

27 April 2022



Dear 

I refer to your email dated 10 March 2022, requesting the following under the Official Information Act 1982 (the Act):

“Any internal or external correspondence (including but not limited to emails, WhatsApp messages, text messages, etc.) regarding whether a CIPA would be needed for either of the following programmes or any of their extensions or associated policies:

- *The Maintaining International Air Connectivity scheme*
- *The Essential Transport Connectivity scheme*

Where any document falls under the scope of this request, please release it in full, including sections which might otherwise be considered out of scope.”

On 4 April 2022, the response timeframe was extended under section 15A(1)(b) of the Act from 7 April 2022 to 27 April 2022.

Information in scope

Annex 1 contains a summary of documents within the scope of your request and any information withheld from these documents.

The timeframe for this information spans from 1 January 2022 (the date mentioned in your request) to 10 March 2022 (the date your request was lodged).

Certain information within these documents is being withheld under the following sections of the Act.

- 6(a) as release would be likely to prejudice the security or defence of New Zealand or the international relations of the New Zealand Government.
- 9(2)(b)(ii) to protect information where the making available of the information would be likely unreasonably to prejudice the commercial position of the person who supplied or who is the subject of the information.
- 9(2)(g)(i) to maintain the effective conduct of public affairs through the free and frank expression of opinions by or between or to Ministers of the Crown or members of an organisation or officers and employees of any public service agency or organisation in the course of their duty.
- 9(2)(a) to protect the privacy of natural persons.
- 9(2)(h) relates to the maintenance of legal professional privilege.
- 9(2)(f)(iv) to maintain the constitutional convention protecting the confidentiality of advice tendered by Ministers and officials.

- 9(2)(i) relates to enabling commercial activities to be carried out without prejudice or disadvantage.

The Government's airfreight support schemes (the International Air Freight Capacity Scheme and the Maintaining International Air Connectivity Scheme) and the Essential Transport Connectivity were established during the height of COVID-19, where quick policy decisions were needed to be made to maintain New Zealand's connectivity, both domestically and internationally, alongside the urgent delivery of critical health supplies.

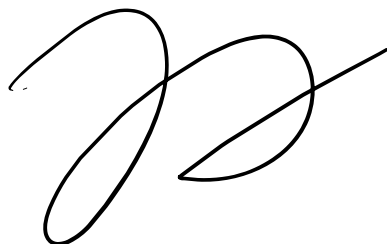
New Zealand has committed to reducing its net emissions of greenhouse gases (except biogenic methane) by 2050. An emissions reductions plan will be published in May 2022 to set out what steps New Zealand will take to reduce its emissions, including emissions for aviation. Government agencies are working with Air New Zealand and the international aviation community to help decarbonise the aviation sector both domestically and internationally.

With regards to the information that has been withheld under section 9 of the Act, I am satisfied the reasons for withholding the information at this time are not outweighed by public interest considerations that would make it desirable to make the information available.

Complaints

You have the right to seek an investigation and review of this response by the Ombudsman, in accordance with section 28(3) of the Act. The relevant details can be found on the Ombudsman's website www.ombudsman.parliament.nz.

Yours sincerely

A handwritten signature in black ink, consisting of several loops and a long horizontal stroke extending to the right.

Jessica Ranger

Manager, COVID-19 Policy and Delivery

Annex 1 – Documents that fall within the scope of your request

Doc#	Date	Document	Decision on release
1	7 March 2022	OC220034 MIAC Exit Strategy Cabinet Paper	Some information withheld under Sections 9(2)(a), 9(2)(g)(i), 9(2)(b)(ii) and 6(a)
2	10 March 2022	Email Chain – ‘James for review by 10 am please’	Some information withheld under Sections 9(2)(a) and Section 9(2)(g)(i)
3	13 December 2021	OC210908 COVID-19-Extension of the Essential Transport Connectivity (ETC) Scheme to 2022	Some information withheld under Sections 9(2)(b)(ii), 9(2)(f)(iv) and 9(2)(g)(i)
4	27 September 2021	OC210668 COVID-19-Maintaining International Air Connectivity (MIAC) scheme extension funding	Some information withheld under Sections 9(2)(b)(ii), 9(2)(g)(i), 9(2)(h), 9(2)(i) and 6(a)
5	21 May 2021	OC210211 COVID-19-Review of the Essential Transport Connectivity (ETC) scheme	Some information withheld under Section 9(2)(b)(ii)
6	12 March 2021	OC210182 Review of the International Air Freight Capacity scheme and future air connectivity	Some information withheld under Sections 9(2)(i), 6(a), 9(2)(b)(ii), 9(2)(h) and 9(2)(g)(i)

Restricted

Office of the Minister of Transport

Cabinet Economic Development Committee

Maintaining International Air Connectivity (MIAC) Exit Strategy


Proposal

- 1 The purpose of this paper is to seek agreement on the exit strategy for the Maintaining International Air Connectivity (MIAC) Scheme.

Relation to government priorities

- 2 This proposal supports the Government's economic response to COVID-19 through its efforts to cushion the financial blow to whānau and families, workers, businesses, and communities from the impacts of COVID-19, position New Zealand for recovery, and reset and rebuild our economy.

Executive Summary

- 3 Air connectivity is vital for trade and economic growth. The Government, through the MIAC scheme and the previous IAFC scheme, has successfully ensured that a minimum level of air connectivity has remained in place for New Zealand throughout the disruption caused by COVID-19. The MIAC has been an important and necessary intervention to enable imports and exports and general air connectivity to continue.
- 4 As we move towards the reopening of our border, Cabinet asked me to prepare an exit strategy for the MIAC to align to the passenger traveller scenarios prepared for the Border Executive Board (BEB) and the Reconnecting New Zealanders strategy [DEV-21-MIN-0186 refers].
- 5 For air connectivity to return on a solely market-provided basis, we need airlines operating to New Zealand and sufficient passenger travel demand. This demand is made possible by border openings and then driven by passenger willingness to travel to New Zealand. As passengers return, the need for the MIAC is expected to progressively reduce.
- 6 The Reconnecting New Zealanders strategy has set out a timeframe for re-opening the border, but uncertainty about passenger demand remains due to self-isolation requirements. Overseas examples show these requirements can dampen travel demand by up to 95% while in place. Even once self-isolation has been removed, tourist recovery will take some time as tourists typically book 9 – 12 months ahead of travel. ^{s 6(a), s 9(2)(g)(i)}

- 7 The MIAC needs an exit strategy that secures the minimum level of air connectivity as passenger demand develops and changes in the coming months. A minimum level of connectivity is critical to ensures New Zealand businesses can get their goods to market, and the importing of medicines / health supplies and critical business parts can continue.

- 8 I recommend a conditions-based approach as the best way for exiting the MIAC scheme. This approach will enable MIAC support to be progressively withdrawn from airlines as passengers return under the Reconnecting New Zealanders strategy. It minimises the risk of airfreight capacity shortages, while being able to exit MIAC support early as passenger travel conditions improve.
- 9 This paper also provides an alternative option that withdraws support on a predetermined basis when current forecasts of passenger numbers indicate that it should be possible to do so. s 9(2)(b)(ii), s 6(a)

Background

The MIAC is a key response to airfreight capacity shortages caused by COVID-19

- 10 In March 2021, Cabinet agreed to establish the Maintaining International Air Connectivity (MIAC) [DEV-21-MIN-0028 refers]. This scheme replaced the International Airfreight Capacity (IAFC) scheme established in March 2020 [CAB-20-MIN-0131 refers].
- 11 The key objectives of the MIAC scheme are, in order of priority:
- 11.1 Retain air connectivity with New Zealand's principal trading partners to ensure that we can access the imports we need, and that our exports can access overseas markets;
 - 11.2 Enable continued essential passenger movements;
 - 11.3 Retain important air connections to the Pacific;
 - 11.4 Retain air connections to key routes and hubs important for tourism recovery; and
 - 11.5 Maintain core capability, capacity and competitiveness within the New Zealand aviation sector to provide a platform for an efficient and competitive market when international air travel recovers.
- 12 Initial MIAC contracts with carriers started on 1 May 2021 following an open-market, competitive procurement process. In October 2021, these contracts were extended to 31 March 2022 [DEV-21-MIN-0186 refers]. At present, nine carriers are supported under MIAC flying to 23 international destinations. This equates to about 50% of New Zealand's international services.
- 13 The total cost of providing MIAC support was s 9(2)(b) to 27 December 2021, with an estimated additional s 9(2)(b)(ii) spent through to 31 March 2022 when the current MIAC contracts expire.
- 14 The MIAC scheme has delivered significant benefits for New Zealanders during its operation, including:

- 14.1 Support for ~3,500 total flights to and from key markets, carrying 84,000 tonnes of freight, worth an estimated total value of \$6.7b¹². Importing critical supplies for the New Zealand economy and health response, such as vaccines and more recently Rapid Antigen Tests.
- 14.2 ~105,000 people returned to New Zealand on IAFC / MIAC supported flights. This equates to about 48% of the total number of people to pass through MIQ.
- 14.3 The Ministry of Foreign Affairs and Trade (MFAT) notes there has been significant benefit received by our Pacific partners from the support of flights into Pacific destinations, including the ability to maintain key supply chain links and connection with New Zealand.

The MIAC scheme has successfully contributed to a minimum level of connectivity, which is considered an appropriate level to maintain throughout an exit process

- 15 Ministry of Transport (the Ministry) analysis shows that the current level of international flight services available for New Zealand is around 10-20% of pre-COVID-19 levels. This includes both flights supported by the MIAC scheme, which are approximately half of all international flight capacity, as well as commercial flights operated outside the scheme³.
- 16 New Zealand industries have been effective at adapting to the new air connectivity levels supported by MIAC. While operating with just 10-20% of pre-COVID flight volumes, New Zealand has still been able to achieve ~90% of pre-COVID airfreight volumes⁴ (albeit at significantly higher prices). This is largely attributed to significantly more effective use of space on aircraft, as well as the flights focusing on freight demand rather than passenger demand.
- 17 While the MIAC scheme has ensured a good minimum level of connectivity, this level is still significantly below the desired level of connectivity from a range of New Zealand sectors (including importers, exporters, and tourism).
- 18 s 9(2)(b)(ii), s 9(2)(f)(iv)
This level has enabled key imports to keep arriving, and has kept many of our exporters in business. Any reduction below this current level would result in further losses of air services and connectivity, threatening our export and import sectors significantly.

¹ Including the IAFC as well, support has enabled ~11,500 flights, carrying 221,000 tonnes of goods worth \$17.7b

² New Zealand exported 93,300 tonnes of airfreight in calendar year 2021 worth NZ\$4.972 billion. The primary sector accounts for 80% of the trade by volume and 40% by value. Airfreight export volumes were on par or higher than 2020 and pre-COVID levels – in part supported by MIAC.

³It is difficult to gauge how much capacity outside the MIAC scheme is being provided on a commercial basis and how much is being supported by connectivity or other airline support schemes operating in other jurisdictions.

⁴ s 9(2)(b)(ii)

Connectivity is critically important for New Zealand, but must be balanced against other obligations

19 Providing a minimum level of connectivity is important for New Zealanders for a wide range of reasons, including:

- 19.1 Reduction in freight capacity shortages – this has a critical impact on many different parts of the New Zealand economy (and especially Māori business due to high investment in primary sector operations reliant on airfreight).
- 19.2 Positive impact on freight rates – without a sustainable minimum level of capacity the market would likely see a surge in freight rates.
- 19.3 Maintaining links for aviation and tourism sectors to recover – having maintained air connectivity, airlines are better positioned to quickly restart services as passenger travel recovers⁵.
- 19.4 Supporting New Zealand's interests and obligations in the Pacific by ensuring connectivity with our neighbours.
- 19.5 Supporting New Zealander's expectations that reasonably priced air travel is available for family reunifications and critical business purposes, as well as readily available later for the return of movement for wellbeing.

20 However, providing this minimum capacity through MIAC must be balanced against public sector obligations, including:

20.1 Fiscal cost and risk – there is a direct material financial cost to operating the MIAC scheme, which must be weighed against other public sector priorities.

20.2 s 6(a) [Redacted]

20.3 Market adaptation delays – by providing MIAC support and continuing with the minimum level of air connectivity, there is a risk of delaying New Zealand businesses' adjustment to what could be long-term or permanent change for some markets.

21 s 6(a) [Redacted]

⁵ Tourism New Zealand notes that carriers lost from the New Zealand market can take at least five years to return, lowering the potential recovery speed significantly.

22 In September 2021, Cabinet requested the development of an exit strategy. Cabinet [DEV-21-MIN-0186 refers]:

s 9(2)
(b)(ii)

█

22.3 **Invited** the Minister of Transport to report back to Cabinet in February 2022 with a strategy for exiting the MIAC scheme, incorporating the Reconnecting New Zealanders approach and forecast traveller scenarios (outlined above).

Key considerations

The airfreight market for New Zealand is at risk

- 23 It is unlikely the New Zealand airfreight market can sustain itself at a level that meets New Zealand's minimum air connectivity needs without government support.
- 24 The airfreight market is particularly challenging for New Zealand. There is a high demand for aircrafts to fly to other countries with opened borders, as well as a lack of staff due to self-isolation requirements.
- 25 United Airlines, American Airways, and Air Canada have exited New Zealand routes entirely, with Cathay Pacific recently suspending New Zealand operations for three months, and Emirates operating reduced services. s 9(2)(b)(ii)
- 26 While the Reconnecting New Zealanders strategy provides clarity around the reopening of the border, the international flight service market in New Zealand remains at risk. Airlines have noted difficulty undertaking long term planning, particularly when self-isolation requirements for arriving passengers are in place.

Passenger recovery is critical for maintaining and improving airfreight connectivity

- 27 The exit strategy for MIAC needs to take into account the recovery of passenger travel to New Zealand. There are a very low number of non-passenger freighters used to carry airfreight commercially to the New Zealand market. s 9(2)(b)(ii)

Scenarios for passenger recovery are being prepared but there are none reflecting the most recent Reconnecting New Zealanders announcements

- 28 Cabinet directed the MIAC exit strategy to align with the passenger traveller scenarios prepared for the BEB. The intent of these scenarios is to provide a cross-government agreed set of scenarios for use in planning by agencies.

29 The current scenarios were approved by the BEB in December 2021, which was prior to the delay in step 1 and 2 of the Reconnecting New Zealanders strategy due to the impacts of the Omicron variant. A new set of scenarios is being prepared to take into account the new reopening dates announced on 3 February 2022. ^{s 9(2)(g)(i)}

30 Estimating passenger numbers is further hampered by uncertainty resulting from the unknown impact that ongoing self-isolation requirements will have on passenger demand. ^{s 9(2)(g)(i)}

The initial view from the scenario development team is that the new scenarios are expected to have passenger travel returning significantly later than the current scenarios suggest.

Passenger recovery will differ across markets

31 An additional complexity is that passenger recovery will differ significantly across markets, based on a range of factors:

31.1 Passenger reasons for travel / domestic isolation requirements – both Tourism New Zealand and airlines have indicated the requirement to self-isolate on arrival in New Zealand will be a significant determinant on overseas consumers' decisions to travel to New Zealand. This will differ by markets.

31.2 Foreign and domestic border settings – while forecast scenarios can account for the New Zealand domestic border setting options, foreign governments may change their own settings independently to New Zealand. This can be seen in the different approaches taken by countries such as Australia, Japan, and China to reopening their borders.

31.3 Seasonality – passenger travel from some markets to New Zealand often has a seasonal lull through the New Zealand winter (particularly Asian and European markets) though seasonality is not as strong in other markets such as Australia and the Pacific.

31.4 Public health response – there may need to be changes in border settings and / or stricter requirements on travellers from time to time as part of the response to Omicron or new variants.

32 As a result of the likely market-by-market differences in passenger recovery, decision-making regarding the MIAC is best done at the individual market level – rather than making a single decision about all markets.

MIAC arrangements already have exit controls in place

33 ^{s 9(2)(b)(ii)}

33.1 ^{s 9(2)(b)(ii)}

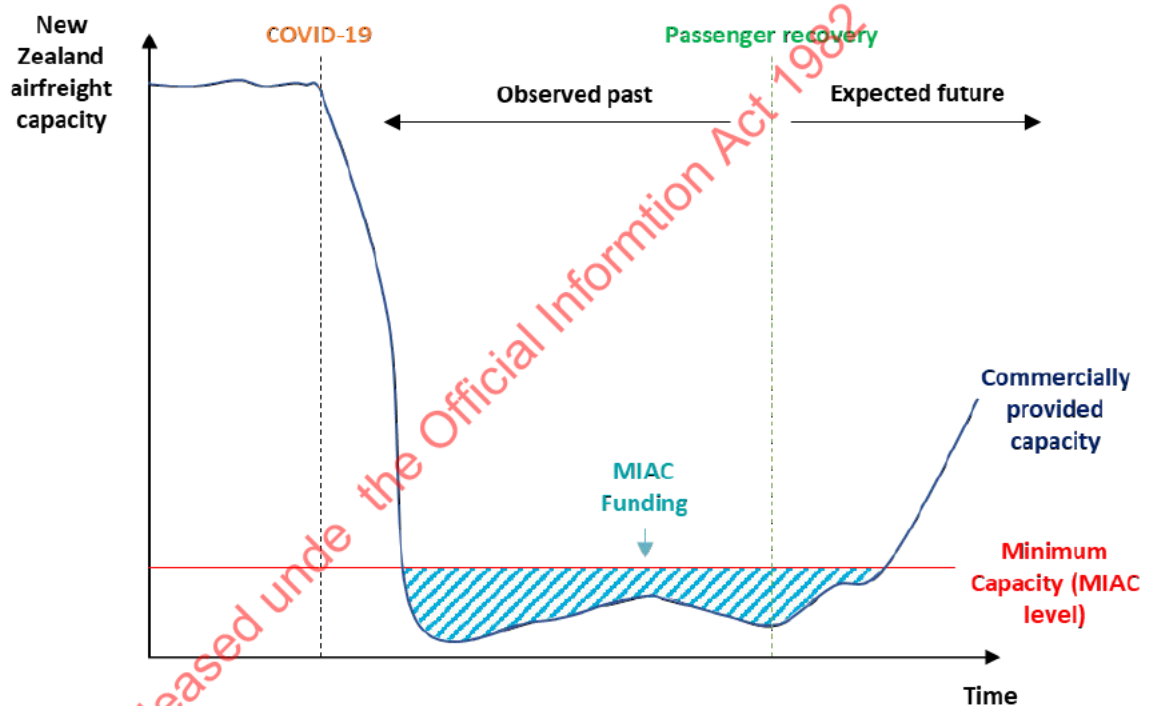
33.2 ^{s 9(2)(b)(ii)}

34

Fundamentally, the MIAC provides protection against the negative impacts of a lack in air connectivity

35 The below diagram⁶ illustrates at a conceptual level how the MIAC functions within the New Zealand airfreight market.

Passenger recovery concept



36 The MIAC supports a critical minimum capacity for the airfreight market, in the absence of commercially provided capacity available. As commercial capacity is provided, the amount of support required under the MIAC is decreased. At a certain point in time, the commercial capacity will be sufficient to provide the minimum level of connectivity, at which point the MIAC support is reduced to zero and no longer required.

37 The key consideration for the exit strategy of the MIAC is the uncertainty as to exactly when commercially provided capacity will exceed the minimum capacity on each route. Withdrawing support prior to that point risks a capacity shortfall for that route, however the on-going provision of support must be balanced against the downsides of the MIAC as noted in paragraph 20.

⁶ The diagram outlined uses a conceptual trend line rather than actual passenger numbers or forecasts.

A conditions-focused exit will best support the rebuild of air connectivity

- 38 I am proposing a conditions-focussed exit from the MIAC scheme. This is the best way to support the rebuild of air connectivity until sufficient passengers return and airlines can operate on a purely commercial basis.
- 39 The combination of using the scheme's existing mechanisms and putting in place a 'back-stop' date will mean MIAC support is not ended until sufficient flights are operating on a commercial basis. This will ensure there is no risk of an airfreight capacity gap arising prior to the 'back-stop' date.

Mechanisms in the scheme can be used to reduce or remove support on a route-by-route basis

40 This approach involves using the current mechanisms in the MIAC contracts to reduce support and then exit on a route-by-route basis when the growth in passenger numbers on a route means support is no longer needed to maintain airfreight capacity.

41 These mechanisms are:

- 41.1 s 9(2)(b)(ii) [Redacted]
- 41.2 s 9(2)(b)(ii) [Redacted]
- 41.3 s 9(2)(b)(ii) [Redacted]
- 41.4 s 9(2)(b)(ii) [Redacted]

42 An example of how these contractual mechanisms could be used to manage the exit of the MIAC scheme is the likely response to trans-Tasman re-connectivity under step 1 of Reconnecting New Zealanders:

- 42.1 s 9(2)(b)(ii) [Redacted] Existing contractual mechanisms means no support will be provided for those flights.

7 s 9(2)(b)(ii) [Redacted]

42.2 If reasonable passenger numbers are sustained, the Ministry will consider activating its rights to suspend or terminate these contracts.

A 'back-stop' date will ensure support is not extended indefinitely

43 I recognise that support for the MIAC can not be extended indefinitely while passenger travel conditions recover. Therefore, a 'back-stop' date is required. I propose 12 months from the expiry of the current MIAC contracts – i.e. 31 March 2023.

44 The Ministry has calculated end dates for each market based on passenger volumes reaching 20% of pre-COVID-19 levels. In general, each market reaches a 12-month cap before the 20% level in the pessimistic scenario.

45 There is some residual risk passenger recovery has not been sufficient at the contractual end date, resulting in a capacity gap. However, under the pessimistic scenario, markets that have been constrained by the 'back-stop' dates are each expected to be above 10% of pre-COVID passenger levels at March 2023.

46 s 9(2)(g)(i)



The benefit of a conditions-focussed approach is improved security of airfreight connections over the next year

47 A conditions-focussed exit:

47.1 Presents a stronger link to the return of passenger numbers, by waiting to remove support until such time as the market delivers passenger movements that enable sector participants to consistently break-even.

47.2 Mitigates the risk of capacity shortfalls or further shocks that might occur under the alternative option if the moderate scenario does not occur and comes at the potential cost of up to an additional s 9(2)(b)(ii) over the alternative option.

48 s 9(2)(g)(i)



49 s 6(a)



50 s 9(2)(g)(i) [Redacted]

51 s 9(2)(g)(i) [Redacted]

A date-based exit is not recommended

52 I also considered an alternative approach of a date-based exit that involves pre-determined exit dates for each route based on the moderate scenario prepared for the BEB in December 2021. Under this approach, each market has their MIAC contract extended until the date that market is expected to reach approximately 20% of the pre-COVID baseline of passenger numbers according to the moderate passenger travel scenario.

A date-based exit relies heavily on the accuracy of scenarios

53 s 9(2)(g)(i) [Redacted]

54 The Ministry has calculated end dates for each market based on passenger volumes reaching 20% of pre-COVID-19 levels. These dates are provided in **Appendix 1**.

55 There is a high risk to connectivity as this approach relies on the scenarios being accurate across each individual market. This risk is increased by reliance on the mid-December scenario, because the revised scenario is expected to indicate slower passenger return. It is possible, but complex, to build this scenario off the future, updated forecast instead. Where the scenarios are not accurate and passenger returns are below expectations, there would be expected to be a capacity gap at the end date if the shortfall is below the minimum necessary range of 10 - 20% of pre-COVID passenger numbers.

56 The extent of a potential capacity gap could be quite significant. For example, if the actual passenger returns follow the pessimistic track as opposed to the moderate, there is an expected shortage of ~12% of pre-COVID baseline (i.e. passenger numbers are at 8% of baseline instead of 20%, which equates to over 50% less than expected) at the end date for the trans-Tasman routes. For other markets, the capacity gap is even greater – at the exit date, the pessimistic scenario predicts only around 6% of pre-COVID levels.

57 s 6(a) [Redacted]

58 The Treasury considers that the date-based option provides a reasonable balance by mitigating the risk of capacity shortfalls while New Zealand progressively opens up its borders, while at the same time reinforcing the Reconnecting New Zealanders approach. Subject to certainty around future self-isolation requirements, this option

would also support greater confidence for market participants to plan longer-term. This mitigates the risk of entrenching market distortions by providing a clear exit strategy and reduces fiscal risk to the Crown.

59 However, the Treasury acknowledges this option carries a risk of capacity shortfalls if the moderate passenger scenario does not play out. This risk is somewhat mitigated as the date-based exit is based on anticipated 20 per cent of baseline passengers, and minimum viable capacity has been articulated as around 10 to 20 per cent, suggesting there is some room for capacity movements even under this option. Finally, the Treasury is unclear that the marginal benefit of extending the MIAC to March 2023 outweighs the potential marginal cost over this option of up to s 9(2)(b)(ii).

s 6(a), s 9(2)(g)(i)

[Redacted]

[Redacted]

[Redacted]

[Redacted]

64 s 9(2)(b)(ii)

[Redacted]

Immediate exit

65 I also considered an immediate exit to the MIAC scheme, but ruled it out as a viable option as the impacts on airfreight connectivity would be too severe to justify the fiscal savings.

66 No agency supported an immediate exit.

Financial Implications

67 Additional funding is required to be approved by Cabinet to give effect to the implementation of the conditions-focused exit.

68 The expected spend under the conditions-focused exit is s 9(2)(b)(ii). A key factor is the progressive drop-off in support payable as passenger travel returns and has been calculated by reference to the moderate scenario prepared for the BEB in December 2021. The actual cost of support may be higher or lower if passenger travel returns faster or slower than contemplated in the scenario; the timing of removal of self-isolation will have a significant influence.

69 s 9(2)(b)(ii) [Redacted]

70 The funding requirement (non-departmental) is as follows:

s 9(2)
(b)(ii) [Redacted]

Legislative Implications

71 There are no legislative implications.

Regulatory Impact Statement

72 No Regulatory Impact Statement is required as this proposal does not introduce or change any legislation.

Climate Implications of Policy Assessment

73 A Climate Implications of Policy Assessment (CIPA) has not been prepared for this paper. The proposal recommends providing financial support for fossil fuel intensive international air transport, which creates greenhouse gas emissions. Even with this support it should be recognised that the total number of flights per week operating to and from New Zealand would still be less than a quarter of the number of flights operating prior to COVID-19. This represents a sizable reduction in the emissions attributable to New Zealand's international air services.

74 It is also worth noting that air freight is being carried significantly more efficiently now than it was pre-COVID. Around 90% of pre-COVID export volumes are being carried on around 25% of the flights. Flights supported by government charge freight rates which are higher than pre-COVID rates, which will encourage those traders who are able to do so consider other, less emission-intensive models for transporting their products to market. Additionally, over the last 18 months, airlines have largely retired their older, less efficient aircraft meaning that emissions from flights to and from New Zealand should be, on average, lower than pre-COVID.

Population Implications

75 Changes to New Zealand's international air connectivity could affect Māori, and rural and coastal communities in particular. 80% of New Zealand's air freight exports (by volume) are primary sector products. A number of iwi have their largest investments in primary industries and tourism, so have been particularly exposed to the collapse in air services caused by COVID-19. The purpose driven business model of many Māori enterprises that includes financial performance and whanau wellbeing means that air service disruption could have wide ranging knock-on effects for the Māori community.

76 Rural and coastal communities, and some regions, could be affected because the local economies in those areas are concentrated on the production of goods and services for export by air e.g. fishing communities, or horticulture in the Auckland region, and international tourism in parts of Otago and the West Coast. Constraints

on the ability to export products in the immediate-term, or for recovery in the medium-term could reduce incomes and lead to job losses in those areas.

Human Rights

77 There are no implications for human rights.

Consultation

78 The following agencies were consulted in the process leading up to the development of this paper: Treasury, Ministry of Foreign Affairs and Trade, Ministry for Primary Industries, Ministry for Business, Innovation and Employment, New Zealand Trade and Enterprise. Department of Prime Minister and Cabinet was consulted.

Communications

79 I will make a public announcement on the exit strategy of the MIAC scheme following Cabinet's decision. I recommend this announcement be made as soon as possible following Cabinet's decision.

80 The Ministry will communicate the details of implementation to the affected airlines, and work with other agencies including MFAT, MPI and NZTE to ensure that affected industry groups are aware that support for air services will continue to be available. I recommend the Ministry can communicate these details to airlines immediately following Cabinet's decision (subject to any airline announcements being embargoed until a formal announcement is made).

Proactive Release

81 Not proposed due to the discussion of matters which are commercially sensitive, and sensitive to New Zealand's international relations.

Recommendations

The Minister of Transport recommends that the Committee:

- 1 **Note** that the MIAC scheme has been in operation since 1 May 2021, and is set to expire on 31 March 2022 and has contributed to a minimum level of air connectivity for New Zealand, which is around 10-20% of pre-COVID flight volumes;
- 2 **Note** that the recovery of airfreight connectivity for New Zealand is reliant on the return of passenger travel, and the Border Executive Board scenarios from December 2021 outline a return to 20% of pre-COVID flight volumes around June 2022 under a moderate scenario and around January 2023 under a pessimistic scenario;
- 3 **Note** that the approved passenger traveller scenarios are set to be updated in mid-March 2022 to reflect latest developments in the implementation of the Reconnecting New Zealanders strategy;
- 4 **Note** that a key assumption affecting the return of passengers is the timing of removal of the self-isolation requirements;

5 s 6(a)



[REDACTED]

6 **Note** the Treasury view that my preferred approach of extending the existing MIAC contracts to March 2023 removes support when passenger numbers return to a point where airlines break even, ^{s 9(2)(g)(i)} [REDACTED], and could cost up to ^{s 9(2)(g)(ii)} [REDACTED] more than a date-based option that aligns with the existing moderate scenario for passenger returns;

7 **Note** that my preferred approach of the conditions-based exit significantly reduces the risk of damaging capacity shortfalls in air capacity by providing a strong link to the return of passenger numbers. Where conditions improve this option carries the same total fiscal cost as the alternative suggested.

8 **Agree to EITHER:**

8.1 my preferred approach of a conditions-focussed exit as the approach to the exit of the MIAC scheme, extending current MIAC contracts for all markets to 31 March 2023 but with contracts being actively managed to end support as passengers return. **(Recommended)**

OR

8.2 the alternative option of a date-based exit as the approach to the exit of the MIAC scheme, extending current MAC contracts to the dates set out in Appendix 1 when the current passenger forecasts indicate that passenger numbers will be sufficient. **(Not recommended)**

9 ^{s 9(2)(g)(i)} [REDACTED]

10 **Authorise** the Ministry of Transport to enter into contracts with airline providers to reflect the new contract end dates considered in recommendation 8 above.

11 **Agree** that the Minister of Transport will work with the Minister for Trade and Export Growth to agree the terms of public announcements of any extension so as to seek to minimise as far as possible the ^{s 6(a)} [REDACTED]

12 **Agree** to extend the Maintaining International Air Services MYA from 30 June 2022 to 30 June 2023 to support the decision in recommendation 7 above.

13 **Approve EITHER**

13.1 if you agree to recommendation 8.1 above (conditions-focussed exit – recommended) the following changes to appropriations to provide for the decision in recommendation 8 above, with corresponding impacts on the operating balance:

s 9(2)(b)(ii)

OR

- 13.2 if you agree to recommendation 8.2 above (date-based exit – not recommended) the following changes to appropriations to provide for the decision in recommendation 8 above, with corresponding impacts on the operating balance:

s 9(2)(b)(ii)

- 14 **Agree** that the expenses incurred under recommendations 8 above be charged as a pre-commitment against the Budget 2022 operating allowance;
- 15 **Agree** that the proposed changes to appropriations for 2021/22 above be included in the 2021/22 Supplementary Estimates and that, in the interim, the increase be met from Imprest Supply;
- 16 **Note** that the appropriation changes above are associated with a Budget 2022 bid, which will be withdrawn if the recommendations above are agreed.

Authorised for lodgement

Hon Michael Wood

Minister of Transport

Released under the Official Information Act 1982

Appendix 1

Date-based exit – contract extensions by market:

- Trans-Tasman: 31 August 2022
- North America: 31 August 2022
- Asia: 30 November 2022
- Middle East: 30 September 2022
- Pacific: 31 March 2023

Released under the Official Information Act 1982

From: [Brent Lewers](#)
To: [Seb \(Parliament\) Brown](#)
Cc: [Tom Gillard](#); [James Macleod](#); [Jessica Ranger](#); [Carmen Mak](#)
Subject: James for review by 10am please
Date: Thursday, 10 March 2022 9:29:10 pm

James, could you please have a look at this and let me know what you think?

s 9(2)(g)(i)

A large block of text is redacted with grey bars. The redaction covers approximately seven lines of text.

Here's a suggested response:

It is unclear whether this policy initiative will result in a level of emissions which exceed the threshold.

The counterfactual is uncertain. In the absence of the support scheme a smaller subset of flights is likely to have operated carrying some freight, perhaps on a charter basis. As the Reconnecting New Zealanders decisions start to take effect, passenger demand increases, and again, it is likely that in the absence of a support scheme a smaller subset of flights would be operated on a commercial basis to meet that passenger demand.

The other uncertainty is the number of flights that will actually be supported over the next twelve months. The government is confident that support for most routes will be able to be reduced and then ended before the final date of 31 March 2023, but exactly how that will eventuate depends on unknowns, including the rate of growth of demand for passenger travel across different routes and the extent to which other countries apply or remove travel restrictions.

From: Seb Brown <Seb.Brown@parliament.govt.nz>
Sent: Thursday, 10 March 2022 5:11 pm
To: Brent Lewers <B.Lewers@transport.govt.nz>
Cc: Tom Gillard <T.Gillard@transport.govt.nz>; James Macleod <J.Macleod@transport.govt.nz>; Jessica Ranger <J.Ranger@transport.govt.nz>; Carmen Mak <C.Mak@transport.govt.nz>
Subject: RE: One Transport oral question today from the Labour Party

Thanks Brent. If you/someone could send me a response to this by 10am tomorrow morning, that would be great.

Seb Brown

Private Secretary – Transport

M: [s 9\(2\)\(a\)](#)

From: Brent Lewers [<mailto:B.Lewers@transport.govt.nz>]

Sent: Thursday, 10 March 2022 1:44 PM

To: Seb Brown <Seb.Brown@parliament.govt.nz>

Cc: Tom Gillard <T.Gillard@transport.govt.nz>; James Macleod <J.Macleod@transport.govt.nz>; Jessica Ranger <J.Ranger@transport.govt.nz>; Carmen Mak <C.Mak@transport.govt.nz>

Subject: RE: One Transport oral question today from the Labour Party

Thanks Seb, will come back to you on this.

Someone – quite possible the same person - asks this every time we extend. s 9(2)(g)(i)

Brent

From: Seb Brown <Seb.Brown@parliament.govt.nz>

Sent: Thursday, 10 March 2022 12:54 pm

To: Brent Lewers <B.Lewers@transport.govt.nz>

Cc: Tom Gillard <T.Gillard@transport.govt.nz>; James Macleod <J.Macleod@transport.govt.nz>; Jessica Ranger <J.Ranger@transport.govt.nz>; Carmen Mak <C.Mak@transport.govt.nz>

Subject: RE: One Transport oral question today from the Labour Party

Hi all

Another MIAC question for you – this is just a media query and isn't related to the OPQ.

We received a question “Was a CIPA done for this latest extension of the MIAC?” – and from the Cabinet paper I see the below:

- 1 A Climate Implications of Policy Assessment (CIPA) has not been prepared for this paper. The proposal recommends providing financial support for fossil fuel intensive international air transport, which creates greenhouse gas emissions. Even with this support it should be recognised that the total number of flights per week operating to and from New Zealand would still be less than a quarter of the number of flights operating prior to COVID-19. This represents a sizable reduction in the emissions attributable to New Zealand's international air services.
- 2 It is also worth noting that air freight is being carried significantly more efficiently now than it was pre-COVID. Around 90% of pre-COVID export volumes are being carried on around 25% of the flights. Flights supported by government charge freight rates which are higher than pre-COVID rates, which will encourage those traders who are able to do so consider other, less emission-intensive models for transporting their products to market. Additionally, over the last 18 months, airlines have largely retired their older, less efficient aircraft meaning that emissions from flights to and from New Zealand should be, on average, lower than pre-COVID.

The follow up question from the journalist was:

“Should I take this to mean the Government didn't think the “direct impact [of the extension] on

greenhouse gas emissions is likely to be equal to or above 0.5 million tonnes CO2-e”? Noting that the [CIPA requirements](#) are about comparing the impact of the policy with a no-policy scenario, not a pre-pandemic scenario.”

Can you please let me know your thoughts on how we should respond to this?

Thanks

Seb Brown

Private Secretary – Transport

M: s 9(2)(a)

Released under the Official Information Act 1982

Commercial in Confidence

Office of the Minister of Transport

Cabinet Economic Development Committee

COVID-19- Extension of the Essential Transport Connectivity (ETC) Scheme to 2022

Proposal

- 1 This paper seeks agreement to extend the Essential Transport Connectivity (ETC) Scheme to 30 April 2022 to align with the proposed commencement of Step 3 of Reconnecting New Zealanders. It also informs Cabinet of the proposed approach to maintaining interregional connectivity in the South Island in the absence of international tourists.

Relation to government priorities

- 2 This proposal supports the Government's economic response to COVID-19 through its efforts to cushion the financial blow to whānau and families, workers, businesses and communities from the impacts of COVID-19, position New Zealand for recovery, and reset and rebuild our economy.

Executive Summary

- 3 The Essential Transport Connectivity Scheme (ETC) supports the continued operation of essential transport routes and services in the face of COVID-19 travel restrictions and reduced passenger demand. The ETC is due to expire on 31 December 2021.
- 4 I recommend Cabinet agree to extend the ETC scheme to 30 April 2022 to align with the planned Step 3 of Reconnecting New Zealanders and to ensure essential transport services are maintained while domestic travel recovers from the impact of the current, and any future, COVID-19 restrictions. Extending the ETC scheme ensures that transport connections can be maintained despite the uncertain impact of COVID, and places New Zealand and its transport operators in a strong position for recovery. Given the proposed staged approach to Step 3, I will come back to Cabinet closer to the time if passenger numbers do not look sufficient and further extension is necessary.
- 5 Extending the ETC does not automatically commit the Government to providing funding for services. ETC funding agreements are generally short term to ensure that the ETC is not locked into providing support for longer than is necessary. s 9(2)(b)(ii)
The level of support provided decreases as passenger numbers increase. The ETC being available to provide support does not mean that it will always do so.
- 6 I expect the extension to cost an average of s 9(2)(b)(ii) per month s 9(2)(b)(ii). The actual spend may in fact be much lower as passenger travel increases, and the amount of support required declines. The extension does not require any new funding as there is sufficient funding remaining within the existing ETC appropriation. At this stage I expect there to be \$12.929m remaining at 31 December 2021 to fund the extension and any new ETC applications received over the coming months.

- 7 I also recommend Cabinet agree that funding for South Island interregional bus services be available through to 30 June 2022 (i.e. beyond the 30 April 2022 end date set out above). ^{s 9(2)(b)(ii)}

The Ministry of Transport will also work with regional councils to investigate ways to transfer responsibility for these services away from the ETC and central Government from 30 June 2022.

The ETC was established to ensure essential transport connections were maintained despite the impacts of COVID-19

- 8 From March 2020, the COVID-19 lockdowns and Alert Levels resulted in local and domestic travel restrictions which significantly impacted the operation of some transport routes and services. These routes were either unable to be operated or operated at reduced capacity due to social distancing requirements. Additionally, New Zealand closed its borders to international travellers. These closures saw the disappearance of the international tourism market overnight and resulted in a marked decrease in domestic travel.
- 9 The dramatic decrease in passenger demand and revenue placed some transport operators and service providers under immense pressure, causing services to be cancelled, threatening the viability of some operators, and exposing potential gaps in regional connectivity. It also created a risk that the ability of New Zealand's transport services to recover post-COVID-19 would be significantly impacted.
- 10 The ETC scheme was established by Cabinet on 11 May 2020 to provide support to maintain these essential routes and services negatively impacted by COVID-19 [CAB-20-MIN-0219.28]. The scheme enables the government to respond quickly where the failure of a transport service would have significant negative social and economic outcomes and would impact New Zealand's post COVID resilience and recovery. The ETC scheme's funding comprised:
- 10.1 \$20 million to enable support for non-aviation essential transport operators [CAB-20-MIN-0219.28]; and
 - 10.2 \$30 million to fund aviation initiatives under the scheme from the underspend of the \$600 million aviation relief package. This was subsequently reduced to \$10.7m to fund an extension of the International Airfreight Capacity scheme in September 2020.
- 11 The Ministry of Transport and the Treasury completed a review of the ETC scheme in April 2021 and recommended that the scheme be extended to 30 September 2021. Cabinet agreed to this extension and authorised joint Ministers¹ to extend the scheme for a further three months (up to 31 December 2021) if Ministers assessed that there is an ongoing need for support [CAB-21-MIN-0180].

¹ The Minister of Transport, Minister of Finance, Associate Minister of Finance responsible for aviation matters, and the Minister of Economic and Regional Development.

- 12 In response to the August 2021 COVID-19 outbreak in Auckland and the return to Alert Level 4 across New Zealand, joint Ministers agreed to extend the ETC to 31 December 2021. Cabinet agreement is required to extend the ETC beyond this date.

The current Delta outbreak has lengthened the impact of COVID-19 on New Zealand's domestic transport services

- 13 On 17 August 2021, New Zealand returned to Alert Level 4 nationally as a result of community cases of the COVID-19 Delta variant. Auckland remains at Alert Level 3 with the rest of the country at Alert Level 2. Since the emergence and taking hold of the Delta variant, the Government has signalled a shift away from its elimination strategy and move to a COVID-19 Protection Framework. The new framework is not expected to come into effect across the country before mid December (at the earliest) and may not apply to all of New Zealand equally (particularly in the event that local restrictions are required to protect the healthcare system or vulnerable population groups).
- 14 New Zealand's vaccine rollout has progressed at pace and there is expected to be a general relaxation of New Zealand's domestic COVID-19 settings under the COVID-19 Protection Framework. However, there is still significant uncertainty about what New Zealand's border settings and domestic restrictions will look like over the coming weeks and months. While it is possible that under the COVID-19 Protection Framework some services quickly become commercially viable, we do not expect this to be the case for all routes and services – particularly for those services which traditionally relied on international tourists to subsidise services for New Zealanders. There is a risk that:
- 14.1 In the immediate term, interregional travel settings remain in a state of flux with the return of some restrictions necessary to protect the healthcare system or high risk groups;
 - 14.2 In the short term, even with high vaccination rates and few to no travel restrictions, there is continued travel hesitancy and low passenger demand. If this occurs, then some essential transport routes and services may continue to be unviable;
 - 14.3 In the medium term, as a result of new variants of concern, a significant domestic resurgence, reduced vaccine effectiveness, or other unforeseen events, New Zealand faces a return to regional lockdowns and domestic travel restrictions. These events would mean that the ETC was once again needed to quickly stand-up support to ensure essential connections are maintained; and
 - 14.4 In the longer term, international tourists, which are an important source of revenue for many services which are also relied on by New Zealand travellers, may take some time to return as the Reconnecting New Zealanders strategy is implemented.
- 15 We know that even last summer, when there were no domestic transport restrictions or COVID-19 cases in the community, many essential transport services were unable to cover their costs of operating. It is a reasonable assumption that passenger demand over the coming months will be lower than last year. The emergence of the Delta variant in New Zealand, an unfamiliar COVID-19 alert framework, and increased travel hesitancy as a result of recent lockdowns are likely to mean that

fewer New Zealanders will be willing to travel long distances or rely on transport outside of a private vehicle over summer.

I propose that the ETC scheme be extended to 30 April 2022 to ensure that essential transport connections are maintained while domestic travel recovers

- 16 I consider it prudent to keep the ETC scheme in place until 30 April 2022. This would ensure that essential transport connectivity can be maintained while domestic travel increases and changes to New Zealand's COVID-19 settings are implemented. An extension of the scheme ensures that domestic transport operators have the confidence they need to schedule services, and passengers know that those services are not going to be cancelled on them at short notice if they might operate at a loss.
- 17 The 30 April end date aligns with the anticipated Step 3 of Reconnecting New Zealanders. At this point, eligible fully vaccinated travellers would be able to return to New Zealand in accordance with the staged approach proposed to be taken under step 3. Coupled with the earlier steps of Reconnecting New Zealanders (which will see an increase in New Zealanders wanting to travel to overseas departure points which boosts demand and the viability of essential transport services), it is hoped that demand for domestic services will be such that ETC support is no longer required.
s 9(2)(f)(iv)
- 18 Extending the scheme also means that the ETC remains in place to provide rapid support in the event there are future lockdowns or unanticipated COVID-19 events. We have recently seen the value in being able to quickly respond to the impact of domestic travel restrictions. When New Zealand returned to Alert Level 4 in August 2021, the ETC was able to rapidly provide support to ensure that critical supplies continued to flow to isolated communities. For example, from 17 August to 4 November 2021, the ETC enabled over 190,000kgs of critical supplies (including fresh food and COVID-19 vaccines) to reach the residents of Great Barrier Island who would have otherwise been cut off.
- 19 I recommend Cabinet agree to extend the ETC scheme to 30 April 2022. This extension can be fully funded within the ETC's existing funding allocation. The ETC currently spends an average of ~s 9(2)(b)(ii) per month. We expect the amount of support required from operators to slowly decrease as passengers return. However, even if the ETC continues to provide support at its historic rate for the entire extension period, only s 9(2)(b)(ii) would be required. I expect the ETC to have \$12.929m remaining at 31 December 2021 to fund the extension (assuming no unexpected, large funding applications are received and approved between now and 31 December).
- 20 Extending the scheme does not mean all the support agreements currently in place would be automatically extended or funding provided. The Ministry of Transport would continue to enter into agreements under which s 9(2)(b)(ii) As passenger numbers increase, the cost to the Government automatically decreases. Support arrangements would continue to be regularly reassessed to determine whether support was still required.

I recommend that Cabinet delegate some future funding decisions to the Secretary for Transport

- 21 If Cabinet agree to extend the ETC scheme to 30 April 2022 then I recommend delegating some future, low value, funding decisions to the Secretary for Transport. For all other funding decisions, the current delegation of decisions to joint Ministers would continue to apply. The following framework sets out the limits of the proposed delegation to the Secretary.
- 21.1 approvals are delegated until 30 April 2022;
 - 21.2 the applicant meets (or still meets) the eligibility criteria;
 - 21.3 the funding agreement does not extend beyond 30 April 2022;
 - 21.4 the approval or extension is within a funding envelope of up to \$0.500m per agreement;
 - 21.5 the Treasury agrees that an application or extension should be put to the Secretary for consideration; and
 - 21.6 the Secretary for Transport may delegate his authority to a Deputy Chief Executive of the Ministry of Transport.
- 22 As under previous delegations, the Ministry would continue to seek joint Ministers' approval where decisions are outside of the delegation to the Secretary for Transport, are considered sensitive, or where the Secretary determines that seeking Ministerial approval is appropriate.

Regardless of a relaxation of domestic COVID-19 restrictions, I do not expect some interregional bus services in the South Island to be viable until international tourists return

23 s 9(2)(b)(ii) [Redacted] These regions have a low population density and have traditionally relied on international tourists to make transport services for residents viable. s 9(2)(b)(ii) [Redacted]

24 s 9(2)(b)(ii) [Redacted]

25 s 9(2)(b)(ii) [Redacted]

s 9(2)(b)(ii)

[Redacted]

26 Joint Ministers have agreed that should Cabinet agree to extend the ETC scheme, the Ministry of Transport will run an open market procurement to seek other operators who could stand up services on the West Coast and Christchurch to Queenstown (inland) routes. s 9(2)(g)(i)

[Redacted]

there is no guarantee that any operator would be willing to stand up new services in the current environment without some Government support – even if just to cover any losses while a new service is established.

27 s 9(2)(b)(ii), s 9(2)(g)(i)

[Redacted]

While more international visitors are expected from 30 April under step 3, the return of these travellers is likely to be staged. A meaningful increase in passenger numbers is unlikely to happen overnight.

28 I propose Cabinet agree that funding for South Island regional bus services be available to 30 June 2022 to allow a worthwhile procurement to take place (i.e. funding would be available beyond the 30 April 2022 date proposed for all other routes/services). s 9(2)(b)(ii)

[Redacted]

This funding is already included in the cost estimates for the ETC, so no new funding is required to support the procurement.

Implementation

29 I propose that following agreement from the Cabinet, the Ministry of Transport:

- 29.1 Reassess all operators, at the time their next extension, against the ETC eligibility criteria;
- 29.2 Continue operation of the scheme until 30 April 2022 (and 30 June 2022 for the South Island interregional bus services);
- 29.3 Begin initial market engagement on the procurement for South Island interregional bus services; and
- 29.4 Prepare advice for joint Ministers on whether the staged approach to step 3 of Reconnecting New Zealanders means the scheme needs to be extended beyond 30 April 2022, and provide this advice to joint Ministers in March 2022 so that I can return to Cabinet for a further decision if required.

Financial Implications

30 No new funding is required to support this initiative. The ETC scheme has sufficient funding remaining in the current financial year (\$12.929m is expected to remain at 31 December 2021) to keep the ETC operating at the same, or a reduced level, well beyond 30 June 2022. ^{s 9(2)(f)(iv)}

31 There is a risk that new applications are made for the ETC which reduce the amount of funding available. For example, the Ministry recently received an application for support ^{s 9(2)(b)(ii)}

The risk of there being an overspend from the ETC or new funding required in the current financial year is low.

Risks and mitigations

32 ^{s 9(2)(f)(iv) and s9(2)(g)(i)}

Legislative Implications

33 There are no legislative implications.

Regulatory Impact Statement

34 No Regulatory Impact Statement is required as this proposal does not introduce or change any legislation.

Climate Implications of Policy Assessment

35 A Climate Implications of Policy Assessment (CIPA) has not been prepared for this paper. The proposal recommends providing financial support for transport operators and services, which creates greenhouse gas emissions. Even with this support it should be recognised that the total number of domestic flights and road/sea transport services provided per week would still be materially less than the number which operated prior to COVID-19. As part of the procurement of South Island interregional bus services we may consider the age of an applicant's fleet and emissions profile as part of the assessment process.

36 More broadly I am looking at how to reduce emissions from the transport sector as part of the 'Hīkina te Kohupara – Kia mauri ora ai te iwi - Transport Emissions: Pathways to Net Zero by 2050' work programme.

Population Implications

37 This proposal has the following anticipated population impacts.

Table 1. ETC extension population implications

Population group	How the proposal may affect this group
Remote/rural populations	Many regions cannot justify transport services based solely on domestic population and they continue to be unviable without international tourists. Many more remote communities and individuals do not have nearby access to essential services (such as health and welfare services) and may not be able to travel to the nearest essential service without a transport connection.
Elderly, vulnerable, and disabled people	Many of the services support by the ETC scheme to date disproportionately support the elderly, vulnerable, and disabled people. These groups often have limited access to private vehicles, struggle with standard transport options, or have complex needs which require regular transport to a main centre to access.

Human Rights

38 There are no implications for human rights.

Consultation

39 The Treasury has been consulted on this paper.

Communications

40 I do not intend to make a formal public announcement of the extension of the ETC scheme as those transport operators and services that are expected to require support are already under the scheme or have been offer the opportunity to apply and have either been declined or chose not to submit an application. The Ministry of Transport will communicate directly with affected parties.

41 I do not intend to formally announce the procurement opportunity for South Island interregional bus services. However, the opportunity will be posted on GETS and the Ministry will engage directly with the affected regional councils and potential operators as part of initial market engagement.


Proactive Release

42 Not proposed due to the extensive discussion of matters which are commercially sensitive.

Recommendations

I recommend that the Committee:

- 1 note that on 11 May 2020 Cabinet established the Essential Transport Connectivity (ETC) Scheme to provide support to maintain essential transport routes and services negatively impacted by COVID-19 [CAB-20-MIN-0219.28].
- 2 note that the ETC scheme is due to end on 31 December 2021 and Cabinet agreement is required to extend the scheme further.
- 3 note that we expect there to be \$12.929m in unallocated ETC funding remaining at 31 December 2021.

- 4 note that the impact of the current COVID-19 outbreak is likely to be felt for some time and it is likely that ETC support will be required for the first part of 2022 as passenger travel begins to recover from the impact of recent COVID-19 restrictions.
- 5 note that Step 3 of the Reconnecting New Zealanders approach would see fully vaccinated eligible travellers able to enter New Zealand from 30 April 2022, under a staged process.
- 6 agree that the ETC Scheme be extended to 30 April 2022 to align with Step 3 of Reconnecting New Zealanders and to allow time for domestic travel to recover from the impacts of the recent Alert Level increases.
- 7 s 9(2)(f)(iv) 
- 8 delegate authority to the Secretary for Transport to enter into funding agreements in accordance with the delegation framework set out in paragraph 21.
- 9 note that the extension of the ETC scheme to 30 April 2022 does not require any new funding and can be funded through the existing ETC multi-year appropriation.
- 10 note that subject to Cabinet agreeing to extend the ETC scheme, joint Ministers intend to run an open market procurement for the interregional South Island bus services currently supported by the ETC scheme (West Coast and inland services from Christchurch to Queenstown).
- 11 agree that funding for the South Island interregional bus services referred to in recommendation 10 be available to 30 June 2022 (i.e. regardless of the 30 April 2022 end date for the ETC scheme set out in recommendation 6).

Authorised for lodgement

Hon Michael Wood

Minister for Transport

Commercial in Confidence

Office of the Minister of Transport

Cabinet Economic Development Committee

COVID-19: Maintaining International Air Connectivity (MIAC) scheme extension funding

Proposal

- 1 This paper seeks Cabinet's agreement to extend the Maintaining International Air Connectivity (MAIC) scheme from 31 October 2021 to 31 March 2022 and to allocate an additional \$125m to support an extension of the scheme and an additional \$25m to ensure connectivity is maintained during future QFT pauses or suspensions.

Relation to government priorities

- 2 This proposal supports the Government's economic response to COVID-19 through its efforts to cushion the financial blow to whānau and families, workers, businesses, and communities from the impacts of COVID-19, position New Zealand for recovery, and reset and rebuild our economy.

Executive Summary

- 3 The MIAC scheme is set to expire on 31 October 2021. Cabinet previously authorised joint Ministers¹ to extend the scheme to 31 March 2022, if they considered an extension necessary, using a \$100m tagged contingency for the extension [CAB-21-MIN-0063 refers].
- 4 However, the \$100m in tagged contingency is no longer enough to support New Zealand's connectivity needs. Additionally, Cabinet already reallocated \$30m of the tagged contingency to support trans-Tasman flights during the current suspension of quarantine-free travel (QFT) with Australia [CAB-21-MIN-0288 refers]. This leaves only \$70m available for the five month extension period which would leave a significant capacity shortfall over the peak export/import season.
- 5 Without additional funding the Ministry of Transport would need to reduce the number of flights and routes supported under the MIAC which would leave a significant capacity shortfall over the peak export season. The Associate Minister of Finance and I recommend that Cabinet agree to extend the MIAC scheme to 31 March 2022, allocate an additional \$125m for the extension period (on top of the remaining \$70m tagged contingency), and set aside an additional \$25m to ensure connectivity is maintained during future QFT pauses or suspensions.

- 6 s 9(2)(g)(i) 

¹ The Minister of Transport and the Associate Minister of Finance responsible for aviation matters

7

s 9(2)(g)(i)

8

s 9(2)(h)

Background

9 In March 2021, Cabinet agreed to establish a new scheme (the MIAC) to support international air connectivity after the expiry of the International Air Freight Capacity (IAFC) scheme [CAB-21-MIN-0063]. The MIAC is a market-led scheme. It provides 'top-up' funding to airlines to ensure connectivity is provided on key routes. Recipients then offer air services to freight customers and passengers on commercial terms.

10 The MIAC has been in place since 1 May 2021 and is due to end on 31 October 2021. The scheme currently supports 9 carriers to operate flights to 17 destinations (excluding Australia, noting that support for trans-Tasman flying is provided during suspensions of QFT). The total budget for the MIAC to 31 October 2021 is \$170m.

11 As at 20 July 2021, airlines had received s 9(2)(b)(ii) in support, carried over 19,000 tonnes of freight, and operated 1,104 flights since 1 May 2021. The inbound and outbound freight carried on MIAC funded flights since May 2021 is estimated to have had a value of \$1.5 billion. In total, both the MIAC and its predecessor IAFC scheme have enabled the movement of over 156,000 tonnes of freight with an estimated value of \$12.5 billion.

12 When Cabinet established the MIAC it agreed to set aside \$100m in a tagged contingency for use if the MIAC was extended beyond 31 October 2021. On 22 July 2021, Cabinet agreed to draw down \$30m of the \$100m tagged contingency to support continued freight connections with Australia while trans-Tasman QFT was suspended [CAB-21-MIN-0288 refers].

13 It was signalled that this transfer would leave only \$70m available for the period 1 November to 31 March and that this amount was unlikely to be enough to provide all the international connectivity required if the MIAC was extended. By way of comparison, the previous IAFC scheme paid s 9(2)(b)(iii) to airlines over the same period in 2020/21 (\$145.5m excluding Tasman services) at an average of s 9(2)(b)(iii) per week.

14 Cabinet authorised joint Ministers to extend the scheme to 31 March 2022 if they assessed that there was a need to continue providing support for international air connectivity [CAB-21-MIN-0063 refers]. Both the Associate Minister of Finance and I

have agreed that an extension of the MIAC is warranted, and that additional funding is required to enable an extension.

- 15 The remainder of this paper sets out the considerations made during our decision to seek Cabinet's agreement to the extension of the MIAC and to the additional funding.

There is a strong case for continued support for international air connectivity

- 16 After considering advice from the Ministry of Transport and consulting our colleagues, the Associate Minister of Finance and I believe that an extension of the MIAC scheme to 31 March 2022 is necessary. An extension of the scheme will ensure that the benefit of maintaining New Zealand's international air connectivity to date is retained, and ensure New Zealand is well positioned for a gradual reopening of the border over the coming months. Our recommendation to extend the scheme is based on a number of factors including:

- 16.1 There has been no substantive change in air cargo capacity to and from New Zealand since the MIAC was established by Cabinet in March 2021, and no material change since the IAFC scheme provide support for peak exports/imports in November 2020.
- 16.2 There is not expected to be any substantive recovery of New Zealand's international aviation sector and capacity until 2022 at earliest. The ability of an airline to operate commercially into and out of New Zealand is directly linked to the ability to carry passengers. We do not see any significant increase in passenger numbers occurring until 2022.
- 16.3 Even if there is an increase in passenger travel in from 2022, the *Reconnecting New Zealanders* approach would see different markets open up at different times to passenger travel. Some routes will therefore take longer than others to become commercially viable again.
- 16.4 The current demand for air cargo is tracking at or above 2020 and pre-COVID levels. We expect demand to increase further given disruptions to maritime supply chains and increased demand for fresh produce in some markets (North America in particular). The current capacity both under the MIAC and provided by the market is not enough to meet New Zealand's air connectivity needs from November 2021 to March 2022.
- 16.5 Without ongoing support from the MIAC, there will be significant regional, sectoral, market, and company impacts due to an inability to access air cargo capacity during the peak export and import season.

As international passenger travel begins to increase (potentially from the first quarter of 2022), the support required from the MIAC will decrease

- 17 Extending the MIAC scheme does not mean that support would automatically be provided to all flights, or for the entire period. ^{s 9(2)(b)(ii)}



Supporting the same level of capacity as was provided in 2020/21 should be enough to ensure freight users have access to key markets

- 18 The level of capacity required by the market in 2020/21 provides a solid baseline for post-COVID demand. While there have been some changes to the profile of New Zealand's exports since then (particularly increased demand from North America), the overall level of demand from November to March is not expected to be any lower than 2020/21. Providing capacity from the MIAC at the same level as provided by the IAFC in 2020/21 would provide a baseline of capacity while leaving room for other operators to enter the market.
- 19 I note that even after matching IAFC levels of 2020/21 capacity, there are likely to still be unmet cargo demand and some missed export opportunities. Over the course of 2021, more freight users would have moved their supply chains to air freight in light of the challenges faced trying to access reliable sea freight capacity and increased demand from North America for fresh produce.
- 20 However, the role of the MIAC has never been to support all demand. The MIAC and the IAFC were only intended to provide a baseline of capacity and ensure connectivity was maintained. ^{s 6(a)}



I recommend Cabinet agree to extend the MIAC to 31 March 2022 and allocate an additional \$125m to support the extension

- 21 I consider that providing sufficient funding to enable 2020/21 levels of freight to be carried is the most prudent option given the uncertainty of border reopening timeframes and the level of capacity that will actually be required. The capacity required will depend on a number of factors including demand from overseas markets and the level of domestic production possible (which is impacted by weather, COVID-19 restrictions, and the availability of seasonal workers). Matching 2020/21 levels of freight provides a baseline of capacity for freight users, commits the Government to providing no more capacity to the market than last year, and leaves room for other operators to enter the market to meet remaining unmet demand.
- 22 In 2020/21, the IAFC supported an average of 52 flights and 1,940 tonnes of freight capacity per week. From November 2020 to March 2021, the cost of this support averaged ^{s 9(2)(b)(ii)} per week. While the previous IAFC scheme required ^{s 9(2)(b)(iii)} I expect the MIAC to require \$195m² over the same period (^{s 9(2)(b)(ii)} per week). There are main two reasons for these increased costs:

22.1 **Increased costs of operating:** While airlines have been able to reduce operating costs compared to pre-COVID, they made these cost reductions in the immediate aftermath of COVID-19. By now, airlines have minimised their

² s 9(2)(i)



costs and are now facing the same inflationary pressures as the rest of the economy. The largest cost increases since 2020 relate to jet fuel, which has risen from a low of 16USD per barrel in April 2020 to 85USD per barrel in June 2021. In November 2020 the fuel price was 40USD – roughly half the current price.

22.2 **Additional carriers under the MIAC:** The MIAC has some additional airlines receiving support (Korean Air, Air Calin, and Air Tahiti Nui). The additional carriers and the connectivity to new markets they provide does have an impact on the overall cost of the scheme.

23 To provide a similar level of capacity to that provided under the IAFC last year would require a total of \$195m (\$125m in new funding). This funding would enable an average of 53 flights to 17 destinations and ^{s 9(2)(i)} [REDACTED] This factors in the ebb and flow of demand on certain routes based on the seasonality of demand – for example additional capacity in the lead-up to Lunar New Year and the Christmas/Easter meat demand from Europe.

24 ^{s 9(2)(b)(ii)} [REDACTED]
^{s 9(2)(g)(i)} [REDACTED]

25 Should demand be as strong as expected and there be any increase in passenger movements, the above cost will reduce (noting the passenger numbers are unlikely to increase prior to March 2022 at the earliest). Additionally, if any of the markets served by the MIAC experience a material reduction in international travel restrictions, they should be able to exit support entirely.

I do not believe that a return to market conditions is appropriate or even possible at this stage

26 I consider that the market has not returned to a functional position (restrictions on market entry and a lack of certainty on timeframes for reopening remain) and that this is largely due to the continued restrictions on passenger movements. As passenger restrictions are removed, the amount of support paid under MIAC will automatically reduce, and can in due course be switched off entirely. High passenger numbers on some Los Angeles flights have seen no support needing to be paid, and quarantine-free travel to Australia and the Cook Islands saw support switched off entirely.³

27 ^{s 9(2)(g)(i)} [REDACTED]

³ ^{s 9(2)(i)} [REDACTED]

- 28 A tapered approach (where support is reduced on a mechanical basis) or a general reduction in support compared to 2020/21 levels is likely to only lead to significant capacity shortfalls as the airlines cannot be compelled to operate flights at a loss and there are no indications that new airlines can/will close any capacity gaps. The natural removal of support as passenger movements increase can be more effectively managed through the MIAC's existing funding mechanisms than through an arbitrary shortening of the support period or tapering of the scheme based on uncertain reopening timeframes.

I also recommend that Cabinet set aside a \$25m contingency in the event support is required during a pause or suspension of QFT

- 29 I expect that the \$125m in new funding for the MIAC extension will be enough to cover the bulk of New Zealand's international connectivity needs. However, this amount does not include any support for trans-Tasman or Cook Islands flights. If support is required for trans-Tasman or Cook Islands flying over the support period, then additional funding would need to be found.
- 30 A separate 'QFT pause contingency' of \$25m would ensure that freight and managed return flights are able to take place in the event of a protracted QFT pause or a suspension, without jeopardising the delivery of any other flights under the MIAC. This is the same approach added to the current phase of the MIAC when the current trans-Tasman QFT suspension was announced. The \$30m which has been set aside for supporting trans-Tasman flights is treated as a separate funding pool and so does not impact the ability of the MIAC to continue its other services.
- 31 I recommend that Cabinet agree a separate funding pool within the MIAC from 1 November 2021 to 31 March 2022 to meet the additional requirements resulting from a protracted QFT pause or a suspension. I propose that this funding would be set aside and only used by the Secretary for Transport when he has assessed that:
- 31.1 There has been a sustained pause in QFT travel, or a suspension has been announced (noting that in the event of a short term pause, airlines are expected to make operational changes and manage without support from the MIAC);
 - 31.2 Airlines are no longer able to operate flights on a commercial basis; and
 - 31.3 There is a high likelihood of significant disruption to freight and/or passenger movements without support.
- 32 My expectation is that the Ministry will follow its practices to date and that:
- 32.1 The Ministry's starting position is no support would be provided in the event of a short-term pause;
 - 32.2 Airlines would be expected to consolidate passengers and make other operational changes before any support is provided; and
 - 32.3 Support would only provide a minimum level of freight and/or passenger connectivity, not replace all capacity lost during a QFT pause or suspension.

33 Given the considerable uncertainty around the need to support Australia and Cook Island flights over the coming months, I consider \$25m a reasonable level of contingency to set aside. This amount would be enough to support continued trans-Tasman connectivity and to support repatriations in the event of QFT pauses with the Cook Islands. ^{s 9(2)(i)}

Implementation

34 The Ministry of Transport is well placed to continue administering the MIAC scheme. If an extension of the scheme is agreed by Cabinet, the Secretary for Transport will enter into funding agreements with airlines as has been the process to date.

35 I recommend that the contracts with current airlines under the MIAC be extended to 31 March 2022 and adjusted to reflect the increased capacity required over the period. ^{s 9(2)(g)(i)}

36 The Ministry of Transport will continue to report on a monthly basis to myself, the Associate Minister of Finance and Treasury on weekly spend, number of flights supported, volume of freight carried, any material contract variations and the exit strategy indicators outlined previously agreed by Cabinet [CAB-21-MIN-0063 refers].

37 If Cabinet agrees to extend the MIAC to 31 March 2022, I intend to task officials to report back to joint Ministers in early 2022 with a framework for an off-ramp/transition from the scheme once circumstances allow.

Financial Implications

38 No new funding is required for the Ministry to administer the extension. Cabinet allocated enough funding to administer the MIAC to 31 March 2022 at the establishment of the scheme.

39 For the current phase of the MIAC, from May to October 2021, the Ministry expects to have little to no funding remaining which could be reallocated to support the extension. At most, the Ministry expects to have ~\$5m in funding remaining at 31 October.

40 To provide the same level of capacity as 2020/21 would require a total of \$195m (\$125m in new funding). This funding amount is based on the current contractual costs the Ministry has with carriers and takes into account lessons learned about seasonal demand in 2020/21. ^{s 9(2)(i)}

- 41 s 9(2)(i)
- 42 I recommend setting aside an additional \$25m as a contingency in case support is required to maintain connectivity during a QFT pause or suspension. s 9(2)(i)
- However, I expect that even if QFT does not fully return over the coming months, Australia will be one of the first markets to benefit from the *Reconnecting New Zealanders* framework and so a reduced amount of support would be required (potentially starting in March 2021).

Legislative Implications

- 43 There are no legislative implications.

Regulatory Impact Statement

- 44 No Regulatory Impact Statement is required as this proposal does not introduce or change any legislation.

Climate Implications of Policy Assessment

- 45 A Climate Implications of Policy Assessment (CIPA) has not been prepared for this paper. The proposal recommends providing financial support for fossil fuel intensive international air transport, which creates greenhouse gas emissions. Even with this support it should be recognised that the total number of flights per week operating to and from New Zealand would still be less than a quarter of the number of flights operating prior to COVID-19. This represents a sizable reduction in the emissions attributable to New Zealand's international air services.
- 46 It is also worth noting that air freight is being carried significantly more efficiently now than it was pre-COVID. Around 90% of pre-COVID export volumes are being carried on around 25% of the flights. Flights supported by government charge freight rates which are higher than pre-COVID rates, which will encourage those traders who are able to do so consider other, less emission-intensive models for transporting their products to market. Additionally, over the last 18 months, airlines have largely retired their older, less efficient aircraft meaning that emissions from flights to and from New Zealand should be, on average, lower than pre-COVID.

Population Implications

- 47 Changes to New Zealand's international air connectivity could affect Māori, and rural and coastal communities in particular. 80% of New Zealand's air freight exports (by volume) are primary sector products. A number of iwi have their largest investments in primary industries and tourism, so have been particularly exposed to the collapse in air services caused by COVID-19. The purpose driven business model of many Māori enterprises that includes financial performance and whanau wellbeing means that air service disruption could have wide ranging knock-on effects for the Māori community.
- 48 Rural and coastal communities, and some regions, could be affected because the local economies in those areas are concentrated on the production of goods and services for export by air e.g. fishing communities, or horticulture in the Auckland region, and international tourism in parts of Otago and the West Coast. Constraints

on the ability to export products in the immediate-term, or for recovery in the medium-term could reduce incomes and lead to job losses in those areas.

Human Rights

49 There are no implications for human rights.

Consultation

50 The following agencies were consulted on this paper: Treasury, Ministry of Foreign Affairs and Trade, Ministry for Primary Industries, Ministry for Business, Innovation and Employment, New Zealand Trade and Enterprise.

51 The Ministry for Primary Industries (MPI), Ministry for Business, Innovation and Employment, and New Zealand Trade and Enterprise agree with the recommendations of this paper.

52 The Treasury and MFAT support an extension of the MIAC to 31 March 2022. However, both agencies have indicated a preference to only provide support up to the \$100m originally agreed by Cabinet.

Treasury and Ministry of Foreign Affairs and Trade comment

53 s 6(a), s 9(2)(i), s 9(2)(g)(i) [Redacted]

54 [Redacted]

55 [Redacted]

56 [Redacted]

57 [Redacted]

[Redacted text block]

58

[Redacted text block]

59

[Redacted text block]

60

s 9(2)(b)(ii) [Redacted text block]

61

s 9(2)(b)(ii) [Redacted text block]

62

s 9(2)(g)(i) [Redacted text block]

⁴ The Ministry of Transport notes that this proportion remains unchanged from the previous IAFC scheme which suggests that there has in fact been no material change in the level of capacity available outside the MIAC over the last 12 months.

63 s 9(2)(h) [Redacted]

64 s 9(2)(h) [Redacted]

Ministry for Primary Industries comment

65 s 9(2)(g)(i) [Redacted]

Additional Treasury comment

66 The assessment of the factors leading to continued MIAC support is linked primarily with passenger movements, rather than border settings. The analysis suggests that even as border settings open (the exact timing of which remains uncertain), passenger numbers are unlikely to recover, even from March 2022.

67 s 9(2)(g)(i) [Redacted]

68 s 9(2)(g)(i) [Redacted]

69 s 9(2)(g)(i) [Redacted]

Communications

- 70 I will make a public announcement on the extension of the MIAC scheme following Cabinet's decision. I recommend that this announcement be made as soon as possible following Cabinet's decision.
- 71 The Ministry of Transport will communicate the details of implementation to the affected airlines, and work with other agencies including MFAT, MPI and NZTE to ensure that affected industry groups are aware that support for air services will continue to be available. I recommend that the Ministry of Transport be able to communicate these details to airlines immediately following Cabinet's decision (subject to any airline announcements being embargoed until a formal announcement is made). Airlines require a minimum of four weeks' notice to schedule flights and secure freight bookings, and it is also important that exporters are given confidence as soon as possible that their goods will be able to reach export markets. A significant delay in announcing the extension of the scheme would not allow airlines enough time operationalise their flights before 1 November.

Proactive Release

- 72 Not proposed due to the discussion of matters which are commercially sensitive, and sensitive to New Zealand's international relations.

Recommendations

I recommend that the Committee:

- 1 **note** that in March 2021, Cabinet agreed to establish the Maintaining International Air Connectivity (MIAC) scheme to replace the previous International Air freight Capacity (IAFC) scheme [CAB-21-MIN-0063].
- 2 **note** that on 15 March 2021 Cabinet (DEV-21-MIN-0028 and CAB-21-MIN-0063 refers):
- 2.1 agreed to establish the MIAC Scheme to operate until 31 October 2021 (phase one), with the potential for an extension to 31 March 2022 (phase two);
- 2.2 agreed to establish tagged operating contingency of up to the amounts as follows in Vote Transport, to provide for any extension of the MAIC Scheme from 1 November 2021 to 31 March 2022:

	\$m – increase(decrease)		
	2020/21	2021/22	2022/23 & outyears
Extending the Maintaining International Air Connectivity Scheme – Tagged Operating Contingency	-	100.000	-

2.3 authorised the Minister of Transport and Associate Minister of Finance (Hon David Parker) jointly to draw down the tagged operating contingency funding in recommendation 2.2 above;

2.4 agreed that the tagged operating contingency above be charged against the COVID-19 Response and Recovery Fund.

3 **note** that Cabinet previously agreed to reallocate \$30 million of the \$100 million tagged operating contingency to support trans-Tasman flights during a suspension of quarantine-free travel (QFT) with Australia [CAB-21-MIN-0288 refers].

4 **note** that the \$70 million in remaining tagged operating contingency is not enough to meet New Zealand’s connectivity needs in future and that additional funding would be required to extend the MIAC to 31 March.

5 s 9(2)(g)(i) [Redacted]
 This would also support a transition period for returning to market-based solutions.

- 6 (a) **agree** to extend the MIAC from 31 October 2021 to 31 March 2022 by drawing down the remaining \$70 million tagged operating contingency and to allocate an additional \$125 million to support this extension; and
- (b) **agree** to allocate an additional \$25 million under the MIAC to support continued connectivity in the event QFT with Australia and/or the Cook Islands is or continues to be paused or suspended.

s 9(2)(g)(i) [Redacted]

OR

- (c) **agree** to extend the MIAC from 31 October 2021 to 31 March 2022 by drawing down the remaining \$70 million tagged operating contingency and to allocate an additional \$30 million to restore the funding to the \$100 million amount agreed by Cabinet in April 2021

s 9(2)(g)(i) [Redacted]

7 **note that** ^{s 9(2)(h)} [Redacted]

8 ^{s 6(a)} [Redacted]

9 ^{s 6(a)} [Redacted]

10 **direct** the Ministry of Transport to continue to administer the scheme;

11 **agree** that the current suite of contracts with airlines under the MIAC (selected in May 2021) be adjusted for seasonal demand and extended by the Secretary for Transport to 31 March 2022 if suitable contractual terms can be reached;

12 **authorise** the Secretary for Transport to enter support arrangements with airlines to maintain connectivity in the event QFT is paused or suspended (in line with the framework set out in paragraphs 31 and 32);

13 **approve** the following changes to appropriations to provide for the decisions in recommendation 6, with a corresponding impact on the operating balance:

(a) if you agree with recommendation 6(a) and (b) above:

^{s 9(2)(g)(i)} [Redacted]

	\$m – increase/(decrease)				
Vote Transport Minister of Transport	2021/22	2022/23	2023/24	2024/25	2025/26 & outyears
Non-departmental Other Expenses: Maintaining international air services MYA	220.000	-	-	-	-

OR

(b) if you agree with recommendation 6(c) above:

^{s 9(2)(g)(i)} [Redacted]

	\$m – increase/(decrease)				
Vote Transport Minister of Transport	2021/22	2022/23	2023/24	2024/25	2025/26 & outyears
Non-departmental Other Expenses: Maintaining international air services MYA	100.000	-	-	-	-

14 **agree** that the proposed changes to appropriations above be included in the 2021/22 Supplementary Estimates and that, in the interim, the increase be met from Imprest Supply.

15 **agree** that \$70 million of the expenses incurred under recommendation 13 above be charged against the Extending the Maintaining International Air Connectivity Scheme – Tagged Operating Contingency, with:

(a) if you agree with recommendations 6(a) and (b), \$150 million charged as a pre-commitment against Budget 2022 allowances.

OR

(b) if you agree with recommendation 6(c) above, \$30 million charged as a pre-commitment against Budget 2022 allowances.

Authorised for lodgement

Hon Michael Wood

Minister for Transport

Released under the Official Information Act 1982

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Restricted and Commercial in confidence

Minister of Transport

Cabinet Economic Development Committee

COVID-19- Review of the Essential Transport Connectivity (ETC) Scheme

Proposal

- 1 This paper seeks agreement to extend the Essential Transport Connectivity Scheme to 30 September 2021, with a potential further extension subject to joint Ministerial approval depending on market conditions.

This proposal reflects government priorities for COVID-19 recovery

- 2 This proposal supports the Government's economic response to COVID-19 through its efforts to cushion the financial blow to whānau and families, workers, businesses and communities from the impacts of COVID-19, position New Zealand for recovery, and reset and rebuild our economy.

Executive Summary

- 3 The Essential Transport Connectivity Scheme (ETC) has achieved the objectives Cabinet originally set out in May 2020 to support the continuation of essential transport routes and services in the face of increased COVID-19 domestic and international travel restrictions.
- 4 The fundamental impacts of COVID-19 are still being felt by many transport services and operators. For the moment, international borders remain closed to most countries and international travellers are severely limited in number. While quarantine-free travel (QFT) has been implemented with Australia and more QFT zones are expected to emerge over the course of 2021, these zones will take time to deliver a significant increase in international tourists to domestic travel operators and it is unlikely that visitors from a limited number of international markets can fully replace all those international visitors unable to enter New Zealand. Compounding the loss of international tourists, domestic business travel which used to provide a significant source of revenue for many transport operators has not yet fully rebounded.
- 5 I recommend Cabinet agree to extend the ETC scheme to 30 September 2021 to help maintain essential transport services across New Zealand. Extending the ETC scheme builds on lessons learned from operating the ETC to date, recognises the essential nature of transport connections for many New Zealanders, and places New Zealand and its transport operators in a strong position for recovery. However, I also recommend that Cabinet also refine and tighten the eligibility criteria for the scheme to reflect the time that has past since the initial 'COVID shock'.
- 6 I expect the extension to cost an average of \$0.100m per week (a total of \$1.8m from June to September), a decrease on the current \$0.115m per week and \$0.150m per

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week at the peak of the ETC's support. The extension does not require any new funding as there is sufficient funding remaining within the existing ETC appropriation.

The ETC scheme was established to ensure essential transport connections and services were protected for those that need them

- 7 From March 2020, the COVID-19 lockdowns and Alert Levels resulted in local and domestic travel restrictions which significantly impacted the operation of some transport routes and services. These routes were either unable to be operated or operated at reduced capacity due to social distancing requirements. Additionally, New Zealand closed its borders to international travellers. These closures saw the removal of the international tourism market overnight and resulted in a marked decrease in domestic travel.
- 8 The dramatic decrease in passenger demand and revenue placed some transport operators and service providers under immense pressure, causing services to be cancelled, threatening the viability of some operators, and exposing potential gaps in regional connectivity. It also created a risk that the ability of New Zealand's transport services to recover post-COVID-19 would be significantly impacted.
- 9 The ETC scheme was established by Cabinet on 11 May 2020 to provide support to maintain these essential routes and services negatively impacted by COVID-19 [CAB-20-MIN-0219.28]. The scheme enables the government to respond quickly where the failure of a transport service would have significant negative social and economic outcomes and would impact New Zealand's post COVID resilience and recovery. The ETC scheme's funding comprised:
 - 9.1 \$20 million to enable support for non-aviation essential transport operators [CAB-20-MIN-0219.28]; and
 - 9.2 \$30 million to fund aviation initiatives under the scheme from the underspend of the \$600 million aviation relief package [OC200394]. This was subsequently reduced to \$10.7m in order to fund an extension of the International Airfreight Capacity scheme in September 2020.

Cabinet agreed a set of principles and criteria to guide the operation of the ETC

- 10 At the establishment of the ETC, Cabinet agreed to a framework for assessing where additional financial support for transport operators (aviation and non-aviation) might be appropriate beyond the Government's general economic support measures [DEV20-SUB-0071]. The focus was on maintaining "essential transport connectivity", rather than supporting individual businesses or tourism operations to survive. The assumptions underpinning the ETC Scheme were:
 - 10.1 Support is by exception, given the general measures available as part of the Government's COVID-19 economic response package;
 - 10.2 Transport operators may need to right-size in the short to medium term until normal volumes resume;
 - 10.3 Crown support should always be viewed as a last resort rather than a first port of call;

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- 10.4 The Government should not, in general, support a business to survive that was already facing financial issues prior to COVID-19; and
- 10.5 The Government will look to enter arrangements where it can exit as services begin to resume.
- 11 Cabinet considered it important that the Government was in a position to respond urgently to cases where there would be significant negative outcomes if a service was not available, either now, or to support the recovery phase. It was recognised that support may be required where a transport service will be essential to the recovery and is viable in the longer term, but requires support to ride out the economic impact of COVID-19 until “normal” operations resume [OC200342].

The ETC has now been operating for 10 months and New Zealand’s COVID-19 environment has changed significantly since its establishment

- 12 Since the ETC was established New Zealand has seen gradual easing of domestic travel restrictions¹ and a return to a reduced, but more ‘normal’, operating environment for many sectors and businesses. Most transport operators are now able to operate without social distancing measure in place (even at Alert Level 2) and there has been increased domestic travel which has gone some way to cushioning the impact of international restrictions on domestic operators.
- 13 Despite these improvements, the fundamental impacts of COVID-19 are still being felt by many transport services and operators. Domestic business travel which used to provide a significant source of revenue for many transport operators has not yet fully recovered. Compounding the loss of business travellers, New Zealand’s border remains closed to most countries and international travellers are severely limited in number.
- 14 While QFT with Australia is expected to improve revenue for some local transport operators and services. Australian visitors are only part of the international tourist market and their willingness to travel to New Zealand in winter in significant numbers is currently untested. Previously, Australians have travelled to New Zealand for ski holidays during winter. However, this is typically direct to destination (with little benefit to many of the operators receiving support from the ETC). There are also some key ETC routes that are not typical tourism routes for Australians on shortstays, and due to those local economies high reliance on international visitors will continue to remain precarious – notably the West Coast and Te Anau. (Cabinet has recently agreed psycho-social support and business advisory services for these communities and three others [DEV-21-Min-0067 refers]). Another potential constraint is the nature of the travel – initial indications are that many of the inbound passengers from Australia are visiting friends and relatives (VFR) and therefore less likely to be using New Zealand operators than genuine tourists.

¹ With the exception of short-term returns to Level 3 for the Auckland region in August 2020, February and March 2021.

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- 15 There is also a risk that a decrease in New Zealanders travelling domestically over winter (with Australia now an option for holidays) could decrease demand for some domestic services over the short to medium term.
- 16 Given the time that has elapsed and changes which have occurred since the establishment of the ETC the Ministry of Transport, alongside the Treasury, has undertaken a review of the ETC scheme (the Review). The Review assessed the performance of the ETC and provided recommendations for future support for essential transport services.

The ETC scheme has met the objectives set out at its establishment and allowed services and connections to be maintained in a challenging COVID-19 environment

- 17 Since May 2020, the ETC scheme has enabled more than 140,000 passengers to travel on over 10,000 services. It has maintained vital connections for New Zealanders with essential services, employment, families and whānau.
- 18 To date, the ETC has supported eight organisations for a total of \$8.600m enabling:
- 18.1 Business and essential travel (i.e. for work or medical appointments) from regional centres to main hubs to continue despite a lack of international tourists which previously cross-subsidised these services;
 - 18.2 Regional bus services and flights to continue servicing geographically isolated communities;
 - 18.3 Passenger travel and the movement of essential supplies to the Chatham Islands, including during Level 3 in Auckland when all flights would otherwise have stopped;
 - 18.4 The ongoing operation of essential transport support services (such as the Seafarer Welfare Board of New Zealand (SWBNZ)) to ensure that the supports underpinning a successful transport system could continue to operate; and
 - 18.5 Key transport operators and services to continue to operate through the initial impact of COVID-19 to provide them the best chance of adapting for the 'new normal' which many operators have begun to do.
- 19 The ETC scheme has spent an average of s 9(2)(b)(i) per week and had a cost of s 9(2)(b)(ii) per passenger, per trip. An average week sees approximately 3,000 passengers utilise ETC supported services which might otherwise not have operated. The scheme has therefore been a relatively inexpensive method of preserving transport connections and keeping vulnerable parts of New Zealand's domestic transport system open and operating.

COVID-19 continues to create challenges for maintaining essential transport services with the impact of COVID-19 continuing longer than originally anticipated

- 20 Many of the issues which impacted services in 2020, and led to the creation of the ETC scheme, are still in effect. These include:

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20.1 *Many essential transport services for New Zealanders were only viable as a result of high numbers of international tourists. Many regions cannot justify services based solely on domestic population and the current services (which were usually built with infrastructure to service high levels of demand) continue to be unviable without international tourists.*

20.2 *Domestic travel remains muted as a result of COVID-19 hesitancy and we are heading into the traditional low point for domestic travel. New Zealanders have not replaced the volume of international visitors on these services despite increases in domestic tourism over summer. Business travel remains muted and there is a risk that over winter domestic tourists instead choose to travel to Australia, further decreasing demand.*

20.3 s 9(2)(b)(ii)



21 Despite the significant length of time that has passed since the initial impact of COVID-19 restrictions, the Ministry continues to receive applications and interest from a small number of operators and service providers. These applicants are generally facing financial difficulties as a direct result of COVID-19 and while they may have been able to operate until now without support, the longer term impact of COVID-19 is now being felt. In most cases, these operators were able to survive for most of 2020 on cash reserves, shareholder injections, and other COVID-19 government support packages. However, some operators have now exhausted these sources of funding and there are no alternatives available.

I propose continuation of the ETC scheme to 30 September with enhanced eligibility criteria

22 The long term impacts of COVID-19 are still being felt by many transport operators and without support some essential routes and services may not be operated in the medium term. I consider that there is therefore a case to continue the ETC scheme, with appropriate refinements and adjustments, to ensure maximum value to the government and taxpayer is provided by the scheme.

23 I propose that support for essential transport routes and services is continued through the ETC to 30 September 2021. I propose that joint Ministers² have the ability to extend the scheme for a further three months until the end of December 2021 if closer to the time we determine it is necessary to continue support in some form. The Ministry of Transport will provide advice on a further extension which outlines any changes to the wider transport operating environment since Cabinet's decision, the extent to which operators are able to provide services without support, and the anticipated need for support from 1 October (if any).

² The Minister of Transport, Minister of Finance, Associate Minister of Finance responsible for aviation matters, and the Minister of Economic and Regional Development.

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24 I propose that if joint Ministers determine an extension is warranted that Ministers be able to adjust the eligibility criteria for the scheme to adapt to any changes in the transport environment between now and then.

Enhanced eligibility criteria for funding

25 To take into account lessons learned over the last 10 months, I propose that the eligibility criteria for the ETC be tightened and that all extensions and new applications to the ETC be assessed against the following criteria. An operator or service provide who meets these criteria would be considered 'essential' for the purposes of the ETC scheme.

Table 1: Proposed eligibility criteria for the ETC scheme

Requirement	Eligibility Criteria
The applicant must meet all of the following criteria	<ol style="list-style-type: none"> 1- There is no substitutable service³ now or in the short term. 2- If the service fails, there is low probability of a market resolution within a reasonable timeframe. 3- The challenges facing the service must be a direct result of and cannot predate COVID-19. 4- The relevant service must, on average, be unable to operate at a break-even level. 5- There must be evidence of a reasonable level of demand for the service⁴.
The applicant must meet at least one of the following three criteria	<ol style="list-style-type: none"> 1- Economic prosperity: The service supports economic activity, including maintaining the core transport network to support response and an efficient recovery. 2- Inclusive access: The service enables all people to access social and economic opportunities, such as work, education and healthcare. If the service did not exist, there would be significant negative outcomes, particularly for: <ol style="list-style-type: none"> a. vulnerable people, including people on lower incomes and those without access to private vehicles b. people living in geographically-isolated communities. 3- Resilience and security: The service is critical for emergency and resilience purposes.
The applicant must meet all of the following financial criteria	<ol style="list-style-type: none"> 1- Made effective use of the support measures available under the Government's COVID-19 Economic Response Package. 2- Taken all available and reasonable operational and commercial measures to ride-out the impact of COVID-19

³ For clarity, a 'service' could include a specific route/connection provided by a transport operator, or a support service which is an essential enabler of the transport system (for example weather forecasting services without which the aviation system cannot operate).

⁴ A 'reasonable level of demand' would be determined on a case by case basis given variability between routes, modes of transport, and the type of support service provided. An operator could fail this criteria where there is a significant gap between current patronage and break-even level for the service.

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	<p>3- Taken all available opportunities to obtain non-Crown funding to ride-out the impact of COVID-19</p> <p>4- Taken into account the capabilities and capacity needed to recover to the “new normal”.</p>
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At this stage I do not anticipate support will be required beyond 30 September 2021, however there is considerable uncertainty in the transport sector

- 26 With QFT in place with Australia and more QFT zones expected to emerge over the course of 2021, I expect that the need for the ETC scheme will reduce over the coming months. However, the exact impact of QFT zones on the viability of New Zealand’s essential transport routes and services is unknown and it is too early to speculate on when or how support can be exited.
- 27 The Ministry of Transport expects that by August 2021 the impact of QFT zones is likely to be clear and further developments on vaccine deployment and effectiveness known. This will allow joint Ministers to make a more informed decision on ending the ETC. At this stage, we expect a reduced need for the ETC beyond September 2021 as a result of border openings and operators heading into peak season for domestic travel. The combination of the October school holidays and Labour Day in the period immediately following the planned end of the ETC should cushion any blow from the removal of support for transport operators.

The Ministry recommends that Cabinet agreement is also sought to delegate some future funding decisions to the Secretary for Transport

- 28 If Cabinet agree to continue the ETC scheme until the end of 30 September then I recommend delegating some future funding decisions to the Secretary for Transport. For all other funding decisions, the current delegation of decisions to joint Ministers would continue to apply.
- 29 I propose that the Secretary for Transport be delegated authority to enter into agreements up to \$0.500m in value and that the agreements be able to cover the period from the recipient’s next extension to the proposed 30 September end date (or for a shorter period if the Secretary considers it appropriate). The following framework would sets out the limits of the proposed delegation.
- 29.1 approvals are delegated to 30 September 2021;
- 29.2 the applicant meets (or still meets) the tightened eligibility criteria;
- 29.3 the funding agreement cannot extend beyond 30 September 2021;
- 29.4 the approval or extension is within a funding envelope of up to \$0.500m per agreement; and
- 29.5 Treasury agrees that an application or extension should be put to the Secretary for consideration.
- 30 The Secretary would retain the ability to enter into a shorter term arrangement (i.e. to end before 30 September) if there was a high likelihood that support would not be required for the full period. As with all previous delegations to the Secretary,

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agreement from the Treasury would be required before any new funding decisions or extensions are made.

Implementation

- 31 I propose that following agreement from the Cabinet, the Ministry of Transport:
- 31.1 Reassess all operators, at the time their next extension, against the revised eligibility criteria;
 - 31.2 Continue operation of the scheme (in the above, revised form) until 30 September 2021. No extensions or new agreements would be entered into beyond 30 September 2021 without prior Ministerial agreement; and
 - 31.3 Prepare advice for joint Ministers on whether to end the scheme on 30 September or extend it beyond that date and provide this advice to joint Ministers in August 2021.

Financial Implications

- 32 No new funding is required to support this initiative. The ETC scheme is supported by a multi-year appropriation and has sufficient funding remaining (\$17.100m) to keep the ETC operating at the same, or a reduced level, for several months. Despite funding being available for a longer period, I do not currently propose extending the ETC scheme beyond 30 September 2021.

Risks and mitigations

- 33 There is a risk that the continuation of the ETC scheme creates a dependency on Crown support for essential transport services and that ending support for these services may become more difficult over time. This is challenging to avoid while these services operate at a loss. However, this risk is partially managed through the ETC's standard 'top-up' funding model. As soon as a service is able to achieve break-even, support stops being paid. This stops support being provided where it is not required to cover costs.
- 34 Following Cabinet's decision, recipients will be informed of the revised criteria and the intention to end the ETC scheme on 30 September 2021. Once joint Ministers have made their decision on a further extension to the ETC, this end date will either be confirmed with recipients or the new end date provided to them. Signalling the ETC's timeframes early will provide operators as much time as possible to prepare for an exit from government support and plan any schedule or service changes required. The 30 September end date was specifically chosen to align with the start of the peak domestic travel period. The cumulative impact of the October school holidays and seasonal increases in travel should make a transition away from government support as smooth as possible.

Legislative Implications

- 35 There are no legislative implications.

Regulatory Impact Statement

36 No Regulatory Impact Statement is required as this proposal does not introduce or change any legislation.

Climate Implications of Policy Assessment

37 A Climate Implications of Policy Assessment (CIPA) has not been prepared for this paper. The proposal recommends providing financial support for transport operators and services, which creates greenhouse gas emissions. Even with this support it should be recognised that the total number of domestic flights and road transport services provided per week would still be less than the number which operated prior to COVID-19.

38 More broadly I am looking at how to reduce emissions from the transport sector as part of the work in response to the Climate Change Commission’s 2021 report.

Population Implications

39 This proposal has the following anticipated population impacts.

Table 2. ETC extension population implications

Population group	How the proposal may affect this group
Remote/rural populations	Many regions cannot justify transport services based solely on domestic population and they continue to be unviable without international tourists. Many more remote communities and individuals do not have nearby access to essential services (such as health and welfare services) and may not be able to travel to the nearest essential service without a transport connection.
Elderly, vulnerable, and disabled people	Many of the services support by the ETC scheme to date disproportionately support the elderly, vulnerable, and disabled people. These groups often have limited access to private vehicles, struggle with standard transport options, or have complex needs which require regular transport to a main centre to access.

Human Rights

40 There are no implications for human rights.

Consultation

41 The following agencies were consulted on this paper: Treasury and the Ministry for Business, Innovation and Employment (MBIE).

Communications

42 I do not intend to make a public announcement of the extension of the ETC scheme as those transport operators and services that are expected to require support are already under the scheme or have been offer the opportunity to apply and have either been declined or chose not to submit an application. The Ministry of Transport will communicate directly with affected parties.

Proactive Release

- 43 Not proposed due to the extensive discussion of matters which are commercially sensitive.

Recommendations

I recommend that the Committee:

- 1 note that on 11 May 2020 Cabinet established the Essential Transport Connectivity (ETC) Scheme to provide support to maintain essential transport routes and services negatively impacted by COVID-19 [CAB-20-MIN-0219.28].
- 2 note that the ETC Scheme has achieved the objectives originally set out by Cabinet and has allowed essential transport routes and services to continue despite the disruptions and negative impacts caused by COVID-19.
- 3 note that many of the COVID-19 related issues which impacted transport services in 2020, and led to the creation of the ETC scheme, are still largely in effect and without continued support there is a risk of significant negative transport outcomes.
- 4 agree that the ETC Scheme be extended to 30 September 2021 to allow essential transport services to continue operating and to position New Zealand's transport sector for recovery and that funding recipients be informed of the new criteria and this end date for the scheme.
- 5 note that this extension does not require any new funding and can be funded through the existing ETC multi-year appropriation.
- 6 agree that all future ETC funding applications and extensions be assessed against the eligibility criteria as outlined in Table 1.
- 7 delegate authority to the Secretary for Transport to enter into funding agreements in accordance with the delegation framework set out in paragraph 29.
- 8 agree that joint Ministers⁵ be delegated authority extend the scheme for a further three months until the end of December 2021 if joint Ministers assess that there is an ongoing need for support.
- 9 note that if the ETC scheme is not continued the funding agreements will be allowed to expire at 30 September and no further support would be made available.
- 10 agree that if joint Ministers decide to extend the ETC scheme beyond 30 September 2021 that they be able to adjust the eligibility criteria for the ETC at this time without returning to Cabinet for approval.

Authorised for lodgement

⁵ The Minister of Transport, Minister of Finance, Associate Minister of Finance responsible for aviation matters, and the Minister of Economic and Regional Development.

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Hon Michael Wood

Minister for Transport

Released under the Official Information Act 1982

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Office of the Minister of Transport

Cabinet Economic Development Committee

Review of the International Air Freight Capacity scheme and future air connectivity

Proposal

- 1 This paper seeks Cabinet agreement to extend the International Air Freight capacity Scheme (to be renamed the Maintaining International Air Connectivity scheme) for another 6 months, with a potential further five month extension depending on market conditions.

This proposal reflects government priorities for COVID-19 recovery

- 2 This proposal supports the Government's economic response to COVID-19 through its' efforts to cushion the financial blow to whānau and families, workers, businesses and communities from the impacts of COVID-19, position New Zealand for recovery, and reset and rebuild our economy.

Executive Summary

- 3 The International Air Freight Capacity scheme (IAFC) has achieved the objectives Cabinet originally set out to achieve in relation to facilitating imports and exports, preserving access to key tourism markets, maintaining the competitiveness and sustainability of the aviation sector and maintaining international relations. The scheme is currently scheduled to end on 30 April 2021.
- 4 Ending support for international air services now would have a direct and negative impact on important capacity and connectivity. This means reduced capacity to trade for importers and exporters, with knock on impact for employment and investment in those sectors and the communities they support. Reduced trade would see a loss of position in markets and a slower economic recovery. It will also have significant impacts on Pacific nations, passenger accessibility, and the ability for our aviation and tourism sectors to recover, with the potential for key connections to be lost that may take some years to return.
- 5 Continued, limited support, with a clear exit strategy helps to secure the gains already made through the IAFC and to sustain the platform of international connectivity that we can build back from when market conditions start to improve. Funding allocated by Cabinet in 2020 to the Aviation Support package is now largely exhausted, so this paper seeks funding of up to \$170m until the end of October 2021, and a further \$100m, if needed, to the end of March 2022.

Background


- 6 Whilst COVID-19 remains prevalent overseas, New Zealand's elimination strategy has been very successful in managing the response to the pandemic in New Zealand. A key component of its success has been extremely tight border restrictions. These have included immigration restrictions and a quota system and then a booking system to manage the finite capacity in Managed Isolation and Quarantine (MIQ) facilities of a maximum 4,500 people every 14 days. Passenger numbers are just 2% of pre-COVID levels.

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- 7 For airlines operating passenger aircraft, this dramatic reduction in international passenger demand means that passenger and freight revenue generally do not exceed operating costs, so all airlines (NZ and foreign) are driven by an imperative to reduce losses and stop operating flights that lose money. As a result, the number of flights to New Zealand collapsed at the end of March 2020 and has remained a small proportion of pre-COVID levels ever since.
- 8 Before the IAFC was put in place, airlines started to retrench, medicines and COVID supplies struggled to make it to NZ, and exporters started to struggle getting goods to market and faced a significant economic shock. As 80% of New Zealand's air freight was carried in the belly hold of passenger services prior to COVID-19, the Government swiftly stepped in to provide support to those consumers and businesses reliant on airfreight for import or export with the introduction of the IAFC.
- 9 On 23 March 2020 Cabinet agreed (CAB-20-MIN-0131) to establish a scheme with a funding appropriation of \$330 million (subsequently increased to \$372 million through a fiscally neutral transfer from within the wider \$600 million aviation relief package).
- 10 The primary objectives for the IAFC were:
- 10.1 Ensuring imports which are important for health (medicines and medical devices), business operations (machinery) and other critical tasks are still brought to NZ;
 - 10.2 Ensuring our high value exports that travel by air still make it to their markets.
- 11 The secondary objectives for the IAFC were:
- 11.1 Maintaining links to tourism markets to enable fast recovery of New Zealand's biggest export
 - 11.2 That the aviation sector is still sustainable and competitive when borders open;
 - 11.3 To maintain international relations.

Key design features of the scheme were:

- 12 **Market Led:** open-market invitations were made to all airlines to submit proposals to operate flights to the key identified ports. Airlines sell the freight capacity (and passenger seats) through their existing and well established channels.
- 13 **Aims to minimise market distortion and support competition:** the scheme did not set freight rates. The Government did not want to artificially suppress rates as this would inhibit a market recovery. It has meant freight users paying higher prices than before COVID, which has encouraged those that could to consider alternatives. Deliberate choices were made not to support proposals that might undermine the commercial viability of other airlines.
- 14 **Was designed with a built in exit mechanism** as passengers return. The amount the scheme pays for each flight is equal to: flight operating cost minus freight and passenger revenue. ^{s 9(2)(f)}
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- 15 The Ministry of Transport has administered the scheme and has **continuously refined the support mechanisms** to target achievement of the IAFC objectives, and to maximise the public value of the scheme. These refinements have been material – three freighter operators have been exited from the scheme, two new carriers have been added, and changes have been made to contracts to significantly reduce the government’s liability.

Assessment of IAFC against objectives

- 16 The Ministry of Transport has led a cross-agency review process to measure the performance of the IAFC against its original objectives and assess New Zealand’s essential air connectivity needs and the role of government (if any). A copy of the Terms of Reference to the review is attached at Appendix 1 and the full report is attached as Appendix 2, and it found that the objectives have been delivered.
- 17 The current IAFC network supports 19 of the 24 destinations that have direct flights to New Zealand. As of 15 February, the airlines contracted under the IAFC had been paid **\$263 million**¹ and carried over 100,000 tonnes of freight on 5,543 flights to and from New Zealand. These imports and exports are estimated to have been worth **\$7.9 billion**. IAFC has helped enable imports to remain at 80% of their pre-COVID tonnage, while exports are around 90%, despite significant increases in freight rates. Given the percentage of flights provided by the IAFC (typically around half the total market) and the high utilisation levels of those flights (because of the funding model used), the IAFC has made a very significant contribution to the preservation of international trade. ^{s 6(a)}
- 18 Whilst international tourism is essentially closed, critical visitor pipelines to key tourism markets and passenger transit hubs have been kept open through support from the IAFC for flights to Dubai, Hong Kong, Shanghai, Tokyo, Los Angeles and San Francisco. In the absence of support, there was a risk that airlines could have closed down these routes. Support has allowed the airlines to retain critical staff and facilities that will provide a foundation on which to rebuild capacity, when circumstances allow. Those major passenger routes have also been the primary mechanism for New Zealanders to return from overseas. Of the 109,836 people who have passed through managed isolation and quarantine facilities, over 60,000 have been carried on flights supported under the IAFC.
- 19 With strict border closures in place, commercial flights to the Pacific Islands would have been impossible. The IAFC has supported a minimum level of connectivity to transport crucial supplies and facilitate a small number of essential passenger movements. Weekly flights to Fiji, Samoa, Tonga, Niue and the Cook Islands has sustained a base level of aviation infrastructure, which will be vital for the islands’ economic recovery.
- 20 The IAFC has supported the competitiveness and sustainability of the aviation sector because it has enabled more airlines to operate more services, and so employing more staff, than they would otherwise have been able to. It has diversified the network amongst a wider range of routes and carriers than would otherwise have operated and made New Zealand less vulnerable to a critical dependency on a

¹ Note this is the actual spend as at 15 February 2021, and the scheme continues until 30 April 2021. By this time, it is expected that the scheme will have largely exhausted the current funding allocation of \$372m. The IAFC was originally intended to last for six months from May 2020 at a cost of \$320m. However, through the reallocation of underspend from the Aviation Relief package of \$52m, this scheme has been able to be extended to 30 April 2021.

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particular route or air carrier. Some airlines which would have left New Zealand have been able to remain because they have operated routes supported by the IAFC.

- 21 The IAFC has allowed New Zealand to introduce the measures necessary to protect public health, without fear that it would lead to significant reduction in freight movement, because we have binding contracts with the airlines to continue flying and can absorb some of the cost. This has supported the aviation system to respond to changing health measures at the border, rapid changes in fuel price, and foreign quarantine restrictions on air crew, domestic and international lockdowns, and pauses to quarantine free travel.

Future international air connectivity

- 22 The funding appropriation for the IAFC is expected to be largely exhausted by the end of April, when the contracts with the current set of airlines are due to expire. This is an appropriate juncture to consider what the Government's role in supporting international connectivity might be beyond April.

The end of the IAFC will see a significant reduction in New Zealand's international air connectivity

- 23 In New Zealand the number of airlines operating regular passenger services has fallen from 30 pre-COVID 19 to 8 now, and they are operating at much reduced frequencies. Direct air connections have almost halved, from 44 destinations to 24. New Zealand's international air services amount to less than one fifth of the capacity prior to COVID-19. We have seen flight schedules **reduced from over 550 international flights per week, to between 130-140 flights per week**, half of which are supported by the IAFC.
- 24 Aviation is a dynamic industry, and the current environment for airlines is extremely volatile and financially challenging, so there is **considerable uncertainty** surrounding any assessment or forecast of the air services likely to be operating over the coming months. Adding to the uncertainty is ongoing COVID disruption of global aviation and sea freight networks, new COVID lock-downs and border control measures and changing trade patterns as countries emerge from the COVID crisis.
- 25 Based on substantial engagement and analysis of what we know of airline plans, financial state, and retrenchment actions, the Ministry of Transport has prepared a base case for an 'assumed residual network' without support from the IAFC. Despite the uncertainty described above, there is consensus between agencies that the withdrawal of the IAFC would lead to fewer flights, and reduced capacity for air freight. The Ministry of Transport expects that services would fall further to in the range of **85 - 95 flights per week, a reduction of 45 – 55 flights per week**.
- 26 While current freighters operating to New Zealand will continue current services, operators have indicated that they will not fill the capacity gap. This is because freighters are in high global demand and it is more profitable for them to operate in the northern hemisphere where they can transport large volumes at high utilisations on shorter routes. Freighters also do not support some exporters and importers which rely on more frequent, smaller services to move time-critical goods, or the passenger and tourism network needed for recovery.
- 27 There has been a small number of airlines operating outside the scheme – ⁵
_{6(a)}

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[REDACTED]

However, we cannot discount that over 2021, as other countries open their borders and stimulate their aviation industries, foreign airlines might find more profitable routes to deploy their aircraft on and could further reduce services to New Zealand.

28 In any case these airlines **do not operate directly to, or have airport slots for, all of the key markets and hubs that other IAFC airlines fly to**, so they cannot cater to some of our critical ports for exporters and importers, passenger movement and tourism recovery when the border can reopen.

29 The removal of IAFC would likely cause some international airlines operating under the scheme ^{s 9(2)(b)(ii)} [REDACTED]

[REDACTED]

Others would be expected to reduce services (given current services are not commercially viable). Some airlines may also look to run fewer services given the high costs (including COVID related health measures for aircrew) of carrying only cargo on passenger aircraft. United have recently informed the Ministry that they are reassessing their New Zealand services

30 The severity of impact of removal of the IAFC would **fall unevenly** across different markets, with the Pacific and North America being the worst affected and Australia being the least affected. ^{s 9(2)(b)(ii)} [REDACTED]

[REDACTED]

There could be significant disruption to trade if the IAFC was to be removed

31 An international aviation network with reduced capacity available for exporters and importers will lead to a situation where demand exceeds supply, with freight rates rising even further as a result.

32 ^{s 6(a)} [REDACTED]

33 There are approximately 6.25 jobs dependent – directly and indirectly – per \$1 million of exports, so any reduction in exports can lead to reduced employment in New Zealand. If exporters lose their regular customers, and their position in overseas markets, it can take years to recover that position even if the air freight capacity were to become available again in the near future. The current pause on export revenue from international tourism and education would heighten the impact of any reduction in export in goods at this time.

34 ^{s 9(2)(b)(ii)} [REDACTED]

[Redacted]

35 s 9(2)(b)(ii) [Redacted]

36 s 9(2)(b)(ii) [Redacted]

37 s 9(2)(b)(ii) [Redacted]

38 However, not all flights can be treated equally, trade data shows a clear preference for direct over indirect air services, only 16% of non-primary air freight (by tonnage) is transhipped. A direct flight is the only viable option for some live and perishable products. Speed to market was the primary reason for choosing air freight identified by respondents to NZTE's customer survey.

39 Another key question in assessing the non-IAFC capacity shortfall is whether certain products that are currently airfreighted could shift to sea freight. All agencies agree that some level of substitution is likely to occur as increased airfreight rates and lower capacity persist; indeed, there has already been evidence of this in the market to date (see MPI analysis). s 9(2)(b)(ii)

[Redacted]

Further industry engagement would be needed to accurately assess the level of possible substitution.

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- 40 Pivoting product format by freezing or otherwise processing a product can enable shipment by sea, but risks fundamentally changing the nature and/or value proposition of a product or sector, including for employment. Even where possible, there are practical limits to the speed with which business can pivot.
- 41 Some Māori businesses and iwi portfolios have already been hit hard, particularly through the downturn in tourism and the drop in lobster exports early in the pandemic. Further disruption to air freight could seriously impact the Māori economy. Premium products make up a significant part of Māori SME exports, including 13% in manufacturing, 12% in agriculture, forestry and fishing, 9% in health care and social assistance. ^{s 9(2)(g)(i)}
- 42 The impact of COVID-19 on iwi investment performance has reflected exposure to premium exports, but also reflects Māori investment in the tourism sector, the returns from which were severely impacted in the 2020 financial year.
- 43 Airlines operating under the IAFC have been flying at consistently high load factors. Our support is conditional upon it. Inbound flights have been particularly well-utilised, and the freight rates have increased much more than the outbound freight rates, over 200% on some routes. There is already anxiety amongst importers, particularly manufacturers and the medical sector, about the capacity and reliability of import channels, particularly in the context of ongoing disruption to sea freight. They are concerned without the IAFC, these issues could be exacerbated, and the network would be more fragile, congested, and expensive. Manufacturers import all year round, and they have signalled they need more, rather than less capacity, and have real concerns they will not get timely delivery of critical goods or machinery.
- 44 PHARMAC is very concerned that if air freight capacity was reduced, and key international routes were under-serviced, contracted pharmaceutical suppliers may not be able to ensure continuous supply of all essential medicines to New Zealanders. In addition, the Ministry of Health expects that the reduction or cessation of flight networks would significantly constrain their ability to be flexible and adaptive in a damaged supply chain model.

Leaving support in place provides a platform for the return of international tourists, and connectivity for important passenger movements now

- 45 Tourism New Zealand recommend continued support for international air connectivity to help position New Zealand for a recovery in the international tourism sector – which **previously accounted for 20.1% of New Zealand’s total export revenue.**
- 46 The current network, with support from IAFC, barely maintains the minimum network TNZ and MBIE Tourism assess is necessary to support New Zealand for tourism recovery. ^{s 9(2)(i)}
- This is because of the fraught current financial state of many international airlines and the fact New Zealand competes with other, higher value, higher volume, more accessible destinations for international airlines - so we are a marginal part of their network.

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- 47 For the Government's vision for the post-COVID recovery to be realised – and for future visitor portfolio resilience and diversity – TNZ's advice is that viable connectivity to five aviation markets will be key (Australia, China, USA, Singapore, Gulf); further, having at least two carriers operating on these routes would ensure a competitive product for consumers. For Australia, three carriers is the desirable model for competitive pricing and a healthy market. Direct flights are important on all of these routes – tourists show a strong preference for direct over indirect flights.
- 48 TNZ expects that without support for international air services, airlines would reassess their overall confidence to remain in the New Zealand market over 2021-22. When airlines and/or air services are withdrawn, it often takes years to attract them back to New Zealand. ^{s 9(2)(i)} [REDACTED]
- [REDACTED] There have always been **high commercial risks** involved in establishing ultra long-haul routes to New Zealand, and these are now likely to be exacerbated. Routes to New Zealand have traditionally been launched by airlines in strong commercial positions looking to utilise excess fleet capacity.

Without government support the Pacific would lose critical air connectivity

- 49 The IAFC has been the most efficient mechanism to support lifeline connections to the Pacific Island countries. The rationale for supporting a weekly flight to these destinations is different to the services to our principal trading destinations. Air freight volumes are much lower, but products essential to life are being shipped on every flight. The IAFC flights represent the **only way** for some goods and people to travel to and from four Pacific Island countries². Some nations have already made representations that the capacity currently offered is insufficient. ^{s 9(2)(ba)(i)} [REDACTED]
- [REDACTED]
- 50 A number of studies of the aviation and tourism sector in the Pacific have identified paths to recovery, and one of these is the continuance of regular flights in and out of key airports to keep key infrastructure and regulatory processes running and maintained. A complete cessation can lead to regulatory approvals lapsing and delay the restart of flights and therefore economic activity. The termination of flights from the Pacific would also remove potential opportunities for businesses on the islands to export time-sensitive goods to New Zealand, posing a further barrier to economic recovery.

Government support has helped to maintain capability in the aviation sector to better position us for recovery

- 51 Border opening is expected to provide a significant economic stimulus, but the extent of that stimulus will depend to an extent on whether New Zealand is positioned to take advantage of the opportunities presented by greater international travel. The IAFC, by enabling more flights than would otherwise have operated has secured more employment, and more capability within the aviation sector than would have been needed to support fewer flights.
- 52 Continued, limited support for international air services **preserves the platform** for recovery. If we lose the current airlines, it will take several years and significant investment to incentivise airlines to return. This was the case after both September

² Tonga, Samoa, Cook Islands and Niue.

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11 and the Global Financial Crisis (GFC), when New Zealand took 4 - 5 years to recover its international network. The aviation sector has already lost capability. Aircraft have been put into storage. Thousands of staff have been made redundant. **Further structural decline will slow recovery.** The more of the industry that we can keep operational, even if at a low level, then the easier it will be to scale up operations when border settings permit more passenger travel.

- 53 We will be in competition with other countries for the return of airline services. Ten airlines that used to operate to New Zealand have withdrawn, and several are currently considering whether to permanently retrench. Carriers have been requesting information about the likely pathway to border reopening over 2021 and the future of the IAFC.
- 54 It is critical New Zealand retains a base level of connectivity not only for tourism and trade connections but also so that we have a sustainable aviation sector which supports competition, reduces freight and passenger costs and enables good social connection for people to come home and to travel overseas.
- 55 Withdrawal of support now would also threaten the future component of the return on the \$263m investment already made. Extending support would enable New Zealand to continue to adapt and respond to changes in the domestic and international operating environment over 2021.
- 56 I note that beyond the on-going freight scheme it is also critical that the Government has a clear plan for border re-opening over 2021. As stated above 10 airlines have already permanently retrenched, and a number of other airlines are currently making decisions about the 2021/22 summer season, and their future in New Zealand. Another airline made decisions to permanently leave the New Zealand market this week, cancelling leases and finishing staff contracts. While an extension of the IAFC scheme may encourage some airlines to stay, many airlines will face significant financial pressures mid 2021.

International comparisons

- 57 New Zealand is not alone in providing support to ensure international air connectivity. Australia committed more than AU\$1.3 billion to maintaining operations across the aviation sector and supporting jobs, which includes export grants. The Australian scheme is currently scheduled to end in June / July 2021, although could be extended.
- 58 Singapore's Aviation Sector Assistance Package aimed to defray business costs and protect jobs by offering a rebate on landing and parking charges. The package also provided funding support to Singapore Airlines to maintain a minimum level of air connectivity, to keep supply chains open, and preserve Changi airport as a global hub.
- 59 On a much larger scale, the United States through the CARES Act made US\$25 billion available in payroll support for passenger airlines, with an additional US\$4 billion for cargo air carriers. This was further supplemented by up to US\$25 billion for loans and loan guarantees to passenger carriers, and US\$4 billion for loans and loan guarantees.

International obligations

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60 s 6(a) [Redacted]

61 s 9(2)(h) [Redacted]

62 s 6(a) [Redacted]

63 s 6(a) [Redacted]

63.1 [Redacted]

63.2 [Redacted]

63.3 New Zealand is one of, if not the, longest haul routes in the world and is reliant on aviation connectivity for trade. It is therefore not surprising during COVID 19 that given our special context that I have focussed the scheme on connectivity.

63.4 s 9(2)(h) [Redacted]

64 Support for international aviation cannot continue indefinitely so we need to provide a clear and visible end date (including to other countries). This underlies my recommendation that any scheme should end once market conditions improve as set out in the Exit Strategy section below. I expect this to occur in early 2022, but given the considerable uncertainty, the Ministry will monitor this situation closely.

The path to recovery is uncertain

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- 65 During 2021 there may be incremental border openings in relation to two-way quarantine free travel (e.g. Australia). This would make air services between Australia and New Zealand profitable, and so would not require scheme support. Support may still be needed for some “red flights” to Australia to enable transit passengers to travel (these are not likely to be commercially viable flights) and to address crew separation measures. Depending on the incidents of COVID resurgence in both countries quarantine free travel may need to open and close regularly. This makes the return of commercial services unpredictable.
- 66 Flights to the rest of the world are still unlikely to be viable with the low passenger numbers permitted, and support may be needed until the exit strategy criteria are achieved. The post-COVID aviation environment will have structurally less capacity than pre-COVID levels but just where that new norm will settle, or when, is not yet known.
- 67 Passenger travel in and out of New Zealand is only likely to really begin to increase when a sufficient proportion of the New Zealand population is vaccinated. If things go well with the vaccine roll-out and the broader health context, this is currently anticipated to be late 2021. It is unclear how the public’s appetite for travel has been affected. On the one hand, there could be pent-up demand (as the retail sector experienced after lockdown) particularly for visiting friends and relatives. On the other hand, anxiety about COVID-19 or confusion around potential on-going border entry requirements could discourage some potential travellers. MFAT notes that if during 2021, a March 2022 end date appears optimistic, then other low risk responses may need to be considered beyond March 2022.
- 68 It cannot be taken for granted that a relaxation of border settings will automatically lead to foreign airlines resuming services, or to Air New Zealand returning to close to its pre-COVID schedule and network. However, with the extension of support we can keep more services and connections operating which will better position New Zealand for a faster recovery.

I propose continuation of a similar support scheme, with a clear exit strategy

- 69 I propose that support for international air services on a similar market-driven basis be continued in operation for a further six months until the end of October 2021 (at a maximum cost of \$170m). I propose that I have the ability to extend the scheme for a further 5 month extension until the end of March 2022 for the summer export season if closer to the time we determine it is necessary applying the objectives below, at a maximum cost of additional \$100m, following consultation with the Associate Minister of Finance responsible for aviation matters, the Minister for Agriculture, the Minister for Trade and Export Growth, and the Minister of Tourism.
- 70 I recommend renaming the IAFC the Maintaining International Air Connectivity (MIAC) scheme– reflecting the analysis above that the value of aviation connectivity are wider than simply supporting air freight. Those objectives should be (in the following order of priority):
- 70.1 retain air connectivity with New Zealand’s principal trading partners to ensure that we can access the imports we need, that our exports can access overseas markets
 - 70.2 enable continued essential passenger movements
 - 70.3 retain important air connections to the Pacific

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- 70.4 retain air connections to key routes and hubs important for tourism recovery
- 70.5 maintain core capability, capacity and competitiveness within the New Zealand aviation sector to provide a platform for an efficient and competitive market when international air travel recovers.

I propose to support the minimum number of services to ensure there is a base level of connectivity to achieve the objectives above.

Exit strategy

71 The support scheme needs to be transitional, because we do not want exporters and importers to become dependent on continued support for air services or expect it to continue indefinitely. The support scheme should provide a bridge through 2021 to ensure we do not face the short and medium impacts on social and economic recovery described in this paper. We will need to communicate the end date for the scheme to the sector.

72 A clear exit strategy is important. s 9(2)(b)(ii) [redacted] note that should passengers return on some routes earlier, the government's liability would be reduced or eliminated. Other indicators, some set out below, will help to determine whether further support is required.

73 Because of the uncertainty around the return of passengers, I recommend a check-in point to determine what support is needed beyond the end of October 2021 for the summer peak export season. Factors to be taken into account when determining whether support is still required for a service will include:

73.1 s 9(2)(b)(ii) [redacted]

73.2 [redacted]

73.3 [redacted]

73.4 [redacted]

73.5 [redacted]

74 Under the current form of agreement supported carriers are required to report to the Ministry on at least a monthly basis on all key physical and financial variables, on a flight-by-flight basis, so the Ministry will be able to make these assessments.

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s 9(2)(i)

Implementation

- 76 The Maintaining International Air Connectivity scheme will be managed in accordance with Office of Auditor General requirements for such schemes. As a conditional grant, the scheme qualifies as an opt-out procurement, but as has been the case for the IAFC, and as a matter of good practice, the Ministry will apply the procurement rules so far as is practicable.
- 77 As an interim step, in order to allow time to undertake an open-market procurement process, I propose that the funding agreements with the airlines currently operating under the IAFC be extended until 31 May 2021. A new procurement will then select the air carriers to be supported under the MIAC until 31 October 2021. Any further support from 1 November to 31 March 2022 would be determined in accordance with paragraph 73 above.
- 78 Having administered the IAFC for 12 months, and successfully delivered two procurement processes, the Ministry of Transport is well prepared to run a similar process again. A number of officials from other agencies have been consistently involved in all aspects of the IAFC and will support the evaluation stage of the MIAC procurement to identify a preferred group of proposals to support.
- 79 The Minister of Transport and Associate Minister of Finance (acting jointly) would initially approve the key terms of the model contract and then decide which proposals to fund, having considered advice from the Ministry of Transport. The Secretary for Transport would be authorised to enter into funding agreements with the selected providers in line with the approved key terms, subject to conclusion of final negotiations.
- 80 The Ministry of Transport will report on a monthly basis to myself, the Associate Minister of Finance and Treasury on weekly spend, number of flights supported, volume of freight carried, any contract variations and the exit strategy indicators outlined in paragraph 73 above.
- 81 The following timetable is proposed, which based on previous experience, is challenging but achievable:

Milestone/Activity	Timeframe
Announce initiative, and extend current IAFC contracts to 31 May	Week ending 19 March 2021
Release Request for Proposals	1 April 2021
Deadline for proposals	29 April 2021
Proposals evaluated and moderated	6 May 2021
Decision from Ministers on preferred portfolio	14 May 2021
Contract negotiation	14-31 May 2021
New MIAC contracts start	1 June 2021

Financial Implications

- 82 For the first phase of the MIAC from May to October 2021, the Ministry expects to support roughly 40 flights per week, at an estimated cost of between s 9(2)(b)(ii). This is equal to the typical weekly cost for the equivalent period

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in 2020. s 9(2)(b)(ii)

- 83 The funding model used for the IAFC, and proposed to be continued, provides support payments calculated on a flight-by-flight basis, equal to the difference between the cost of operating the flight and the freight and passenger revenue earned. This provides assurance that the flight would not have been commercially viable without support, ensures that the minimum necessary funding is provided, and provides a built in exit mechanism.
- 84 This means there is considerable variability in the amounts actually paid – high levels of freight and passenger revenue will reduce (or even eliminate) payments, but payments are higher where the Ministry agrees to support increased costs (such as fuel or crewing costs) or where revenues are lower than anticipated. Careful financial management is needed to ensure that this variable payment calculation does not result in the government having an unexpected or open-ended financial exposure, and this is done by:
- 84.1 including a maximum payment for each flight (typically reflecting an expectation of freight loads of between 75% and 90% at a specified freight rate)
 - 84.2 including a “lifetime maximum” in each contract with each airline
 - 84.3 ensuring that lifetime maximums of all of the contracts entered into for a contract period do not exceed the total amount of funding available (so that, regardless of performance or cost adjustments, I will not need to return to Cabinet for urgent additional funding to meet the government’s obligations inside a contract period).

85

s 9(2)(i)

- 86 Should it be decided that a second phase of the MIAC is necessary over the summer peak period from November 2021 to March 2022, s 9(2)(i) As a contingency, I recommend a budget of \$100 million for the second phase of MIAC. This lower level of contingency reflects that it is likely that there will be some unspent funding carried over from the previous period.
- 87 As part of the original \$12b COVID-19 relief package announced in March 2020, Cabinet set aside \$600m an initial aviation support package. IAFC received \$372m from that package, with a range of other international and domestic interventions also being supported:

Category	Allocation \$m	Amount remaining \$m	Comment
IAFC	\$372.0	~\$10.0	Estimate only, considerable uncertainty at this time. Scheme continues until end-April and remaining amount will be unknown until late June, at which stage likely to seek approval to transfer any remainder to MIAC

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			after 30 June 2021.
Relief of passenger-based levies and Airways fees	\$136.8	\$25.6	Proposed to be held in reserve pending Cabinet decisions to be sought on the future of the ETC scheme; otherwise can be transferred to MIAC after 30 June 2021.
Airways NZ capital injection	\$70.0	-	
ETC aviation	\$10.7	\$6.9	Proposed to be held in reserve pending Cabinet decisions to be sought on the future of the ETC scheme; otherwise can be transferred to MIAC after 30 June 2021
Urgent airfreight scheme (Mar / Apr 20)	\$6.4	-	
Milford Aerodrome	\$2.3	-	
Singapore – New Zealand Airfreight Programme	\$1.5	\$0.8	Returned to Aviation Relief Package
	\$600		

88 Because of the small amounts remaining from the original \$600m Aviation Relief Package and uncertainty around their availability and timing, I propose to seek new funding for the \$170m at this time. If the new scheme is to be extended beyond 30 October 2021, any other funding then available can be considered when the decision to draw down the contingency for that period is made. If the decision is made not to extend beyond 30 October 2021, then any un-needed funding can be returned.

89 The Ministry of Transport will require additional funding to administer the MIAC. The estimated cost of administrating the MIAC to 31 March 2022 is \$1.270 million. However, the anticipated \$0.270m of MIAC administration costs for FY20/21 can be met from underspends within current administration funding for the IAFC, and no new funding for FY20/21 is required. At the end of FY20/21 we expect to have approximately \$0.300m remaining which can be transferred to FY21/22 (subject to the approval of the recommendation in this paper requesting transfer of \$0.200 million to FY21/22, and the approval of an in principle expense transfer of approximately \$0.100m). As a result of these transfers, only \$0.700 million in new funding will needed for 2021/22.

Legislative Implications

90 There are no legislative implications.

Impact Analysis

Regulatory Impact Statement

91 No Regulatory Impact Statement is required as this proposal does not introduce or change any legislation.

Climate Implications of Policy Assessment

92 A Climate Implications of Policy Assessment (CIPA) has not been prepared for this paper. The proposal recommends providing financial support for fossil fuel intensive international air transport, which creates greenhouse gas emissions. Even with this support it should be recognised that the total number of flights per week operating to and from New Zealand would still be less than a quarter of the number of flights operating prior to COVID-19. This represents a sizable reduction in the emissions attributable to New Zealand's international air services.

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- 93 It is also worth noting that air freight is being carried significantly more efficiently now than it was pre-COVID. Around 90% of pre-COVID export volumes are being carried on around 25% of the flights. Flights supported by government charge freight rates which are higher than pre-COVID rates, which will encourage those traders who are able to do so consider other, less emission-intensive models for transporting their products to market.
- 94 More broadly I am looking at how to reduce emissions from aviation as part of the work in response to the Climate Change Commission's 2021 report and also through international emissions reduction work with the International Civil Aviation Organisation.

Population Implications

- 95 Changes to New Zealand's international air connectivity could affect Māori and rural and coastal communities in particular. 80% of New Zealand's air freight exports (by volume) are primary sector products. A number of iwi have their largest investments in primary industries and tourism, so have been particularly exposed to the collapse in air services caused by COVID-19. The purpose driven business model of many Māori enterprises that includes financial performance and whānau wellbeing means that air service disruption could have wide ranging knock-on effects for the Māori community.
- 96 Rural and coastal communities, and some regions, could be affected because the local economies in those areas are concentrated on the production of goods and services for export by air e.g. fishing communities, or horticulture in the Auckland region, and international tourism in parts of Otago and the West Coast. Constraints on the ability to export products in the immediate-term, or for recovery in the medium-term could reduce incomes and lead to job losses in those areas.

Human Rights

- 97 There are no implications for human rights.

Consultation

- 98 The following agencies were consulted on this paper: Treasury, Ministry of Foreign Affairs and Trade, Ministry for Primary Industries, Ministry for Business, Innovation and Employment, New Zealand Trade and Enterprise, Tourism New Zealand, Ministry of Health, Pharmac, Ministry of Education and Te Puni Kokiri. They all support the recommendations in this paper.
- 99 Two of the key industry bodies made their views known to me. The New Zealand Airline Pilots Association strongly supports the continuation of the IAFC. It notes the key role of the IAFC in supporting productivity growth, aviation infrastructure, education and skill supply, and intergenerational wellbeing. It sees these last two as being supported by the retention of opportunities for highly skilled New Zealanders currently employed, and to be employed in the future, in the aviation sector. NZALPA shares the views set out earlier in this paper about the importance of the aviation sector for the recovery of international tourism.
- 100 The Board of Airline Representatives of New Zealand represents foreign airlines which fly here (or did fly here). It notes the success of the IAFC to date, and the importance of the government continuing to send a signal to foreign airlines that their presence here is welcomed and valued. It notes the risk that up to one-third of

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current scheduled flights are at risk, and further airlines likely to withdraw, without continued government support.

Communications



101 I will make a public announcement on the establishment of the Maintaining International Air Connectivity scheme following Cabinet's decision. The Ministry of Transport will communicate the details of implementation to the affected airlines, and work with other agencies including MFAT, MPI and NZTE to ensure that affected industry groups are aware that support for air services will continue to be available. Public communications will be managed with MFAT so as to mitigate as far as possible trade law and trade policy risks.

Proactive Release

102 Not proposed due to the extensive discussion of matters which are commercially sensitive, and sensitive to New Zealand's international relations.

Recommendations

I recommend that the Committee:

- 1 note that in March 2020, Cabinet agreed to establish the IAFC in response to the significant decline in air services as a result of COVID-19 [CAB-20-MIN-0131];
- 2 note that the IAFC has successfully achieved its primary objectives to ensure the supply of critical imports and maintain the economic benefits of high value exports.
- 3 note that the IAFC has successfully achieved its secondary objectives to maintain future tourism capacity, international relations, and the competitiveness and sustainability of the aviation sector.
- 4 note that in the absence of continued support, there will be: significant impacts on the ability to export and import goods resulting in potential further job losses, a loss of position in trade markets, and a likely slowing of economic recovery. In addition, there will be a loss of connectivity to the Pacific and key tourism routes and hubs critical for tourism recovery, and a slowing of the aviation sector ability to support recovery.
- 5 s 6(a) 
- 6 s 6(a) 
- 7 note that I have weighed these factors against the other considerations and assess the economic and social risks of not continuing the scheme are high.
- 8 agree to establish the Maintaining International Air Connectivity scheme (the Scheme) to operate until the 31 October 2021 (phase one), with the potential for an extension to 31 March 2022 (phase two) with key objectives (in the following order of priority) to:

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- 8.1 retain air connectivity with New Zealand's principal trading partners to ensure that we can access the imports we need, that our exports can access overseas markets
 - 8.2 enable continued essential passenger movements
 - 8.3 retain important air connections to the Pacific
 - 8.4 retain air connections to key routes and hubs important for tourism recovery
 - 8.5 maintain core capability, capacity and competitiveness within the New Zealand aviation sector to provide a platform for an efficient and competitive market when international air travel recovers.
- 9 agree to delegate a decision on whether to extend the Maintaining International Air Connectivity scheme from 1 November 2021 to 31 March 2022 to the Minister of Transport and the Associate Minister of Finance, following consultation with the Minister for Agriculture, the Minister for Trade and Export Growth, and the Minister of Tourism, if joint Minister consider an extension is necessary considering the objectives set out in recommendation 8 and the following:
- 9.1 Whether ongoing support is necessary to achieve the MIAC objectives set out above (in particular the necessary level of capacity).
 - 9.2 The extent to which a supported airline has not been making financial claims under the MIAC.
 - 9.3 The level of capacity provided by unsupported carriers.
 - 9.4 The level of freight utilisation achieved by supported carriers.
 - 9.5 Freight rates charged by supported carriers.
- 10 direct the Ministry of Transport to administer the Scheme.
- 11 note that the Ministry of Transport will report on a monthly basis to the Minister of Transport, the Associate Minister of Finance and the Treasury on weekly spend, number of flights supported, volume of freight carried, variations to contracts and the exit strategy indicators outlined in 9.1 to 9.5 above.
- 12 note that the Ministry of Foreign Affairs and Trade will work with the Ministry of Transport, Ministry for Primary Industries, New Zealand Trade and Enterprise and The Treasury on public communication around establishment and operation of the new scheme to mitigate as far as possible the trade law and trade policy risks.
- 13 agree that, within the constraints of contractual arrangements, support for services should be ceased when that support is no longer required to meet the objectives set out in recommendation 8, or when other key indicators outlined in 9.1 to 9.5 above indicate that support is no longer required or good value.
- 14 agree that the current suite of contracts with airlines under the IAFC (selected in November 2020) be extended by the Secretary for Transport to 31 May 2021.
- 15 agree that the Ministry of Transport would run an open market procurement process inviting air carriers to submit applications for the period from 1 June to 30 October

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2021 (with possible extension to 31 March 2022 in accordance with recommendation 9) to cover:

- 15.1 the proposed routes, frequency and capacity to be provided
 - 15.2 the applicant's track record and capability to meet the scheme's key objectives
 - 15.3 the financial viability or otherwise of the operation proposed, including details of the cost of operating, and achievable revenue.
- 16 note that proposals be assessed against criteria by the Ministry of Transport, supported as required by other agencies including the Ministry of Foreign Affairs and Trade, New Zealand Trade and Enterprise, the Ministry of Primary Industries and the Treasury.
- 17 authorise the Minister of Transport and Associate Minister of Finance (acting jointly) to approve the key terms of the contracts, and which carriers and routes would be funded under the MIAC, following advice from officials.
- 18 authorise the Secretary for Transport to enter into funding agreements with the providers in accordance with Ministers' approval as set out in recommendation 17, if suitable contractual terms can be reached.
- 19 agree to allocate funding of \$0.700m to the departmental output appropriation: "Transport – Policy advice, ministerial servicing, governance, and other functions" for the administration of the Scheme to 30 June 2022, and an expense transfer of \$0.200 million from 2020/21 to 2021/22.
- 20 agree to establish the following new multi-year appropriation, to run from 1 May 2021 to 30 June 2022 for the scheme

Vote	Appropriation Minister	Title	Type	Scope
Transport	Minister of Transport	Maintaining international air services	Non-departmental Other Expense	This appropriation is limited to a funding scheme to air carriers to maintain international air services.

- 21 approve the following changes to appropriations to give effect to the Maintaining International Air Connectivity scheme from 1 May 2021 to 31 October 2021, and for the Ministry of Transport to administer the scheme, as outlined in recommendation 8 and 19.

Vote Transport Minister of Transport	\$m – increase/(decrease)		
	2020/21	2021/22	2022/23 & Outyears

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Non-departmental Other Expenses: Maintaining international air services	170.000		-
Departmental Output Expense: Transport – Policy advice, ministerial servicing, governance, and other functions (funded by Revenue Crown)	(0.200)	0.900	-

22 note the indicative funding profile for the multi-year appropriation described in the recommendation above is as follows:

Indicative annual spending profile	\$m – increase/(decrease)		
	2020/21	2021/22	2022/23 & Outyears
Maintaining international air services	50.000	120.00	-

23 agree that the proposed changes to appropriations above be included in the 2020/21 Supplementary Estimates and that, in the interim, the increase be met from Imprest Supply.

24 agree that the expenses incurred under recommendation 21 above be charged against the COVID-19 Response and Recovery Fund.

25 agree to establish a tagged operating contingency of up to the amounts as follows in Vote Transport, to provide for the extension of the Maintaining International Air Connectivity from 1 November 2021 to 31 March 2022:

	\$m – increase/(decrease)		
	2020/21	2021/22	2022/23 & Outyears
Extending the Maintaining International Air Connectivity Scheme – Tagged Operating Contingency	-	100.000	-

26 authorise the Minister of Transport and the Associate Minister of Finance jointly to draw down the tagged operating contingency funding in recommendation 25 above, subject to their satisfaction of the conditions described in recommendation 9 above.

27 agree that the tagged operating contingency in recommendation 25 above be charged against the COVID-19 Response and Recovery Fund.

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Authorised for lodgement

Hon Michael Wood

Minister of Transport

Appendices

Appendix 1 - Terms of Reference for the Review of the IAFC and future air connectivity

Appendix 2 - Final Report: Review of the IAFC and future air connectivity

Released under the Official Information Act 1982