Key strategic issues affecting the airline industry

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Reader in Airline Economics
Scheduled and charter airlines: current issues and future developments

- Key characteristics of airline markets
- Market penetration of low cost scheduled airlines
- Recent developments in the charter sector
- Future prospects
Key characteristics of airline markets

- Unique economic regulatory framework
- Strongly influenced by economic cycles and safety related issues
- Poor profitability of most airlines
- Rapid growth of low cost airlines
- Falling yields
- Increasing consumer awareness
- Link with national identity still a feature
IATA Airlines’ Operating Margins

Source: IATA
Net profits / losses of the world’s airlines

- Net profit of US$8,500 million in 1999
- Net profit of US$3,700 million in 2000
- Net loss of US$13,000 million in 2001
- Net loss of US$11,300 million in 2002
- Net loss of US$7,600 million in 2003
- Net loss of US$5,600 million in 2004
- Net loss of US$4,100 million in 2005
- Net loss of US$500 million in 2006

- Accumulated net loss of $29,900mn (1999-2006)
Sir Richard Branson is said to have admitted when asked how to become a millionaire:

“Start as a billionaire and buy an airline.”
Industry Performance Comparisons

Average ROIC 1996 - 2004

Source: Value Chain Profitability (June 2006), IATA

Source: Airline Business, Dec 2005
The Airline Sector in 2006

- **Passengers**
  - 71.1% of scheduled world Revenue Tonne-Kilometres

- **Freight, Mail & Express Cargo**
  - 28.9% of scheduled world Revenue Tonne-Kilometres

(Source: ICAO)
Non-scheduled share of passenger traffic

![Bar chart showing the non-scheduled share of passenger traffic from 1997 to 2006.](chart.png)
Forecasting demand

- Traditional analysis identified *Economic Growth* (measured in terms of GDP per capita) or *Volume of International Trade* as the key driver of air transport demand.

- Market liberalisation and the resulting advent of low cost scheduled airlines has made demand much more difficult to forecast. The supply of seats in short haul markets is often now a more significant driver of demand.
Market Penetration of Low Cost Carriers

• Some 30% of passengers travelling on intra-European routes in 2006 used low cost scheduled airlines.

• Seat capacity of European low cost carriers rose by over 25% in 2006.

• More than 40 airports in Europe rely on low cost airlines for more than 95% of flights operated.
UK Domestic Trunk Routes

✈ Low cost scheduled carriers have had a major impact on UK domestic air routes, with 50% of passengers now travelling within the UK on such services (up from 22% in February 2001 and 37% in February 2003).

✈ London – Glasgow is one of the UK’s busiest domestic city pairs, with services provided from four of the capital’s airports.

✈ Of the 3.2 million journeys undertaken in 2005, some 46% were on flights operated by low cost airlines.
No frills traffic at UK Regional Airports

• Since 1999 UK regional airports have attracted the attentions of low cost operators

• Go, for example, began operations between Bristol and Edinburgh in September 2001, producing an even more dramatic increase in traffic volumes than that experienced on London-Glasgow

• Passenger journeys have trebled from 107,000 in 2000 to 330,000 in 2005
Bristol – Edinburgh traffic 1996-2004
Market Penetration of No-frills Carriers

- No-frills carriers account for 54% of traffic to EU destinations from the UK

- Within the EU 26% of passengers travelled on low cost carriers in 2006
Prospects for scheduled carriers

- Network carriers are competing on price and distribution – elimination of Saturday night stay requirement and booking via the Internet

- With over 30 low cost carriers now operating in Europe further consolidation is inevitable – there will only be three or four large airlines in the longer term, plus a small number of niche operators

- Independent low cost quality airlines are not viable in Europe (eg. Duo, JetMagic)
Developments in the European Charter Market

1960s
- Hotel Based Inclusive Tours
- Affinity Group Charters

1970s
- Advanced Booking Charters
- *Bucket* Shops

1980s
- Direct Sell Tour Operators
- Self Catering Inclusive Tours
- Seat Only
- Horizontal & Vertical Integration

1990s
- Long Haul Inclusive Tours
- Wider Choice of Destinations
- International Tour Operator Integration
- Competition from *No-frills* scheduled airlines

2000s
- Dynamic Packaging
Europe’s Inclusive Tour Market in 2005

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Europe’s Charter Airline Groups in 2007/2008

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Characteristics of the Charter Market

There are four types of airline company that operate charters:

- vertically integrated charter carriers
- independent charter carriers (some destination based)
- charter airline subsidiaries of scheduled flag carriers
- scheduled airlines
Market Trends

- Short Haul Charter Markets
- Long Haul Charter Markets
- Specialist Charter Markets
UK - Australia / New Zealand Charter Traffic

- **Australia**
- **New Zealand**

Yearly data from 1987 to 2005 is shown.
Come and see me in Lapland!
Future developments

- Poor financial results likely to continue
- Continuing rapid growth of the low cost sector
- Airline consolidation
- Increasing environmental constraints
- Increasing use of e-commerce
Constraining Factors

- High Oil Price
- Environmental Controls
- Infrastructure Limitations
- Global Warming Concerns
Oil Prices Rising Sharply
Brent crude spot, $ per barrel
Continuing Evolution

More differentiation:

• Lower cost business class only airlines

• Greater emphasis on customers’ convenience

• Low cost with frills

• Longer haul low cost services?