



The National Organisation in New Zealand of:
Aviation Education and Research Organisations
Aircraft Repair and Maintenance Organisations
Unmanned Aerials Systems Organisations
Air Rescue/Air Ambulance Organisations
Aviation Fuel and Oil Suppliers
Flight Training Organisations
Aviation Service Providers
Air Charter Operators
Helicopter Operators
Aircraft Constructors
Aviation Suppliers
Airport Operators
Airline Operators
Aviation Insurers

4 May 2013

Inquiry into the Services Sector
New Zealand productivity Commission
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Submission on behalf of the Aviation Industry of New Zealand

The Aviation Industry in context

The Aviation Industry Association represents the interests of commercial aviation in New Zealand. Our membership includes New Zealand based aviation businesses and suppliers of services and goods to the industry. In total there are 450 members representing around 96% of the volume of aviation in this country.

The Aviation Industry's contribution to the New Zealand economy was quantified in 2009 as around \$9.7Bn, with \$5.9 billion from domestic activities and \$3.8 billion from export activities. We think its contribution today is around \$12Bn with the potential to be \$16 Bn by 2016

In 2009, the last time the industry was researched in any great depth, there were here are more than 1,000 organisations participating in the industry, employing 23,525 staff with wages and salaries estimated at \$1.3 billion. Using input / output economic modeling, the direct and indirect impacts of the New Zealand aviation industry together has been calculated at 11.8% of total revenue across the New Zealand economy and 6.9% of GDP in the year to December 2009.

The aviation industry is estimated to have grown from a total revenue contribution of \$6.8 billion in 2005 to \$9.7 billion in 2009. This represents a growth rate of 9.5% per annum over the five year period. The data indicated increased productivity during this period, with average revenue per employee growing from \$366,700 to \$456,861.

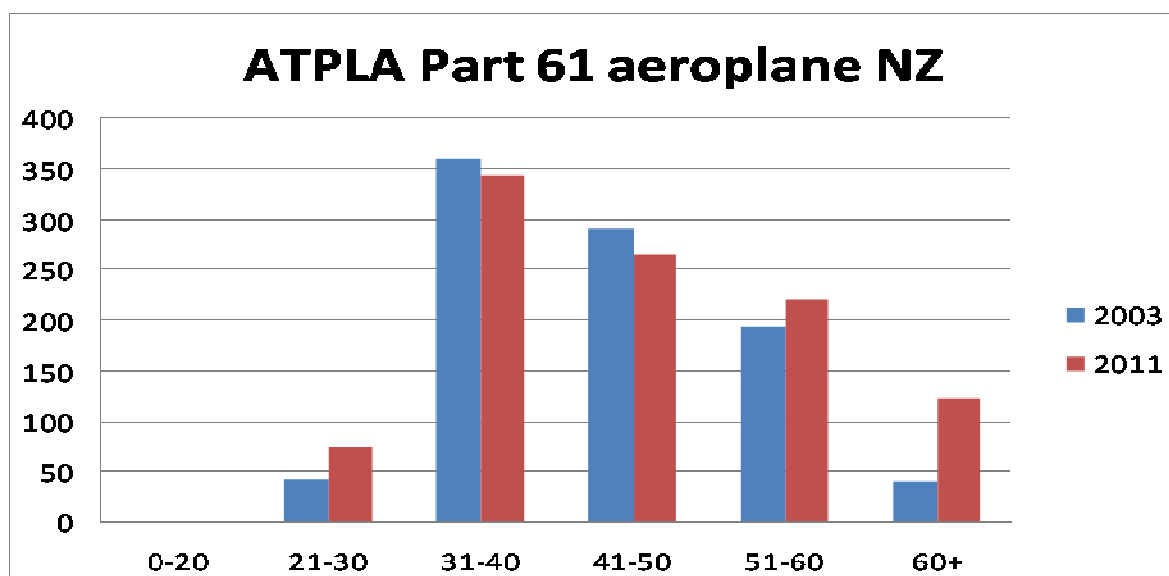


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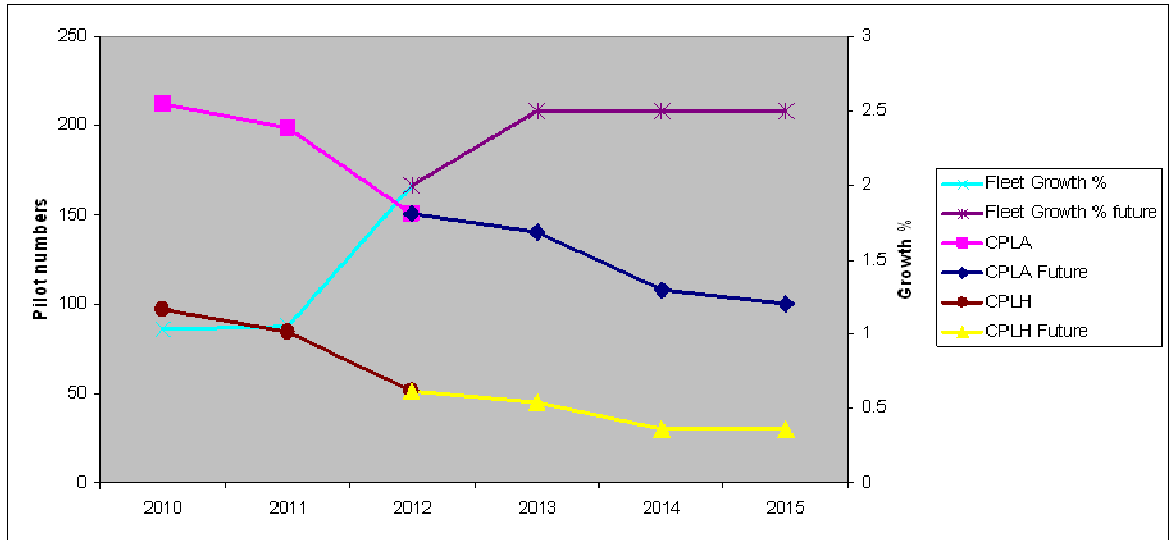
The service industries component is placed at around 94% of the revenue contribution to the sector to the New Zealand economy.

The aviation industry is characterised by very high average incomes placed at around \$70,000 in 2009. It employs personnel who generally are highly skilled with international qualifications.

The workforce itself however is displaying all of the characteristics of an aging population. This is an example for pilots holding airline qualifications. However a similar profile can also be produced for engineers. The key point being is that there is no technological solution which will reduce the requirement for pilots in the foreseeable future.



Recently supply of some of our key strategic skills has been plummeting at a time when global demand is increasing. An example of this is the number of pilots graduating.



Data source CAA for actual numbers to Dec 2012 and industry projects 2013-2015. Growth FAA forecast. IATA forecast has 5.5% growth which escalates the problem.

This change has been largely driven by government policy settings and decisions made to reduce the number of pilots who can be trained under government student loan schemes.

Will the Commission’s proposed approach to this inquiry deliver the best outcomes for New Zealand? How can it be improved?

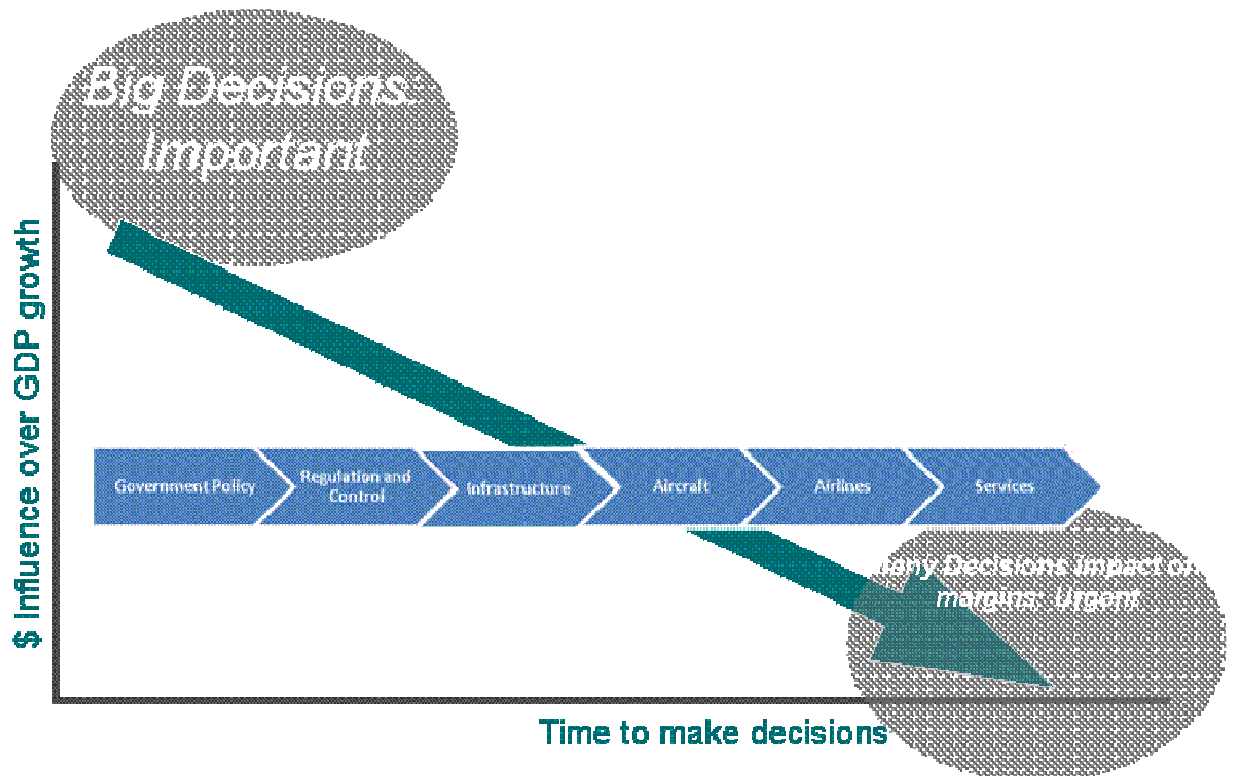
No we think there is so much diversity across sectors that a value chain approach should be taken.

Here is the value chain for the aviation industry



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We see time and again the big value decisions for the sector (ie government policy settings and the regulatory environment) take an enormous amount of time to develop but they one made have incredibly long lasting consequences for the sector.

Getting those decisions right is critical therefore excluding one our most important contributors to the success or otherwise of the sector is eliminating one of the factors that can really drive important wealth creation and productivity improvements. We would urge the Commission in part B of your review to look at the importance of the inter-relationships between the public and private sector.

What are the relevant publications and data sources should the Commission explore for this inquiry?

For Aviation we suggest the New Horizons report www.nzte.govt.nz

Which activities within the following industries are provided in a market (non government environment):

- **Education and training;**
- **Healthcare and social assistance; and**
- **Public administration and safety?**

In our environment education and training is almost exclusively provided by the private sector with the following exceptions: – the RNZAF (ie Royal New Zealand Air force), Massey University and NMIT (Nelson Marlborough Institute of Technology).

In the Healthcare sector we provide all emergency air ambulance and air rescue services and inter hospital transfers provided by air.

We provide safety services under delegation from the Civil Aviation Authority and an extensive safety programme to support all commercial operators as this is mission critical to our businesses. We also provide some public administration services such as exam assessment however the process of delegating this to the private sector has significantly slowed since the reforms of the early nineteen nineties. This is an area where we think change could be made and more delegated to the private sector.

To what degree should the market-provided parts of these industries be included within the scope of this Inquiry?

Absolutely they should be included as well as some public services where these directly impact on the productivity of the sector.

For example, our pilot manpower crisis, has been largely caused by the adoption of inappropriate central government policies in relation to forward demand for pilots. This is a critical supply chain issue for the sector with the ability to impact on our tourism industry.

In your opinion do weaknesses and gaps in service industries handicap the performance of other industries? If so how?

Yes absolutely – we have just provided you with an example where the looming problem we have with insufficient supply of appropriately trained pilots will impact on our ability to provide the appropriate level of connectedness by air within the New Zealand



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economy and an inadequate number of tourism services to meet the demand from tourists to experience the New Zealand wilderness from the air. These are very real and urgent problems today.

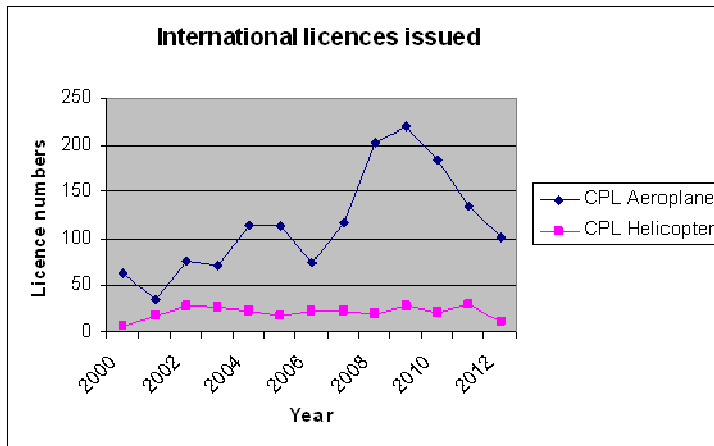
What are the causes of the productivity gaps between firms in the same service industry or sub industry? What can be done to reduce such gaps?

In our sector some of the productivity gaps between firms are caused by government policy settings. An example being our flight training industry. To produce an identical qualification – a Diploma in Aviation (pilot) takes a non student loan funded organisation about 15-18 months and this is broadly consistent with global practice whereas for a student loan funded organisation this can take up to two and a half years. This is because the student loan funded organisation is having to train to an external imposed education based cash flow. For example one difference is that an equivalent full time student is assessed for funding for a maximum of 32 weeks whereas our training sector at maximum productivity works seven days a week and for 52 weeks of the year.

This is further capped by how much a student can borrow and imposed credit values for academic attainment which have no relationship to the actual cost of producing the goods.

What is the potential for improved productivity and growth in service industries you are familiar with? What are the impediments to improved productivity and growth in those industries?

Substantial we believe it is possible to accelerate growth in the aviation sector to over 9% however we need a number of changes to achieve this in some service sectors. We have highlighted the issues with pilot training because this is an area of massive global demand which New Zealand is missing out on.



Data Sources: CAA and * New Horizons Report June 2010

2012 v 2009

Loss of \$10.4m In trainer income

Loss of \$46.2m In economic activity*

Challenges

Training is a global and globally connected industry

More competitive and internationally relevant curricula

Better funded industry investing in facilities with focus on quality and value

To what extent is there insufficient competition in New Zealand service industries? In which industries? What are the impediments to competition in those industries?

No comment

What are the opportunities for productivity growth in service industries where production and consumption of the service happens in the same location and demand is geographically spread out?

No comment

Are there service industries that perform less well than they could due to problems such as low levels of skills or lack of specialised inputs, scale, appropriate infrastructure or opportunities for agglomeration? What are the impediments to improving productivity and growth in these industries?



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No comment

What are the barriers to the export of service? What are the economic impacts of those barriers? What can be done to reduce them?

We attach a recently completed barrier paper for the flight training industry. There is still debate around two of the barriers cited for the helicopter training sector but there is general agreement of everything else.

Your will see the barriers are a mixture of regulatory and non regulatory. Even though we produce a license which is globally recognised there are still wide variations regarding content of the syllabus. This is because customisation to the New Zealand environment has crept in over time without too much regard to the impact this is having on delivery of a competitive product.

However the major barrier particularly in the educational space is that our closest competitors namely Australia and Canada do not impose GST on educational services. This means we are automatically at a 15% disadvantage and this has to impact somewhere in our price structure and it is normally that we adjust our variable cost structures downwards and this is primarily salaries paid to Instructors.

In the export aviation sector services are treated one way and GST imposed but manufacturing another way even though essentially what the service sector is doing is "value adding" and re-exporting. For example an overhaul of an engine GST is charged on its import but off-set when re-exported. There is no such treatment for foreign students however what we are doing is importing a student for "up skilling" and re-exporting. Zero rating GST would have a major and long lasting impact on the competitiveness of the sector. We are not training aviation personnel to stay in this country whether they are air traffic controller's engineers or pilots. The objective is re-export to their home country where there are severe shortages.

To what extent are their barriers to the efficient import of services? What are the economic impacts of those barriers? What can be done to reduce them?

We still have extensive regulatory and non regulatory barriers some of which are imposed for safety purposes and others relate to bilateral constraints such as the single aviation market only applies to air services and not all aviation services.

An example of a non regulatory barrier is the skills shortages demand list. We perceive the application of this list is becoming more and more limited. It is quite an exhaustive process that must be gone through to the point that even though we consider we have a shortage of qualified instructors it is impossible to prove the point as we quite simply do not have access to all of the data because we don't have a registration board as such and no agency collects the data.

What are the barriers to cross movement of people that affect international trade in service? How do those barriers affect New Zealand service industries and the economy more generally? Are there opportunities to remove or reduce those barriers?

Refer comment above. The entry of skilled aviation personnel into New Zealand is very much determined by the Civil Aviation Authority. In general they do not operate a permissive environment. For example it is virtually impossible for a pilot or mechanic from the United States to gain entry into New Zealand. With Canadians and Australian's there is much greater flexibility however all personnel hold international license. Their training establishments are regularly audited by the regulatory equivalent of the Civil Aviation Authority so one wonders why there is this very different standard.

Moves are a foot globally to develop a fully transportable commercial airline pilot license and this will be a major break through if this occurs.

What barriers exist to cross border investment in service industries? How do these barriers affect New Zealand



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industries and the economy more generally? Are there opportunities to remove or reduce these barriers?

The issue of equity investment in airlines has already been examined by the commission. To our knowledge there are no other constraints in aviation.

How is trade in services affected by New Zealand's current international agreements? What features should negotiators seek or avoid in the future agreements and why?

Until very recently we have found international agreements pertaining to aviation only applied to air services. Over the last 12 months these agreements have widened to include all aspects of aviation.

Of course the international agreements are very high level and we find there are lawyers of implementation agreements required. One areas that we perform badly in is understanding how we can maximise international agreements for the service sector because in general these agreements are written in the context of export in manufacture and while trade barriers in these sectors are generally quite tangible trade

To what extent do New Zealand's service businesses invest in and make effective use of ICT? What are the barriers to them doing so?

Aviation is a major user of ICT and this has been a driver for substantial productivity gains. There are some restrictions when it comes to the interface with safety matters as the rule making process tends to be very prescriptive and this has slowed technology uptake.

What is the scope to raise productivity and wages in service industries that traditionally employ low-skill workers? How would this best be achieved.

No comment

Are there non-targeted regulations that have a disproportionately negative impact on service industries? How can this situation be improved?

One of the important issues for aviation is the non targeted nature of HSE regulations applying to a very targeted and quite sophisticated understanding of safety cultures. We think the recently released HSE taskforce report is heading in the right direction in that there needs to be one highly competent regulator charged with all matters relating to safety in certain sectors whether that safety is of employees or customers

Which service industries are significantly impacted by industry specific regulation? Are there opportunities to Improve?

Our whole sector is heavily regulated in every aspect of our operation. In general we accept that regulation is part and parcel of doing business however we do see the rule making process as being a major impediment to efficiency in the sector and technology uptake. In saying this the Ministry of Transport has recently set about developing a whole new process for making rules with a target of delivering these within 24 months of activation of the project. We think this is an absolute worthy goal but there is scepticism that the process will fail. Presently it can take anywhere between 5-14 years to write a rule.

Are the important issues relating to intangible assets in service industries that the commission should investigate?

No comment

What are the most important policy issues relating to management organisational culture and employee skills in the service sector?

Diversity while still holding onto the cultural values that distinguishes New Zealand from other countries – critical in the tourism industry.

What other policy issues have an important impact on productivity in the service sector



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The aging of the population. With most service sectors there is no automation solution and while ICT can and does accelerate productivity what will be the impacts and effect of an aging population.

What other topics should be considered for in-depth analysis in Part B of the inquiry? In what ways do they meet the criteria of the Terms of Reference?

We think exclusion of the public service is wrong particularly in those areas where there is a key interface with the service sectors.

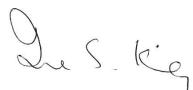
In our environment the policy and regulatory settings of government have a critical impact on both our sectors productivity and its international competitiveness. This is one of the reasons why we take a value chain approach to explain our industry.

Q23 With who should the Commission consult?

There should be some case studies of really successful service businesses. We have a number of stand out examples in the aviation industry – ASPEQ (go to www.aspeq.com). They deliver high stakes assessment tools and services to regulatory agencies and awarding bodies around the globe. The company started as a spin out devolution of a government function (examinations delivered by civil aviation) and with an equity of \$5,000 20 years ago. The company is now a global leader with an internationally competitive product. It is a model of spinning out what would otherwise be seen as “core government” functions in a highly regulated environment. This is a lower cost model that has driven international competitiveness for the sector. Unfortunately this was the only function devolved whereas there are others across government agencies not simply civil aviation which can reduce cost and improve the productivity of the sector. For example Australia has devolved maritime exams to ASPEQ whereas New Zealand has not. This increases the downstream costs to New Zealand industry by not having optimum productivity in the shipping sector in this one area.

There are other example in our sector such as a number of tracking companies who provide enhance environmental product application tracking and or tracking of assets – we would be happy to provide names and contacts.

Yours sincerely



Irene King
Chief Executive



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