

# China

## Aviation Overview

Aviation developments along with exchange rates, income growth and other factors influence inbound tourism to Australia. Total arrivals historical and forecast:

- Up 43% in 2004;
- Up 13% in 2005;
- Up 11% in 2006 (TFC); and
- Up 15% in 2007 (TFC).

The key aviation related challenge for the inbound tourism industry is to encourage new direct air links from China to further Australian ports beyond Sydney and Melbourne. This is most obviously an issue for Queensland given the high share of Chinese visitors who visit this State and have more tiring itineraries from having to backtrack southward to leave Australia.

A second aviation related challenge is to improve access to domestic air links for Chinese inbound travellers (for arrivals on other airlines than Qantas) to encourage more multi-destination trips and lift the current low level of Chinese regional visitation within Australia. This latter issue has become more important with the growing dominance of low cost carriers in domestic leisure destinations.

- ✈ Chinese aviation is growing quickly as are links provided by other countries' airlines to China. China is Australia's fastest growing major inbound tourism market and a significant and fast growing outbound destination for Australians.
- ✈ China has direct services to Sydney and Melbourne while services fly directly from Australia to Beijing, Shanghai, Guangzhou with a through service to Shenyang.

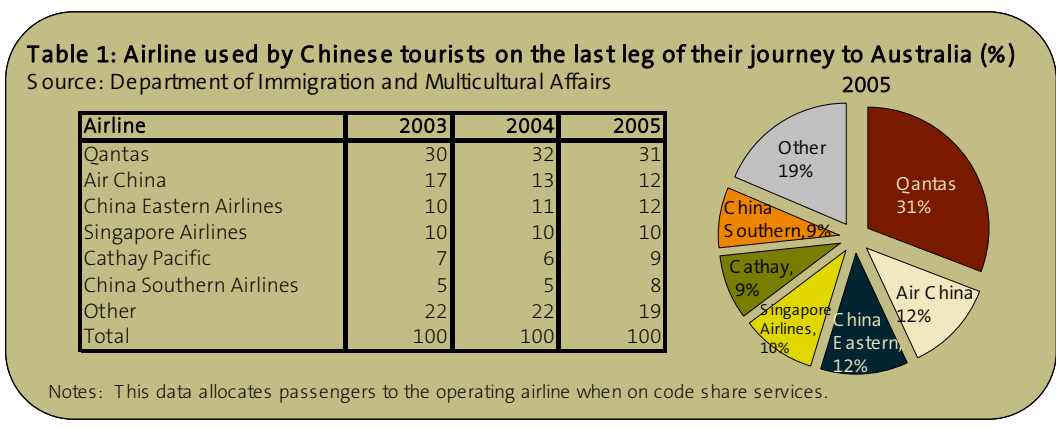
Figure 1: The more common aviation routes from China to Australia



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- ✈ As well as direct air links a large share of Chinese visitors come through Hong Kong and Singapore, often to access Australian cities beyond Sydney and Melbourne. There is a separate aviation overview for Hong Kong.
- ✈ The three largest Chinese carriers of Air China, China Eastern and China Southern along with Qantas provide direct services with significant indirect traffic carried by Cathay Pacific, Qantas and Singapore Airlines. In the last three years Qantas has increased its market share with new direct services.



### Direct non-stop China-Australia services

- ✈ At present, Chinese carriers are currently using just over 60 per cent of their bilateral maximum capacity allocation, while Australian carriers are only using 25 per cent.
- ✈ Under the current air services agreement (signed mid 2003) between China and Australia there is approval for 8,500 seats per week from airlines of China and airlines of Australia.
- ✈ Table 1 (below) is quite complex. As there are a number of ports in China connecting to the same Australian route and vice versa. The following table therefore features significant double counting. In particular, Air China routes operate through a number of Australian and Chinese ports.

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Table 1: Current direct weekly schedules from China to Australia

Chinese Port	Australian Port	Airline Operating	No. of flights	No. of seats	Comments
Beijing	Sydney	Air China	4	924	Shenyang is the originating point and the service operates via Shanghai
		Air China	3	978	Operates via Shanghai and Melbourne
		Qantas	3	906	Commenced non-stop services in January 2006
	Melbourne	Air China	3	978	Operates via Shanghai and onto Sydney
		<b>Sub-total</b>	<b>10</b>	<b>2,808</b>	
Shanghai	Sydney	Air China	4	924	Services Shenyang and Beijing before connecting to Shanghai.
		Air China	3	978	Beijing is the originating port connecting to Shanghai and operates via Melbourne
		Qantas	4	1,208	One service operates via Melbourne. Commenced services in Dec 04.
		China Eastern	7	1,904	All code shared with Qantas. Three services operates via Melbourne
	Melbourne	Air China	3	978	Beijing is the originating port connecting to Shanghai and onto Sydney
		China Eastern	3	816	All code shared with Qantas. Three services operates continue to Sydney after Melbourne
		Qantas	1	302	Service continues to Sydney
		<b>Sub-total</b>	<b>15</b>	<b>4,036</b>	
Guangzhou	Sydney	China Southern	5	1,395	Three services operates via Melbourne
	Melbourne	China Southern	3	837	
		<b>Sub-total</b>	<b>5</b>	<b>1,395</b>	
Shenyang	Sydney	<b>Air China</b>	<b>4</b>	<b>924</b>	Operates via Beijing and Shanghai before connecting to Sydney
		<b>Total</b>	<b>26</b>	<b>7,315</b>	

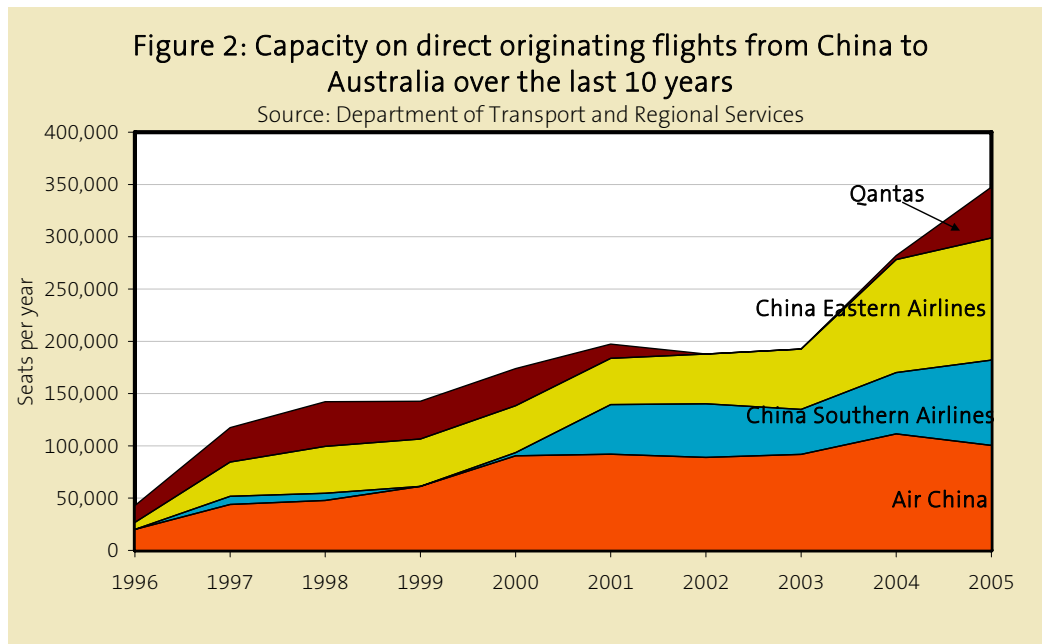
Source: Air Transport Intelligence, 11 May 2006 for schedules in April 2006 (the first month of the Northern Winter schedule).

Note. The sum of all the services in above table does not equal the total figure. This is because Qantas, Air China, China Eastern Airlines and China South Airlines operate flights that service more than one Australian port and hence there are issues of double counting.

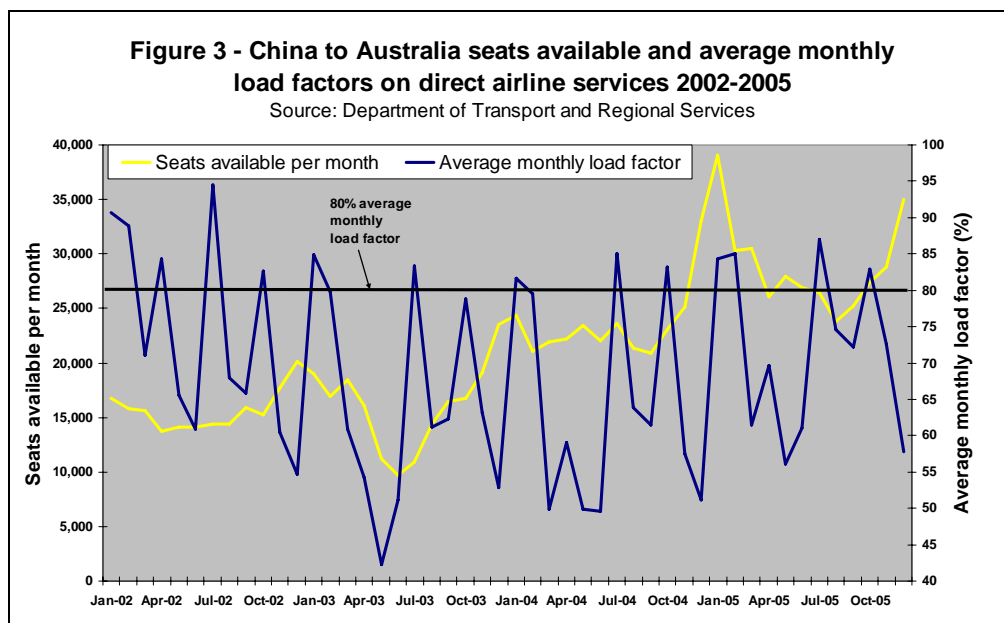
- ✈ Over the last ten years, capacity on the direct China-Australia route has grown over 700 per cent (as shown in Figure 2).

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- ✈ Chinese travellers arrive both on direct services from Chinese carriers and since late 2004 on Qantas on direct services from Shanghai and from early 2006 on Qantas from Beijing.
- ✈ All carriers operating on the China-Australia route in 1996 are still present - though the level of capacity has grown significantly on the Chinese carriers.
- ✈ As shown in Figure 3, the direct China-Australia route has commonly enjoyed quite low load factors, in part due to this route receiving little through traffic from Europe or other regions. Peak periods are around Chinese New Year (January or February), July and October, with trough periods in March to June, August and September.



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### Key indirect China-Australia services

- ✈ The Chinese inbound tourism market to Australia is unusual, given its accessibility for non-stop services using medium range aircraft and size, for the high level of reliance on indirect airline services.
- ✈ The merger of Cathay Pacific and Dragonair along with increased equity share of the combined group by Air China has a range of potential implications for development of both direct and indirect airline services to Australia for Chinese inbound visitors.
- ✈ It is clear that following the merger of Dragonair into Cathay Pacific, Hong Kong could become a much more important hub for China traffic seeking to visit Australia. This reflects the fact that previously Cathay Pacific which has an extensive network into Australia had few rights to fly into China from Hong Kong with only 22 services per week in June 2006. In contrast Dragonair has an outstanding route network into China from Hong Kong with nearly 200 flights per week. As shown in Figure 4, the Dragonair network includes over 20 destinations in China.

**Figure 4 – Dragonair’s route network in June 2006**



Source: Dragonair website 14 June 2006

- ✈ Singapore Airlines also has a useful network into China and they are proving successful in transporting Chinese inbound visitors particularly to Queensland. Singapore Airlines in June 2006 was flying to four destinations in China with 63 services per week.

### Recent airline development and looking forward

- ✈ Chinese aviation is in the midst of major growth challenges. After strong profitability in 2004, the three major Chinese carriers suffered large reversals in profitability in 2005 and the first quarter 2006 with the increase in fuel prices, large increases in capacity and growing competition in the Chinese market reducing yields.
- ✈ According to Chinese Civil Aviation Authority (CAAC,) Chinese carriers reported a combined net loss of CNY2.1 billion (A\$353 million) in the first quarter of 2006 (Source: CAPA, 22 May 2006). China Eastern reported the largest loss of China's big three airlines reporting a net loss of CNY955.1 million (A\$161 million), compared to a net profit of CNY50.4 million (A\$8.5 million) in the same period in the previous year.
- ✈ In the current period of high fuel prices, China Eastern Airlines has called for China's fuel monopoly to be broken (Source: China Daily, 18 September 2005). At present Chinese carriers are required to purchase fuel through a single holding company. China Eastern claims Chinese carriers are disadvantaged and several companies that supply fuel should be able to compete in a big country like China.
- ✈ In addition, Chinese carriers have requested the Chinese government reduce its value-added jet fuel taxes and exempt them from tariffs on jet fuel to help them cope with rising fuel costs (AFX, 6 January 2006). Government intervention on surcharges, fares and other areas are also helping to relieve pressure on yields and profitability.
- ✈ China's Airlines are adjusting their strategies in 2006. Air China recently strengthened its links to Hong Kong through a restructure involving Cathay Pacific and Dragonair. On 8 June 2006, Air China, Cathay Pacific, CNAC Limited, CITIC Pacific and Swire Pacific (SPAC) entered into a conditional agreement to restructure the parties' shareholdings in Cathay Pacific and Dragonair.
- ✈ If the agreement becomes unconditional:
  1. Dragonair will become a wholly-owned subsidiary of Cathay;
  2. Air China will become a substantial shareholder of Cathay (10 per cent);
  3. Cathay will increase its shareholding in Air China from 10 to 20 per cent (Source: CAPA 9 June 2006).
- ✈ Air China is also trying to strengthening its links to Australia through a proposed codeshare agreement with Qantas on Qantas' Beijing-Sydney services. More generally, Air China and Shanghai Airlines have announced they will join Star Alliance while China Southern Airlines will join SkyTeam.
- ✈ Shanghai Airlines has traditionally focussed on domestic operations. However the airline is increasingly looking at international opportunities but currently has limited long haul aircraft to service them. The carrier has announced its intention to join Star Alliance to help it expand its international operations (Source: Air Transport Intelligence, 10 May 2006). The airline receives two B767s in July and November 2006, which could possibly service Eastern Australia (Source: China Securities Journal, 23 August 2005).
- ✈ As shown in Table 2 (below), Chinese aviation's strong growth expectations are reflected in their aircraft orders. In April 2006, Chinese carriers ordered 80 B737s. This comes after Chinese carriers ordered 52 B787-800s in August 2005 (Source: Air Transport Intelligence).

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- ✈ CAAC forecasts Chinese carriers will acquire 100 to 150 aircraft over the coming five years. Similarly, Boeing forecasts Chinese carriers will acquire over 2,600 new aircraft over the next 20 years, in other words a new aircraft every 2.8 days (Source: CAPA, 15 November 2005).

Table 2: Current and future aircraft for Chinese carriers

Aircraft	In active service				On Order			
	Air China	China Southern	China Eastern	Shanghai Airlines	Air China	China Southern	China Eastern	Shanghai Airlines
A380						5		
A310-200			3					
A319-100	24	22	11		11	10	4	
A320-200	6	36	63			13	4	
A321-200		12	4			8	11	
A330-200		4	3		20	2	2	
A330-300			2			8	13	
A340-300	6		5					
A340-600			5					
B737-300	33	24	25					
B737-500		5						
B737-600	6							
B737-700	11	16	24	6	3	12	8	
B737-800	19	22	7	13	15	15	1	7
B747-400	4							
B757-200	13	28		13				
B767-200ER	5							
767-300	4			4				
B767-300ER	5		3	1				2
B777-200	10	4						
B777-200ER		6						
B787-800					15	10	15	9
Other	13	56	44	6	0	0	0	
<b>Total</b>	<b>159</b>	<b>235</b>	<b>199</b>	<b>43</b>	<b>64</b>	<b>83</b>	<b>58</b>	<b>18</b>

Source: Air Transport Intelligence, June 2006

- ✈ Chinese airlines continue to face widespread skills shortages. In March 2006, Civil Aviation University of China estimated that China aviation sector will require 240,000 trained staff over the next 20 years (Source: XIC, 29 March 2006). In order to combat these challenges, CAAC implemented (August 2005) compensation measures while Ministry of Civil Aviation extended the retirement age of commercial pilots from 61 to 65 years (Source: The Pioneer, 23 November 2005).
- ✈ One further possibility is that **Jetstar International** could start flying to China around the end of 2008. When the carrier begins to receive the first of its B787-8s due in August 2008, Jetstar International could consider operating services to China. Qantas has announced that Jetstar International expects an additional four B787-8s to be delivered in 2008.

<sup>1</sup>This briefing was significantly assisted by: research from Centre for Asia Pacific Aviation, Air Transport Intelligence and assistance from the Department of Transport and Regional Services (Avstats). Data on scheduled frequencies is understandably available on a more timely basis than data on load factors and passengers carried.