australia and two within New South Wales. All these routes had at least 300,000 annual passengers prior to the pandemic and the largest, Brisbane-Cairns, had 1.3 million.

During the first 17 full months of the pandemic (April 2020 to August 2021), total traffic on these 10 routes declined by 42%, which is 30 percentage points higher than the overall domestic market decline and 40 percentage points higher than the 82% decline recorded by the top 10 interstate routes. The best performing intrastate route among the top 10 during this period was Sydney-Ballina, which experienced only a 14% decline.

Sydney-Ballina has benefitted from a surge in demand for holidays in Byron Bay, a popular beach down in northern New South Wales, particularly when travel within New South Wales was permitted but the border with nearby Queensland was still closed. For several months Sydney-Ballina experienced monthly traffic that was significantly higher than pre-COVID levels. Growth peaked at 51% in November 2020, when Sydney-Ballina was the fourth largest domestic route in all of Australia.

For several months Perth-Broome also experienced growth above pre-COVID levels. Perth-Brome growth has generally been more modest than Sydney-Ballina but Perth-Broome has continued to perform above pre-COVID levels in recent months while Sydney-Ballina was suspended due to the restrictions on travel in New South Wales. Therefore, Perth-Broome will assume the distinction of the best route for the entire pandemic period once September 2021 data is available.

Several other top 10 intrastate routes have experienced months where they were close to pre-COVID levels but have not posted any positive figures.

**Australia top 10 intrastate routes based on RPT passenger traffic (thousands): 17 months before the pandemic vs first 17 months of the pandemic**

| RANK | ROUTE (STATE) | OVERALL RANK | PRE-PANDEMIC | PANDEMIC | DECLINE |
|---|---|---|---|---|---|
| 1. | Brisbane-Cairns (QLD) | 11 | 1,855 | 1,027 | 45% |
| 2. | Brisbane-Townsville (QLD) | 14 | 1,455 | 759 | 48% |
| 3. | Brisbane-Mackay (QLD) | 20 | 1,095 | 581 | 47% |
| 4. | Brisbane-Rockhampton (QLD) | 27 | 761 | 384 | 50% |
| 5. | Perth-Karratha (WA) | 29 | 658 | 434 | 34% |
| 6. | Sydney-Ballina (NSW) | 30 | 604 | 518 | 14% |
| 7. | Perth-Port Hedland (WA) | 31 | 537 | 342 | 36% |
| 8. | Perth-Newman (WA) | 33 | 484 | 299 | 38% |
| 9. | Perth-Broome (WA) | 34 | 484 | 406 | 16% |
| 10. | Sydney-Coffs Harbour (NSW) | 35 | 465 | 117 | 75% |
| | ***TOTAL*** | | ***8,399*** | ***4,868*** | ***42%*** |

*Notes: Overall rank is for all domestic routes (interstate and intrastate)*
*Ranks are based on pre-pandemic passenger traffic*
*Decline is calculated using 2019 and three months of 2018 (April to June) as a baseline*
*Source: Sobie Aviation, BITRE*

The next 10 largest intrastate routes also have performed relatively well during the pandemic but on a smaller base. These include another three routes within Queensland (Brisbane to Proserpine, Gladstone and Emerald), five within New South Wales (Sydney to Albury, Port Macquarie, Dubbo, Tamworth and Wagga Wagga), one within Western Australia (Perth to Kalgoorlie) and one within Victoria (Melbourne to Mildura). These routes generated between 170,000 and 280,000 annual scheduled passengers prior to the pandemic.

Brisbane-Proserpine has done particularly well with traffic above pre-COVID levels in recent months. Brisbane-Hamilton Island has been the strongest intra-Queensland route, with traffic significantly above pre-COVID levels, but is smaller and further growth is constrained due to a lack of hotels on Hamilton Island. Brisbane-Hamilton Island was the 25th largest intrastate route prior to the pandemic with 132,000 annual passengers. In the 12 months ending August 2021 this route generated nearly 200,000 passengers.

Intrastate routes overall have dominated for most of the pandemic as state borders have been closed more than open. Internal border closures are unique to Australia and have significantly hampered the ability of the domestic market to recover.

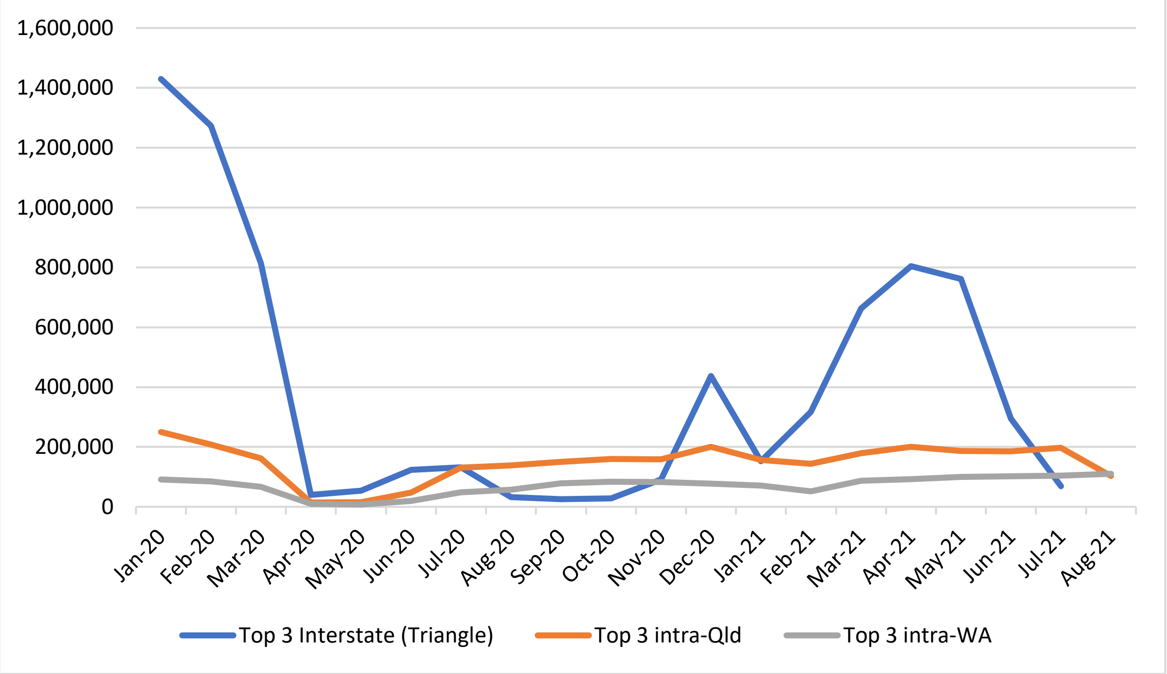
Prior to the pandemic the Brisbane-Melbourne-Sydney triangle generated 1.4 to 1.6 RPT million passengers per month. During the pandemic there has been only two months that traffic has exceeded 50% of pre-COVID levels.

In comparison the top three intrastate routes (Brisbane to Cairns, Townsville and Mackay) exceeded 50% of pre-COVID levels every month from July 2020 to July 2021. They were at about 40% of pre-COVID levels in August 2021 due to a lockdown in the Brisbane area during the first part of August but have since been closer to pre-COVID levels. Prior to the pandemic, these routes combined generated 200,000 to 300,000 passengers per month or about one sixth of the traffic generated by the top three interstate routes.

The top three intrastate routes in Queensland generated more traffic than the top three interstate routes for four months of 2020 (August to November) and again in January 2021. They again generated more traffic than the top three interstate routes in July and August 2021, a trend which continued in September and October although data is not yet available for these months.

The top three intrastate routes in Western Australia generated more traffic than the top three interstate routes in three months of 2020 (August to October) and again in July and August 2021, a trend which continued in September and October.

**RPT passenger traffic for top 3 interstate routes combined vs top 3 intra-Queensland and top 3 intra-Western Australia routes: January 2020 to August 2021**




*Note: August 2021 data for Top 3 Interstate route routes not available but was negligible*
*Source: Sobie Aviation, BITRE*

## The impact on airlines and the overall market

While intrastate routes have helped provide airlines with some revenues during the crisis, restricting all the major interstate routes to all but essential traffic for most of the pandemic has had a devastating impact. Some of the impact was unavoidable, particularly the initial couple of months when virtually the entire world was in lockdown. However, much of the impact since June 2020 could have been avoided by keeping internal borders open and – in more recent months – with a faster vaccination rollout.

Without the pandemic, the Melbourne-Sydney route alone would have generated 14.5 million RPT passengers over the 19-month period from April 2020 to October 2021. Instead, this key route generated less than 1.9 million passengers for a reduction of 87%.

A relevant comparison is Seoul-Jeju, which prior to the pandemic was the only route in the world that was larger than Melbourne-Sydney. The total traffic reduction for Seoul-Jeju over the same 19-month period was only about 10%. Seoul-Jeju traffic has been above 2019 levels most months so far this year.

While some of the 87% reduction on Melbourne-Sydney was obviously unavoidable, under different political circumstances the route could have performed more similar to Seoul-Jeju or other large domestic routes in countries that had relatively low COVID-19 case numbers. A 10% reduction may have been difficult to achieve but a 30% reduction could have been feasible, resulting in over 8 million more passengers and a couple of billion dollars in revenues.

For the top 10 domestic routes combined there has been a reduction of 84% or about 43 million passengers for the first 19 months of the pandemic. If the reduction was 30%, there would have been over 27 million additional passengers, generating several billion dollars in additional revenues.

Australian carriers lost about AUD16 billion in domestic revenues in the first 19 months of the pandemic (April 2020 to October 2021). While government support packages and subsidies offset some of the revenue reductions, airlines have been significantly impacted by the sharp decline in domestic passenger traffic along with thousands of companies in the broader aviation and travel sectors.

Domestic air transport and tourism has recovered rapidly in many countries. Unfortunately, this has not been the case in Australia.

# DOMESTIC MARKET OUTLOOK: REMAINDER OF 2021

The domestic market is again starting to recover. Traffic for November 2021 will likely be only slightly improved compared with the previous four months but in December 2021 could reach April and May 2021 levels.

New South Wales and Victoria lifted intrastate travel restrictions in early November but this will only generate a relatively modest volume of additional domestic passenger traffic. The reopening of the New South Wales-Victoria border will have a more significant impact as it will enable Melbourne-Sydney traffic to start recovering in the second half of November. Several smaller routes connecting New South Wales, Victoria and the Australian Capital Territory will also start recovering by the end of November.

Leisure destinations such as Ballina/Byron Bay and Coffs Harbour in northern New South Wales will be particularly popular – from both Sydney and Melbourne. But low vaccination rates in some regional destinations such as Byron Bay is a concern and could impact the recovery of some routes.

By the end of the year domestic traffic could reach 70% of pre-COVID levels. But this is contingent on all states and territories reopening their internal borders except for Western Australia, which is expected to remain closed until at least early 2022.

Northern Territory and South Australia plan to reopen internal borders on 23 November followed by Tasmania on 15 December and much larger Queensland on 17 December. These four states/territories have generally been open to each other the past few months – with some brief closures – but have not been open to New South Wales, Victoria or the Australian Capital Territory.

If all the internal border re-openings occur as planned, there will be quarantine free domestic travel by Christmas for all of Australia except Western Australia. However, there could be setbacks, making it far from certain all interstate domestic travel across seven of Australia's eight states and territories will resume by Christmas.

During the pandemic many times states have reclosed borders or delayed planned re-openings with little or no notice. While the reopening this time is intended to be permanent and is part of a national plan, a spike in cases or hospitalizations could prompt some of the states to reconsider their border strategies. The border situation remains tenuous and some passengers will lack the confidence to plan interstate travel until it is clear there will be no more flipflopping or sudden closures.

Even if there are no setbacks, the recovery will be modest until the last couple weeks of the year. Therefore, the impact on domestic figures for 2021, and even fourth quarter 2021, will be relatively small.

Given the current outlook for the last two months of the year, the total impact of the pandemic on the overall domestic market will reach 77 million passengers at the end of 2021. This equates to a reduction of 71% in scheduled or RPT traffic the first 21 months of the pandemic (April 2020 to December 2021).

With a 71% reduction in scheduled domestic passenger traffic for first 21 months of the pandemic, the revenue impact on Australian carriers will exceed AUD17 billion. The impact on other companies in the aviation and travel sectors also cannot be underestimated. Prior the pandemic, domestic overnight visitor spend was about AUD78 billion per year and total overnight trips was 113 million or an average of more than four per person (based on Tourism Research Australia data). During the pandemic, the reduction in overnight visitor spend has already exceeded AUD60 billion and there has been nearly 100 million fewer domestic overnight trips. There are more than 300,000 tourism related businesses in Australia with about 600,000 employees.

Interstate domestic tourism has particularly been impacted due to the border closures and has accounted for most of the reduction in domestic overnight visitor spend. This has had a disproportionate impact on aviation as the more resilient intrastate market relies more on road than air.

In the current quarter ending December 2021, Australia will once again have the distinction of having the world's most impacted major domestic air transport market. Even if Australia achieves 70% of pre-COVID domestic traffic in the last two weeks of the year this will be less than almost all other major domestic markets. While the outlook is finally starting to improve, the gap between Australia and the rest of the world continues to widen.

# DOMESTIC MARKET OUTLOOK: 2022 AND BEYOND

Australia's domestic air transport market should enjoy a more meaningful recovery in 2022. But this is contingent on all states reopening borders, including Western Australia, and keeping all of the borders open. Any setbacks or delays will cause further damage to Australia's battered aviation industry.

Vaccination rates have accelerated significantly in recent months, enabling a reopening of the domestic market. All states and territories should reach an 80% vaccination rate for adults (16+), the threshold for permitting interstate travel, by the end of 2021. Western Australia will be the last state to reach this threshold, likely in late December, but has announced it will wait until 90% of the population aged 12 and over is vaccinated before reopening. While this is tentatively expected in late January or early February 2021 there is still uncertainty and Western Australia could further delay its reopening, preventing a full recovery of the domestic market. It is also unclear if all the other states and territories will keep borders open, particularly if there is a spike in cases or hospitalizations.

Even under the best-case scenario it will be April 2022 before domestic traffic finally returns to 2019 levels. It is possible domestic traffic will not fully recover until late 2022 or even 2023.

Australia could be one of the last domestic markets to fully recover. Domestic politics has so far been a major impediment. There is a risk the political issues that have so far made it so difficult for interstate domestic air travel and tourism will linger.

Australia could essentially be split into two – with virtually no travel between the two parts – for several more months. Such a scenario is unfortunate as it separates families and friends. Economically there are also consequences, particularly for the aviation and travel sectors.

Eventually Australia will reunite and keep internal borders open permanently. But it could be several months before this is achieved. The impact on airlines and the damage to the broader economy will be massive with potential long-term ramifications.

All of Australia needs to move on from COVID zero strategies and quickly transition as a single country to living with COVID. Domestic travel is critical for the overall economy and the well-being of Australian residents. The domestic air transport market is capable of fully recovering in 2022 but only with the right policies and more favorable political conditions.

# IMPACT ON THE INTERNATIONAL MARKET

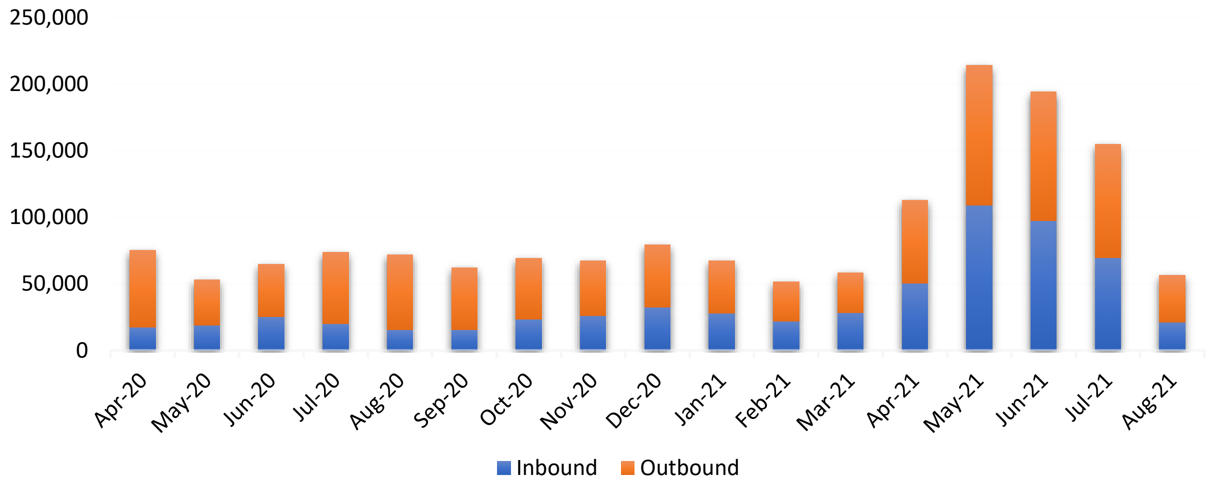
Australia's international market also has been more impacted and recovered more slowly than the global average. While the gap between Australia and the rest of the world in terms of international traffic is much narrower than the gap for domestic traffic it has been widening in recent months and Australia could become one of the last international markets to fully recover.

In the first 17 months of the pandemic (April 2020 to August 2021) only 1.53 million scheduled international passengers flew to and from Australia. This represents a decline of 97.5% compared with the equivalent 17 months prior to the pandemic (based on BITRE data).

The international market was stalled at about 2% of normal traffic levels in the first 12 months of the pandemic (April 2020 to March 2021), when monthly traffic ranged from 51,000 to 75,000 passengers or 97.9% to 98.5% below 2019 levels. The month-to-month variation was driven by frequent changes in the government-imposed cap on international arrivals, which made it impossible for all Australians stranded abroad to repatriate.

There has not been any cap on outbound travel, which has been relatively stronger than the inbound segment for most of the pandemic but still at anemic levels. Outbound demand was constrained until 1 November 2021 by a controversial policy that did not allow Australian residents from departing without applying for and securing a special exemption to travel overseas. This limited the outbound market to mainly essential traffic or one-way traffic, including visitors that were stranded in Australia at the beginning of the pandemic.

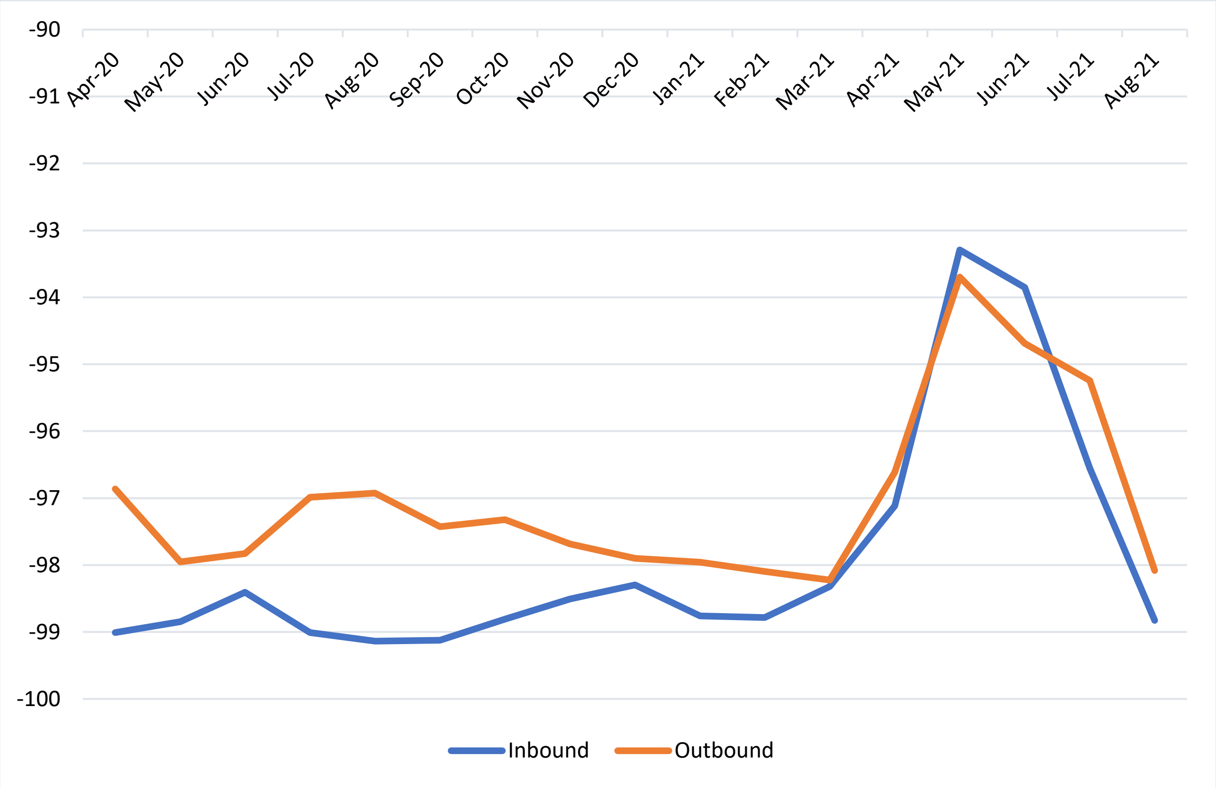
**Monthly scheduled international passenger traffic: April 2020 to August 2021**




*Source: Sobie Aviation, BITRE*

In the first 12 months of the pandemic (April 2020 to March 2021), outbound scheduled international passenger traffic declined by 97.6% while inbound international traffic was down by a steeper 98.8%. The monthly inbound decline ranged from 96.9% to 98.2% while the monthly outbound decline ranged from 98.3% to 99.1%.

**Monthly scheduled international passenger traffic growth (%): April 2020 to August 2021**




*Note: 2019 is used as the baseline for all 16 months*
*Source: Sobie Aviation, BITRE*

## Impact of the Trans-Tasman bubble

International traffic improved in the April 2021 to July 2021 period – both inbound and outbound – due to the air travel bubble with New Zealand. For the first 17 months of the pandemic (April 2020 to July 2021), the outbound international decline was therefore a slightly more moderate 97.0% and the inbound international decline was 98.0%.

The Australia-New Zealand bubble permitted two-way quarantine free travel across the Tasman from 19 April 2021 until it was suspended on 23 July 2021. Australia began permitting one-way quarantine free travel from New Zealand much earlier, in October 2020, but there was very limited demand as New Zealand did not initially reciprocate. There were less than 10,000 monthly Australia-New Zealand passengers during the one-way bubble while the two-way bubble resulted in monthly passenger traffic peaking at above 150,000.

In May 2021 and June 2021, there was a larger decline in monthly outbound international traffic than inbound for the first time since the start of the pandemic. This was partially due to stronger inbound traffic on the Trans-Tasman bubble than outbound. The difference between inbound from New Zealand and outbound to New Zealand was much more pronounced in late 2020 and early 2021 due to the one-way bubble, leading to a reduction in the gap between total inbound and total outbound international traffic, but this only had a slight impact as the one-way bubble volumes were very low.

In the three months it was active, the two-way Trans-Tasman bubble experienced several partial suspensions affecting certain but not all states in Australia. The temporary setbacks and fragile nature of the bubble dented demand as many potential passengers were concerned they would be stranded or required to quarantine on return. Australia-New Zealand passenger traffic was still down by 69% in May 2021 compared to May 2019 and by 72% in June 2021 compared to June 2019.

However, the Trans-Tasman bubble still had a positive impact on international traffic, generating about 400,000 additional passengers for Australia during the three months it was in place. As a result, total monthly scheduled international passenger traffic increased to 214,000 passengers in May 2021 and 194,000 passengers in June 2021, resulting in more modest declines compared to 2019 of 93.5% and 94.3%. In April and July there was also an impact but not as significant because the Trans-Tasman bubble was only in place parts of these months.

New Zealand accounted for nearly 78% of total international traffic in May 2021, the first full month of the Trans-Tasman bubble, and 74% in June 2021. In March 2021, the last full month before the bubble started, New Zealand accounted for only 17% of total international traffic.

New Zealand was Australia's largest international market prior to the pandemic, accounting for 17% of international passenger traffic (based on BITRE data for 2019). Singapore was second largest, accounting for 14%. China, the United Arab Emirates, Indonesia and the US were the next largest markets, each accounting for about a 4% share of the total.

## Impact on foreign airlines

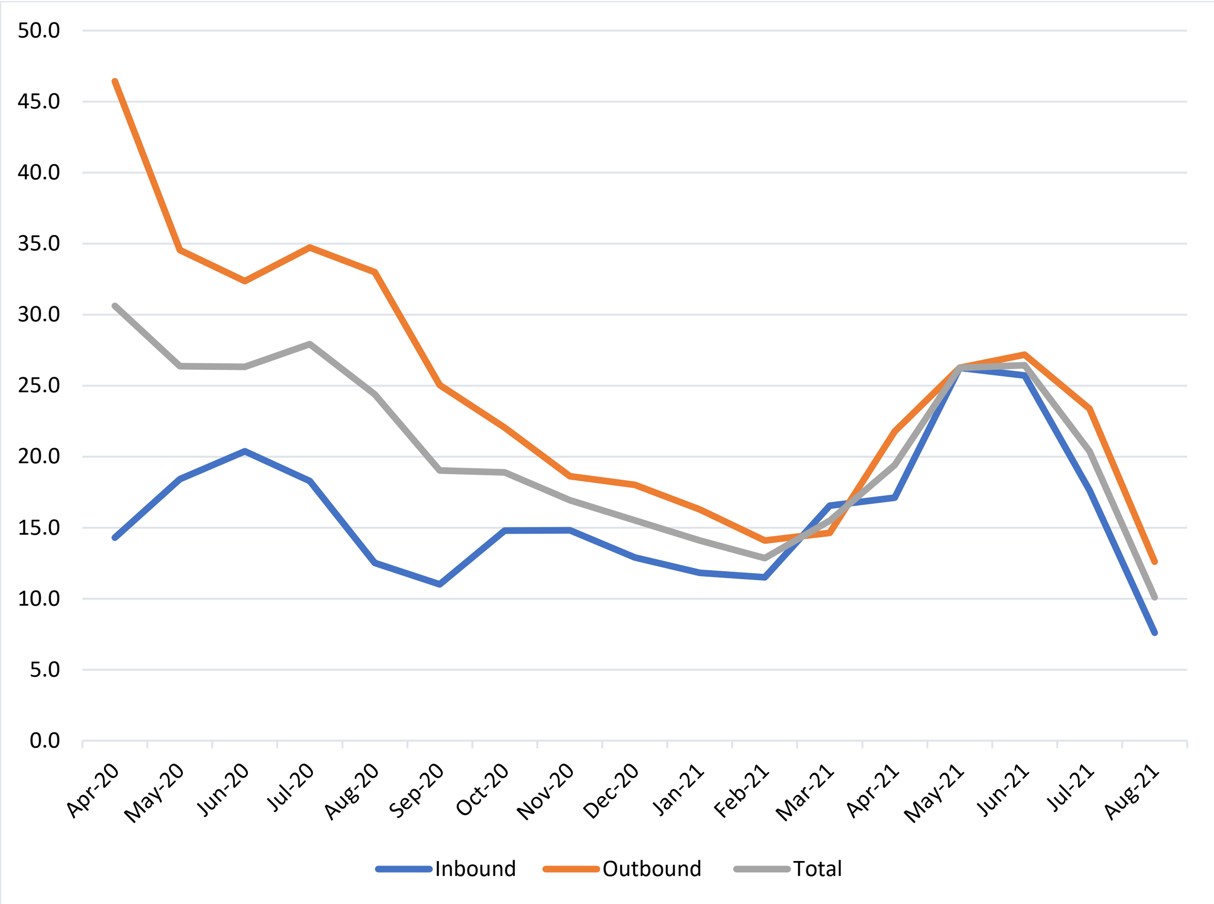
Singapore Airlines (SIA) was the largest foreign airline in Australia prior to the pandemic, accounting for 8.3% of total international traffic in 2019 followed by Emirates and Air New Zealand, which each accounted for a 6.8% share. The fourth largest foreign airline in 2019 was Cathay Pacific with a 4.5% share followed by China Southern with a 3.1% share, Qatar Airways with a 3.0% share and Malaysia Airlines with a 2.0% share. Foreign airlines overall accounted for a 67% share.

Of the three international carriers in Australia, Qantas is the largest with a 17.4% share of total international traffic in 2019 followed by Jetstar Airways with 8.7% and Virgin Australia with 6.7%.

During the pandemic foreign carriers have increased their market share although on an extremely low base. Australian carriers did not operate any scheduled international services from April 2020 through October 2021 with the exception of New Zealand as travel restrictions, particularly the strict cap on inbound arrivals, made scheduled flights commercially unviable. However, Qantas operated special repatriating flights were arranged by the Australian government. These are not counted in the BITRE data as they are not scheduled services.

Several of the foreign airlines that served Australia prior to the pandemic suspended scheduled services in March 2020. Those that continued to operate or resumed services (in some cases on a sporadic basis) have endured extremely low load factors. In the first 17 months of the pandemic (April 2020 to August 2021), the average seat load factor on scheduled international flights was only 20.2%. This includes an average inbound seat load factor of 16.9% and an outbound seat load factor of 23.3%. In 2019 the average international seat load factor was 81.3%

**Monthly international seat load factor (seat utilization %): April 2020 to August 2021**




*Source: Sobie Aviation, BITRE*

Both the inbound and outbound seat load factor improved slightly while the Trans-Tasman bubble was in place. The average seat load factor for bubble flights was above 50% but still well below the pre-pandemic average.

Cargo has provided some revenues but scheduled passenger services have generally been highly unprofitable due to the very low load factors. There have also been charter flights by several foreign airlines, including some airlines that did not operate to Australia previously.

In the first 17 months of the pandemic (April 2020 to August 2021), Air New Zealand was the largest foreign airline, carrying 407,000 passengers and accounting for 27% of the total. But this is skewed by the Trans-Tasman bubble as 304,000 of these passengers were carried during the months the two-way bubble was in place (April 2021 to July 2021). In the first 12 months of the pandemic (April 2020 to March 2021), Qatar Airways was the largest followed by Air New Zealand, Singapore Airlines (SIA) and Emirates.

In the first 17 months of the pandemic (April 2020 to August 2021), Qatar Airways carried 226,000 passengers to and from Australia or 15% of the total. While Qatar has jumped five places in the rankings, from sixth prior to the pandemic to second during the pandemic, this is relative. In 2019, Qatar's Australia operation needed only two months to carry 226,000 passengers.

SIA has been the second largest foreign airline during the pandemic, carrying 131,000 passengers over the same 17 moths and 9% of the total. SIA had an almost even inbound/outbound mix with 63,000 passengers inbound compared to 68,000 outbound while Qatar has been heavily focused on the outbound segment, which has accounted for 150,000 passengers compared to 76,000 inbound.

Qatar had a much larger operation than SIA in the initial seven months of the pandemic (April 2020 to October 2020), carrying 6.5 times more passengers than SIA during this period. Over the following 10 months (November 2020 to August 2021), SIA was slightly larger.

Emirates carried only 91,000 passengers to/from Australia in the first 17 months of the pandemic. Unlike Qatar or SIA, Emirates has not maintained services to Australia throughout the pandemic. In recent months Emirates has continued to carry significantly less than Qatar and SIA but significantly more than any other foreign airline (excluding Air New Zealand).

Several other foreign airlines have operated scheduled services to Australia during the pandemic. However, many of these services have not been regular and some were suspended entirely after the arrival cap was halved in mid-July 2021. In August 2021, Air New Zealand, Emirates, Qatar and SIA were the only airlines that carried more than 3,000 passengers in the international market.

## The impact on Australia's carriers

New Zealand was the only destination that Australian carriers have operated scheduled international services to during the first 19 months of the pandemic (April 2020 to October 2021). Qantas carried 142,000 passengers to and from New Zealand in the first 17 months of the pandemic (April 2020 to August 2021) with 137,000 of these carried in the April 2021 to July 2021 period when the Trans-Tasman bubble was in place. Jetstar carried 43,000 over the 17-month period, including nearly 40,000 in the April 2021 to July 2021 period. Virgin Australia has not operated any international services during the pandemic but was planning to resume New Zealand September 2021 before the Trans-Tasman bubble was suspended.

The inability to operate scheduled passenger services, with the partial exception of New Zealand, has had a huge impact on Australia's main carriers. Prior to the pandemic Australian carriers generated more than AUD10 billion in international revenues per annum, led by Qantas with more than AUD7 billion. While cargo and charters has provided somewhat of a lifeline, international revenues during the pandemic have dropped to less than AUD2 billion per year.

The pandemic has so far cost Australian carriers about AUD13 billion in international revenues and 21 million passengers (based on the first 19 months on the pandemic).

## Comparing Australia with other international markets

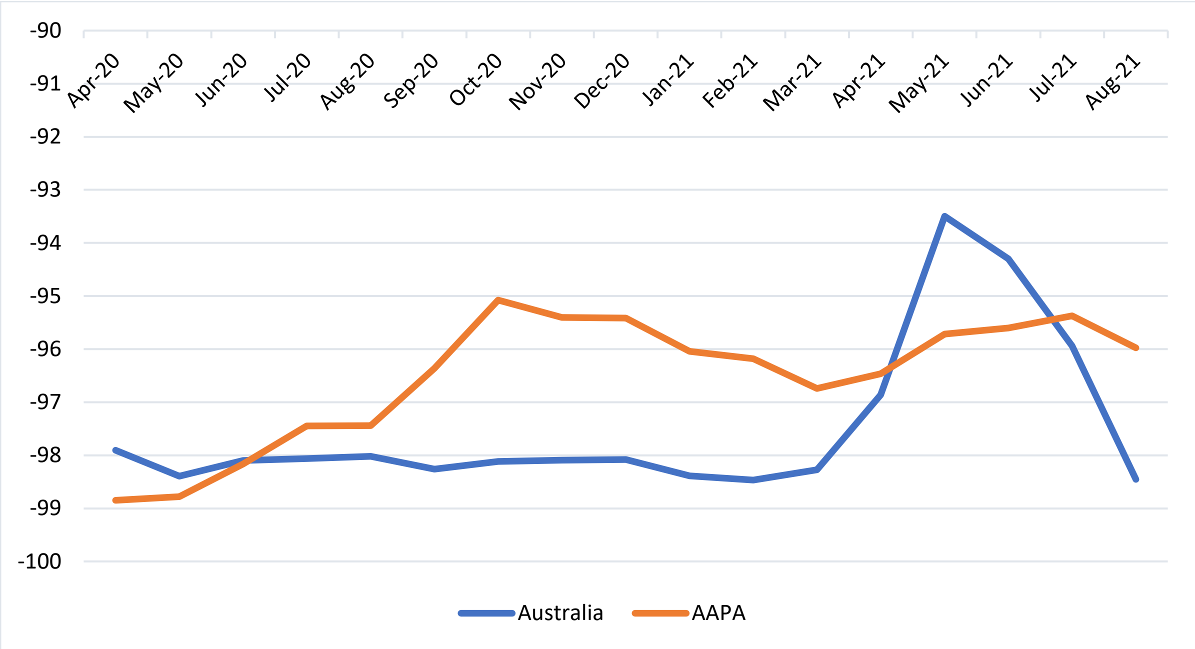
Unlike the domestic impact, most of the international impact can be considered unavoidable. Globally, the rate of international passenger traffic recovery has been very slow and much slower than domestic. But Australia's international market has performed worse than the global average throughout the crisis due to the cap on arrivals and policies blocking most citizens from departing. It also has performed worse than the Asia Pacific average with the exception of April to June 2020 as well as May and June 2021.

In the first three months of the pandemic, Australia had a slightly lower decline than the Asia Pacific average due to relatively strong outbound demand as visitors stranded in Australia returned home. In May and June 2021, the short-lived Trans-Tasman bubble enabled Australia to perform ahead of the Asia Pacific average but Australia was still well below the global average.

The overall Asia Pacific decline in international passenger traffic has been at least 95% every month since the start of the pandemic. Australia's decline was about 94% while the Trans-Tasman bubble was in place but in other months has been about 98%.

The overall Asia Pacific figure is reported by the Association of Asia Pacific Airlines (AAPA) and based on the combined international passenger traffic for 40 leading Asia Pacific airlines. All three of Australia's international carriers – Jetstar, Qantas and Virgin Australia – are among the 40 carriers included in the AAPA data although they are not AAPA members.

**Monthly international passenger traffic growth (%) for Australia vs all of Asia Pacific**




*Note: 2019 is used as a baseline for both 2020 and 2021*
*Source: Sobie Aviation, BITRE, AAPA*

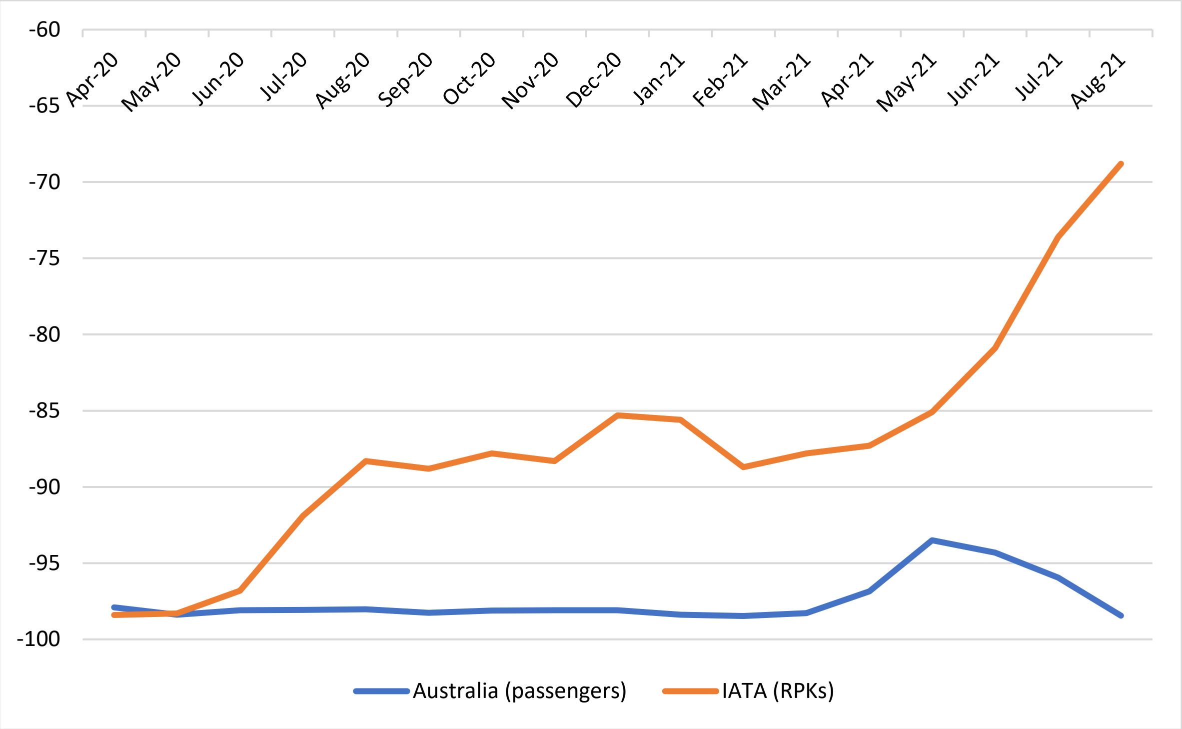
In the first 17 months of the pandemic (April 2020 to August 2021) the overall AAPA decline in international passenger traffic was 96.5% while Australia's decline was 97.9%. Asia Pacific carriers combined carried 18.9 million scheduled international passengers during this period with the Australian carriers accounting for only 1% of this traffic or 185,000. Prior to the pandemic Australian carriers accounted for 3.6% of the total scheduled international traffic carried by Asia Pacific carriers (13.9 million of a total 383.5 million in 2019).

Global international passenger traffic has started recovering and has been down by about 70% in recent months as borders have reopened in other regions. In August 2021 IATA reported a 68.8% reduction in international RPKs, representing the first time since the start of the pandemic the global decline was less than 70%. The gap between Australia and the global average has gradually widened as other international markets have reopened.

IATA does not report monthly international passenger numbers but reports scheduled international RPKs while BITRE only reports scheduled international passenger numbers.

In the first eight months of 2021, the global scheduled international RPK decline compared with 2019 was 81.6% while in Australia the scheduled international passenger decline was 96.8%. In September and October 2021, Australia's decline reaccelerated while the global decline continued to moderate (data for these months was not yet available as of the end October when this paper was completed).

**Monthly international passenger/RPK growth, Australia/global: April 2020 to August 2021**




*Note: 2019 is used as a baseline for both 2020 and 2021*
*Source: Sobie Aviation, BITRE, AAPA*

# INTERNATIONAL MARKET OUTLOOK: REMAINDER OF 2021

The Australian government lifted its controversial outbound travel ban on 1 November 2021. Each state and territory is able to lift the cap on arrivals and quarantine requirements once 80% of its adult population (16+) is fully vaccinated. New South Wales and Victoria reached this threshold in October 2021 and decided to lift the cap on international arrivals as well as quarantine requirements as of 1 November 2021, leading to an increase in international flights from Sydney and Melbourne. Unvaccinated international travelers (as well as travelers with unverified vaccinations) are still required to quarantine and are subject to small caps – 210 per week in New South Wales and 250 per week in Victoria.

Queensland, South Australia, Northern Territory and Western Australia are not following New South Wales and Victoria in eliminating quarantine when they reach the 80% threshold. Instead they plan to require home quarantine for vaccinated international arrivals, starting in late November for South Australia and in December for Queensland and Northern Territory. Home quarantine represents an improvement over the current hotel quarantine requirement and strict caps on arrivals. However, imposing home quarantine will significantly limit demand for international services at Brisbane, Adelaide and Darwin for at least the remainder of this year.

There will also be limited demand for international services at Perth as Western Australia until at least February 2021. Unlike the other states, Western Australia has not yet provided a timeframe on when or if it will lift quarantine requirements. It will be the last state to reopen and transition from a COVID zero strategy. Western Australia may not even permit home quarantine when it reaches 80%, which is expected in late December.

Tasmania is lifting quarantine for all arrivals – both domestic and international – from 15 December but this will not have a significant impact on the overall market given its small size. Tasmania did not have any international services prior to the pandemic and its residents typically travel via Melbourne or Sydney, which have already reopened.

Quarantine for Australia Capital Territory residents, who also typically travel via Melbourne or Sydney, ended on 1 November. Canberra had very limited international services prior to the pandemic and it is also a very small market.

Australia's international passenger traffic will start to increase in November and December, driven by Melbourne and Sydney. Most of the additional passengers will be carried by foreign airlines, enabling an improvement in the paltry load factors they have endured since the start of the pandemic. Emirates, Singapore Airlines and Qatar Airways will likely benefit the most as they already had the most capacity in the Sydney and Melbourne markets.

Some foreign airlines are planning to add flights in November or December while some of those that suspended their Australia routes are planning to resume services before Christmas. But the increase in demand may not be sufficient for foreign airlines to add a significant number of flights, particularly given that almost all international visitors are still not allowed to enter Australia.

Qantas, Virgin Australia and Jetstar are also resuming scheduled international services. However, Australian carriers will capture a relatively small share of the market for the remainder of this year as it will take time to restore their networks.

Qantas resumed flights from Sydney to London (with a stop in Darwin) and Los Angeles on 1 November. These flights represent the first scheduled international flights for Qantas – except New Zealand – since March 2020.

Qantas Group also has announced the resumption of flights from Melbourne and Sydney to Singapore from 22 November 2021 and from Melbourne to London (with a stop in Darwin) from 27 November. In December 2021, Qantas Group is planning to resume flights from Sydney to Fiji, Honolulu and Vancouver, from Melbourne to Los Angeles and from Darwin to Singapore. Some of the Fiji and Singapore flights will be operated by Jetstar. Qantas is also planning to launch in December a new route from Sydney to Delhi (with a stop in Darwin in the outbound direction only) contingent on Indian government approvals.

The resumption of several scheduled services from Qantas is an important step in the recovery of Australia's international market. However, the impact on 2021 international passenger traffic will be relatively small as there will initially be a limited number of flights and destinations.

Virgin Australia is only planning to resume one international destination, Fiji, by the end of the year. The resumption of other international destinations – for Virgin Australia as well as Qantas and Jetstar – are not planned until 2022.

Fiji Airways is also resuming Australia-Fiji services to coincide with the 1 December reopening of Fiji. While there is pent-up demand for two-way quarantine free travel to Fiji, competition is fierce between the four airlines in this market and overcapacity is possible.

Other destinations in the South Pacific could follow Fiji in opening up but this is unlikely to happen until 2022. The Trans-Tasman bubble – or another scheme permitting two-way quarantine free travel between Australia and New Zealand – is also not likely to resume until 2022.

While the elimination of quarantine requirements in New South Wales and Victoria will improve demand, many residents will still be hesitant to travel overseas due to the cumbersome requirements, costs and stress related to international travel. The possibility of quarantine requirements changing when overseas could also dent demand. Similar to the domestic border issues it is possible home or even hotel quarantine requirements can be re-imposed.

For the last two months of this year, Australia's international air transport market will still be a small fraction of pre-COVID levels and significantly behind most other major international markets. The total international market impact of the pandemic on Australian carriers will likely exceed AUD14 billion and 22 million passengers by the end of 2021. When including foreign airlines, the impact will exceed 73 million international passengers.

# INTERNATIONAL MARKET OUTLOOK: 2022 AND BEYOND

The pace of the recovery will gradually pick up in 2022 and beyond but Australia risks lagging well behind the global average for potentially several years.

The biggest concern is Australia's attractiveness as a destination. Other parts of the world have started to travel overseas again and rediscover international tourism while Australia has kept its borders sealed.

The initial phase of Australia's reopening of borders only includes citizens, permanent residents and their immediate families. The federal government has not yet announced a date for opening to visitors with the exception of vaccinated Singapore citizens, whom are permitted to travel quarantine free to New South Wales and Victoria from 21 November. New Zealand residents who are fully vaccinated are also now able to again enter New South Wales and Victoria without quarantine but this is moot as there is no date yet for reestablishing two-way quarantine free travel with New Zealand.

Any early attempt by a state to open up to all international visitors is likely to be overruled by the federal government. This is what happened on 15 October when New South Wales stated it would open to visitors at the same time as opening up international travel for residents only to be overruled by Canberra.

Once Australia lifts restrictions on visitors it is uncertain if quarantine requirements will be waived. Even if only some states require quarantine for visitors, it will impact Australia's overall ability to attract visitors and recover tourism. Any home quarantine requirement would result in hotel quarantine for visitors as they do not have their own accommodation. This is costly and will dissuade virtually all travelers. So far during the pandemic tourists have almost always avoided countries with any quarantine requirements and instead decide to travel to countries that do require any quarantine. Australia therefore will not be competitive with other destinations if quarantine is required.

Inbound is a huge segment and a much larger source of overall revenue for Australia's travel industry than outbound. In 2019, visitors accounted for 43% of total international passenger traffic. International visitors spent about AUD45 billion per year in Australia prior to the pandemic (based on Tourism Research Australia data).

International visitor numbers will likely be less than 20% of pre-COVID levels in 2022. International spend will likely be even lower as most visitors will consist of visiting friends and relatives (VFR) rather than pure leisure. The massive reduction in international visitors has already had an impact of more than AUD75 billion impact in the first 21 months of the pandemic and the impact will likely exceed AUD110 billion by the end of 2022.

In order to again generate significant revenues from international visitors, Australia will need to reopen to all visitors and provide a blanket no quarantine option. If there is any uncertainty, potential visitors will simply travel to other destinations. Not being able to travel to all of Australia without quarantine will dissuade international tourists as many international visitors travel around the country rather than stick to one or two states.

So far only New South Wales and Victoria have eliminated quarantine requirements, having reached the 80% vaccination threshold in October 2021. But it is possible these requirements can be re-imposed and there is a risk that South Australia, Northern Territory and Queensland will not eliminate quarantine as planned when they reach the higher 90% threshold. There is also still uncertainty on if Western Australia will eliminate quarantine when it reaches the 90% threshold. International visitors are not likely to return in significant numbers until all these uncertainties are resolved and there is no risk of quarantine when they enter or travel around Australia.

With quarantine requirements decided at the state level traveling becomes messy and complicated, particularly for international visitors. For example, it is possible to enter a state that does not have any quarantine requirement and after 14 days travel to a state that still requires quarantine for international arrivals but not domestic arrivals. Such scenarios are not ideal as they require complicated itineraries and there is a risk of last second changes which could result in unexpected quarantine. Many potential visitors will avoid Australia entirely and select other less complicated destinations.

Australia will also need to focus on source markets that have the potential to recover fast. Some major source markets such as China will remain impossible to tap for most and potentially all of 2022 due to border restrictions.

The industry is focusing on Japan, New Zealand, South Korea, the United States and the United Kingdom as it tries to recover international tourism in 2022. But New Zealand may be the only source market with significant visitors in

2022 – and this hinges on the resumption of two-way quarantine-free travel across the Tasman. For the other four markets, it will not be easy to attract visitors outside of the VFR segment. Travelers from most of these countries have been enjoying other international destinations for several months. Australia may no longer be top of mind and the chance of travel around Australia being disrupted due to possible internal border issues is an impediment.

Outbound is a larger segment by volume, accounting for slightly over half of all international passenger traffic prior to the pandemic, while transit is a very small segment due to Australia's isolated geography. The quarantine requirement is less of an issue for the outbound segment as this is essentially a captive market. Australian residents have accommodation to quarantine at when returning home if necessary. They are much more likely to accept quarantine, or the risk of quarantine, compared to visitors.

However, there will also be a significant impact on outbound demand if the quarantine requirement for all returning vaccinated travelers is not eliminated entirely (for all states and territories). Australians will travel overseas less frequently if there are any quarantine requirements or a risk of quarantine being re-imposed while overseas. This is particularly an issue with international business travel, a critical source of revenue for Qantas and several foreign airlines serving Australia.

The cost and hassle associated with COVID testing requirements will also impact demand. Some states/territories plan to require as many as seven tests in order to enter without quarantine. This is another area lacking consensus between states and territories.

The longer international travel restrictions and cumbersome requirements remain in place the harder it will be for Australia to fully recover. Several foreign airlines are likely to be dissuaded to resume services to Australia due to stronger demand in other markets. In 2019, 56 foreign airlines operated scheduled passenger services to Australia. About half of these airlines are at risk and may not resume services by the end of 2022. While these airlines were relatively small players in the Australian market they fostered competition and, in many cases, provided unique destinations that were not served nonstop by any other airline. Some could return to Australia in the future but it will not be easy to persuade them back given their investments in other markets. Many of these airlines are relatively small and have shrunk during the pandemic and may not have the capital or capacity to resume all the destinations they served prior to the pandemic.

The larger foreign competitors will continue to serve Australia but are likely to hold off in restoring full capacity if there are better markets to focus on as global travel starts to resume. Australian carriers could benefit to some extent but have limited flexibility to add long-haul capacity following restructurings. Virgin Australia has phased out all widebody aircraft and Qantas also has reduced the size of its widebody fleet.

Globally international passenger traffic is expected to fully recover in 2023 or 2024. But some markets will recover sooner while other markets will take longer or may never fully recover. Australia is likely to recover slower rather than faster. There has already been potentially irreversible damage on Australia's ability to compete as an international destination and fully recover international traffic.

It is now critical that Australia starts to put in place policies to support a rapid recovery of the international market and its competitiveness as an international destination. This is about more than just the short-term economic consequences. It is about the long-term future of Australia and its position in an increasingly competitive global travel marketplace.

## AIRLINE OUTLOOK/FUTURE AIRLINE MARKET CONDITIONS

While market conditions will gradually improve, Australian carriers will need to adjust to potential shifts in travel patterns.

In the international market, leisure traffic is likely to recover faster than business traffic. Airlines will need to be flexible and add capacity to international destinations that are popular with leisure travelers in the post-pandemic or endemic environment. These will not necessarily be the same destinations that were popular prior to COVID-19.

Strong international business routes may struggle due to a slow recovery in business traffic. Some services will become hard to sustain due to a significant decline in premium business traffic, which has traditionally been highly profitable and enabled airlines prior to the pandemic to maintain long-haul routes despite losses in the economy cabin.

However, there could be an opportunity for Australian carriers to pick up market share from foreign airlines as foreign airlines shift some of their international capacity to better performing markets. Australian carriers will also benefit from a stronger preference for nonstop services, giving them a competitive advantage over airlines that rely heavily on sixth freedom traffic. There is a lot of room for potential market share gains given that foreign carriers flew about two-thirds of international passengers to and from Australia prior to the pandemic.

Therefore, Australian carriers should be able to recover international traffic faster than the total market. While some routes may have to be reduced or dropped, other routes can potentially be launched or increased if they have a strong leisure component and/or if a foreign competitor has pulled back.

Qantas in particularly could enjoy a relatively fast international recovery due to the restructuring at Virgin Australia, which has resulted in it dropping all long-haul markets, as well as the withdrawal of several foreign airlines and the growing popularity of nonstop services. Virgin Australia will still be to take advantage of potential opportunities in regional international markets, which typically rely mainly on leisure traffic, using its all-narrowbody fleet. Jetstar will be able to take advantage of opportunities regionally as well as on medium haul routes to Asia as it continues to operate a small widebody fleet and will begin taking delivery in 2022 of A321LRs, enabling longer narrowbody routes. Rex and Bonza may also be able to take advantage of regional opportunities using their 737 fleets although their focus for now is entirely on the domestic market.

Overall, 2022 will be very challenging for all international competitors. An international recovery in terms of traffic or profitability for any Australian carrier is not likely until at least 2023.

The domestic market will recover much faster but there are also numerous challenges and airlines will similarly have to adjust to potential shifts in travel patterns.

Domestic leisure traffic is likely to fully recover rapidly assuming there are no new setbacks that cause internal borders to stay closed or reclose. Interstate domestic leisure travel will benefit from strong pent-up demand as most internal borders have been closed for most of the pandemic, making it impossible to travel to many of the most popular destinations. There will also be strong demand in the domestic VFR segment as families that are spread out across multiple states look to reunite.

International travel will remain cumbersome, even if there are no quarantine requirements, making domestic holidays more attractive. Domestic leisure travel could potentially grow beyond pre-COVID levels in 2022.

But how big domestic leisure travel becomes in 2022 partially hinges on how quickly Australia’s economy rebounds and consumers’ discretionary income levels. A significant portion of the population has been financially impacted by the pandemic and may not have the means to travel in the near term or as frequently as prior to the pandemic. A recent Inmarsat survey found 25% of Australian passengers said their finances or jobs had been affected by the pandemic. Low fares, driven partially by government incentives such as the half-price ticket scheme, could help stimulate demand but some Australians may still be dissuaded by the total cost of travel.

Domestic business traffic is likely to recover slowly, significantly impacting airline revenues. There could be an initial surge in domestic business traffic after internal borders reopen as companies will want to reconnect with customers, partners and colleagues. However, the number of annual domestic business trips for many companies could reduce significantly.

The pandemic has enabled some companies to recognize they can permanently replace some in-person meetings with virtual meetings. Road warriors may cut back their frequency of domestic trips – for example from every week to every fortnight or from every fortnight to every month. This could potentially have a big impact on Australia's carriers given the pre-pandemic strength of the domestic business market.

Prior to the pandemic Australia had one of the strongest domestic business markets in the world in terms of yields and portion of total passengers. Even if some or all of the reduction in business traffic volumes are offset with increased leisure traffic the average yield will decline significantly, pressuring profitability.

In addition to the prospect of having to rely more on lower yielding and typically less profitable leisure traffic, Australian carriers will have to contend with intensifying domestic competition. The pandemic has attracted new start-ups, which will result in more competition on both trunk and regional routes. Rex started competing on trunk routes in March 2021, providing new competition for Qantas, Jetstar and Virgin Australia, and is planning to expand its new 737 operation in 2022 and beyond.

Bonza recently announced plans to launch in second quarter of 2022 using 737 MAX aircraft. While Bonza will focus on unserved or underserved point to point rather than trunk routes, it will compete to some extent with the main players and fight for a share of the same pie. Bonza and Rex are mainly focused on the leisure segment of the market, which should grow but will become extremely competitive. Virgin Australia, which is also planning domestic expansion in 2022 and beyond, is also mainly focused on the leisure segment following its 2020 restructuring. All the new competition, as well as a reinvigorated Virgin Australia, could pressure yields and load factors even if the market grows.

Domestic operations have historically been profitable – much more profitable than international operations and most other major domestic markets in Asia Pacific. Australia's carriers need domestic operations to return to profitability as soon as possible in order to recover from the pandemic and an extremely challenging two years that has damaged balance sheets. However, a slow recovery in business traffic and the intensification of competition in the leisure or value segment of the market could make it difficult to achieve a return to profitability in the near to medium-term.

# FUTURE PASSENGER EXPECTATIONS

Airlines will also need to adjust to changes in passenger preferences and expectations.

Passengers are generally eager to travel by air again but most have at least some concerns and different expectations than prior to the pandemic. Connected technologies are particularly important in rebuilding passenger confidence.

Airline digitalization has accelerated during the pandemic, continuing a trend that started prior to COVID-19. But there is still a lot more work to be pursued in this area. Retirement of legacy systems and transitioning to self-service solutions can be time consuming and expensive.

Australian carriers need to continue to invest in a wide range of new technologies in order to boost passenger confidence – which in turn will help facilitate a recovery in both the domestic and international markets. Digital heath passports and inflight wi-fi are among the technologies that passengers are keen for airlines to adopt.

Inmarsat published in September the 2021 version of its Passenger Confidence Tracker, which provides insights from surveying more than 10,000 passengers globally. Of the 506 passengers surveyed in Australia, 47% have taken a flight during the pandemic with 70% of these passengers only flying domestically.

An overwhelming majority of passengers – both globally and in Australia – said they were satisfied with airlines' responses to the pandemic. In Australia 66% were very satisfied or fairly satisfied compared to only 7% that were very or fairly unsatisfied with the remainder stating they were neither satisfied or unsatisfied or were unsure. While the general level of satisfaction is high there are many potential improvements or upgrades to boost satisfaction scores in the post-pandemic environment.

Of the Australian passengers surveyed, 28% said inflight wi-fi has become more important following the pandemic. Extra leg room and overall service experience were cited the most, with 39% and 35% of passengers respectively voting for these factors becoming more important following the pandemic.

When asked what else can airlines and the travel industry do to make them more confident about flying, the most common response both globally and in Australia was that all airlines should follow the same hygiene practices. A consistent worldwide set of safety standards was the second most common response both globally and in Australia followed by mandatory proof of vaccination/immunity for all passengers.

Globally 84% of passengers, including 82% of passengers in Australia, said vaccine passports are a good idea. A majority of Australian passengers also said digital health passports were among the new aspects of the travel experience that should be kept after the pandemic. Digital health passports and personal protection packs (masks, gloves and sanitizing wipes) were cited the most by passengers, with 51% of the passengers surveyed saying each of these aspects should be kept after the pandemic.

Digital health passports were the third most common response for Australian passengers when asked what would improve their confidence within the airport and during boarding. The most common responses were pre-flight COVID testing and thermal scanning.

An overwhelming majority of Australian passengers, 79%, said travel habits are likely to change post-COVID. Globally 84% of passengers said their travel habits are likely to change.

Not surprisingly quarantining and unpredictable border closures were the main worries cited by Australian passengers when asked what was preventing them from travelling. Globally the biggest concern was catching the virus on board, which ranked the third biggest worry for Australian passengers.

A majority of Australian passengers similarly cited providing better information about border restrictions and adopting the same quarantine rules across all countries when asked what can be done to improve their confidence. This highlights the importance of governments having clearer and more uniform policies for border restrictions and quarantine. While it is somewhat understandable that countries have had their own rules and policies, different rules and policies within a country is extremely frustrating and has impacted passenger confidence in Australia.

There continues to be a lot of uncertainty towards future air travel in Australia as it is unclear when all states and territories will waive quarantine requirements. It is also unclear when international visitors will be allowed to enter Australia again.

All states and territories need to be clear on their policies and plans. The risk of reclosing borders or reintroducing quarantine requirements has to be eliminated. Consensus and uniformity with regulations and policies is critical as otherwise it erodes passenger confidence.

While there is still a lot of uncertainty globally with international travel, there have been significant improvements over the past few months in most markets, resulting in passengers slowly regaining confidence. Australia still has a long way to go in this area. The current situation of a divided Australia – with one portion not open to the other or the rest of the world – sends a mixed message. The situation with different quarantine requirements for different states and territories is also complicated and sends the wrong message to potential visitors from the rest of the world.

The good news is Australians are by and large ready and eager to fly. Australia has always had a very high propensity for air travel with one of the highest trips per capita globally. Australia also has always been one of the most aspired destinations for international travelers, generating one of the highest international visitor spend per trip globally.

Australia will at some point regain these distinctions. But when this happens – and how long it takes for Australia to catch up with the rest of the world – will hinge on how quickly the current impediments to air travel are lifted.

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