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# Reinventing the Airline Business

## If you want dinner, go to a restaurant!

**Nigel Piercy**

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# Reinventing the airline business*

## If you want dinner, go to a restaurant!

***'the airline industry has experienced a revolution in the last decades as governments have introduced deregulation'***

Throughout the world, the airline industry has experienced a revolution in the last decades as governments have introduced deregulation to allow companies greater freedom in the way they operate. However, while the major airlines have been pursuing 'hub and spoke' strategies (you are in Cardiff and want to be in Dallas, so the airline naturally enough offers to fly you from London to Detroit and then to Dallas/ Fort Worth), and global alliances, something new has emerged – the 'no-frills' airlines and flights from regional airports.

There are some interesting questions to be raised about this reinvented airline concept and whether the 'no-frills' strategy is robust enough to achieve long-term success.

## The airline industry

Traditionally, the airline industry was hemmed in by severe regulation by governments on where and how they could compete. Landmarks were 1978 in the USA when the domestic skies were

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* This material has been produced by Nigel F. Piercy from secondary sources and discussions with industry executives. 

opened up to competition and 1997 in Europe when the EU wrapped up its own programme of deregulation, allowing any EU airline to start domestic operations in another member state. (This is, however, a long way from free-for-all competition in 'open skies', but it is a start.) At the same time, many state-owned airlines have become commercial organizations.

This limited revolution in the freedom for airlines has led to many new entries to the industry, and some considerable carnage. Between 80 and 85 per cent of the new carriers launched in the USA after deregulation have already gone out of business, and in the tough times of 1993–96, sixty out of eighty new European airlines failed. Developing robust new strategies in this business is easier said than done. However, one approach to reinventing the airline business which stands out is the 'no-frills' airline, with a value proposition which is radically different to the branding and service offer of the conventional airlines. The model for the 'no-frills' airline is Southwest Airlines in the USA.

***'one approach to reinventing the airline business which stands out is the "no-frills" airline, with a value proposition which is radically different to the branding and service offer of the conventional airlines'***

## The Southwest model

Southwest Airlines started operations in Texas in the early 1970s, and it has declared a profit every year for the past twenty-five years – which is a boast that no other US airline can make. By 1997, Southwest was the seventh largest carrier in the USA, with revenues of $3.8 billion and operated a fleet of 250 aircraft. It is the low-cost airline against which its countless imitators are judged.

After a shaky start in 1971, Southwest captured the Texas market with its 'no-frills' concept, flying between Dallas, Houston and San Antonio. The large carriers, more concerned with their intercontinental business, did not take the competition seriously. This left Southwest space to build a cash-pile, which then enabled it to attack prime markets such as California. By the time it expanded, Southwest was no longer a small start-up operation.

The 'no-frills' offer Southwest makes to its customers has been the model for many others. The essential elements are:

- very low fares – with the effect of filling the aircraft with people who might not otherwise have flown at all
- cattle-car boarding with no assigned seating or classes of seat
- no in-flight service apart from a soft drink and a bag of nuts

From the outset, the airline drew attention to itself by being weird. The company takes the idea that work can be fun to extremes, led by a remorseless practical joker – Herbert Kelleher as chief executive. For example, at its launch targeting a predominantly male Texas clientele, Southwest adopted a 'love' theme: air hostesses wore hot pants and white PVC go-go boots; drinks were called 'love potions'; peanuts were 'love bites'; and tickets came from 'love machines'. (The inspiration was that Southwest flies out of DalIas' Love airport.) In a broader market than Texas and an era of rabid political correctness in the USA, the love campaign was replaced by a mission to deliver 'positively outrageous service at unbelievably low fares'.

***'Southwest adopted a "love" theme: air hostesses wore hot pants and white PVC go-go boots; drinks were called "love potions"; peanuts were "love bites"; and tickets came from "love machines"'***

The fun elements persists, however, and practical jokes and wisecracks are almost compulsory:

***'sometimes flight attendants play tricks on passengers by hiding in the overhead luggage bins and leaping out at unexpected moments'***

- sometimes flight attendants play tricks on passengers by hiding in the overhead luggage bins and leaping out at unexpected moments
- safety announcements turn into comedy routines: 'Those of you who wish to smoke will please file out to our lounge on the wing, where you can enjoy our feature movie presentation 'Gone With the Wind' . . .'
- routinely in-flight announcements are not spoken but sung

There are more serious sides to the Southwest strategy, however.

Southwest has made huge efforts to build and sustain a highly motivated workforce. The 'fun' theme is pervasive and is backed by recognition for good service, greetings cards and parties for birthdays and special occasions and a large investment in training and personal development.

The result of almost fanatical dedication to the CEO and the company is that employees show exceptional levels of productivity compared to the rest of the industry. For example, Southwest has got turnaround time between arrival and departure for its aircraft down to twenty minutes – less than half the time other carriers take to get the plane back in the sky. One reason is that flight attendants and even pilots are ready to help out in cleaning the passenger cabin, loading the bags or doing anything else needed to get back in the air.

Southwest has driven other elements of the cost structure for getting in the air to very low levels:

- operating mainly on short-haul flights with high traffic densities
- the fleet is standardized on Boeing 737s, simplifying the spare parts inventory and reducing training needs
- regional airports have substantially lower charges for airlines

As well as the low cost base and the 'no-frills' offer, there is something else striking about Southwest – its aggressive customer service strategy. In 1997 Southwest ranked first in customer service among major US airlines in a *Money* magazine survey. Lorraine Grubbs, manager of Southwest's training programme the 'University for People' says 'the frills are not what's important for most people, it's the compassion and caring and the people'.

Currently in the US market low-cost carriers account for about 30 per cent of the domestic air travel market. Southwest is the most successful, but other operators include Tower Air and ValuJet (renamed AirTran after a much-publicized DC9 crash in Florida). The other low-cost entrants did not survive the retaliation of the large airlines who reduced prices and increased capacity until the newcomers disappeared – the failure rate was 85 per cent.

## 'No-frills' flying in Europe

Following EU policies of aviation liberalization, several European 'no-frills' airlines started with the Southwest model: low fares, no on-board meals, no allocated seats, often using regional airports and lower staffing costs. Initially expected to attract mainly leisure travellers, much of the demand has turned out to be from business travellers who resent paying premium fares to travel within Europe. Estimates suggest that almost half the customers for the low-cost carriers are price-conscious business travellers. One executive was quoted in the national press, 'I've given up paying £100 for breakfast' to explain his choice of flying to Glasgow with easyJet for £68, compared to the £198 quoted by British Airways for the same trip. The low-cost flight market from the UK to Europe grew from zero to 5 per cent in just two years.

***'Estimates suggest that almost half the customers for the low-cost carriers are price-conscious business travellers'***

The 'no-frills' operators undercut the big carriers by as much as 50 per cent and focus mainly on high volume, short-haul, point-to-point trips. Low fares are achieved by exploiting several important levers to achieve low cost (the alternative of low fares

***'"no-frills" operators can get costs per seat down to* half *those of the major network carriers'***

with high costs is clearly unattractive). A recent report by the Civil Aviation Authority of the UK notes that the 'no-frills' operators can get costs per seat down to *half* those of the major network carriers. Savings come from:

- *Distribution costs* – it has been estimated that as much as 25 per cent of the cost of conventional air tickets comes from distribution, e.g. travel agent commissions and promotion, the computerized reservation system shared by major airlines and the coupon exchanges to reconcile passenger switches. Direct selling and ticketless travel avoid most of these costs.
- *In-flight catering and staffing* – conventional airlines provide 'free' meals and drinks in their ticket prices. Removing these services saves money (and a lot of waste when passengers turn down the food because they want to sleep). However, easyJet estimates that while it has three cabin crew on a short-haul flight, the equivalent BA flight will have six cabin crew, because that is the only way to distribute and collect hot towels and serve all passengers with drinks and food and another round of drinks on a short flight.
- *Fleet uniformity* – a fleet standardized on a single aircraft type drastically reduces maintenance and spares costs and crew training.
- *Regional airports* – using regional airports instead of the major hubs has several important implications. It gives access to the underserved regional population in the regional airport's catchment area; fees are lower; less congestion allows the operator to be more efficient and to get better utilization from the aircraft (because they stay on the ground for less time).

The major players in establishing and growing this market in Europe are the following companies.

## easyJet

easyJet was started by Stelios Haji-Ioannou, heir to a Greek shipping fortune, in 1995. Haji-Ioannou joined his father's shipping business after graduation and then set up his own shipping line, Stelmar Tankers, in 1992. He caught the 'airline bug' after meeting Richard Branson, founder of Virgin. He started the easyJet operation in Luton with little more than an office, a booking system and sub-contractors to provide the rest of the services. By the end of 1998 he was operating seventeen

European routes with a rapidly expanding fleet of owned aircraft. The easyJet operation has much in common with the Southwest model: point-to-point flights, short haul only, scheduled flights not charters, no frills, low fares and low costs.

Haji-Ioannou's thinking is dominated by two things: keeping in touch with the customer and driving out bureaucracy in the business. In spite of his personal shyness, he flies his own aircraft three or four times a week to talk to the passengers and he delights in customer letters thanking him for making air travel affordable, saying things like 'You've saved my love life, you made it more affordable for me to go and see my other half!' He believes in motivating his staff by example – focusing on the external enemy by holding 'war meetings', standing up to signal urgency.

The easyJet mission is stated as 'To Make Flying Affordable' and Haji-Ioannou says the goal is that more people will fly, and the same people will fly more often. He describes his target customers as everyone who pays for travel out of their own pockets (including leisure travel but also business), with the exception of 'fat cats who want airmiles'.

***'The easyJet mission is stated as "To Make Flying Affordable"'***

His frustration with the formality and bureaucracy in his father's company has turned into a quest for informality and the paperless office in his own company. He describes easyJet as a 'socialist company' in which 'there are no secrets', because all employees have access to the computer system on which all information is stored. He says easyJet has a 'unique people culture', no neck-ties, no fuss, no formality, no secretaries for executives, no private offices, and no paperwork, but plenty of parties, including a regular Friday afternoon barbeque at the back of the Luton office. Haji-Ioannou says he aims to recruit people with talent and character who will enjoy working in the easyJet culture and this counts for more than experience in the traditional airline business.

In fact, easyJet was modelled directly on the Southwest Air approach from the very beginning, boasting that flights from the Luton-base to Scotland would 'cost as little as a pair of jeans' – starting from £29 one-way. At this time, the London to Scotland fare with conventional airlines was more than £100. Route extensions include Amsterdam, Nice, Athens and Barcelona as well as Scotland. It has established a second hub in Liverpool with flights to Amsterdam and Greece. In 1998 plans were announced for a massive increase in easyJet's fleet with orders placed for fifteen new generation Boeing 737–700s, in addition to a 1997 order for twelve older generation 737–300s. This will increase the fleet from seven to thirty-five aircraft in five years.

In 1998, easyJet bought a 40 per cent stake in TEA Switzerland, a Swiss chartered carrier with four leased Boeing aircraft, with the option to increase the stake to 90 per cent. The goal is to relaunch TEA as easyJet Switzerland as a 'no-frills' airline and to ease pressure on the Luton Airport base. A major attraction of this purchase was that TEA operated the same aircraft as easyJet, so the fleet increased but remain standardized.

***'easyJet's founder is fond of reminding his customers, "If you want a meal, go to a restaurant"'***

Costs have been contained, Southwest-style, from the outset. easyJet's founder is fond of reminding his customers, 'If you want a meal, go to a restaurant'. Passengers are fed jokes instead and also have to face recycled boarding passes, no first or business class privileges, and the trek out to secondary airports such as Luton. Luton is the alternative to London Heathrow, Liverpool is the alternative to Manchester, and the purchase of TEA makes Geneva a third base (recently vacated by Swissair pulling out).

In addition, easyJet is a 'ticketless' airline. By refusing to honour competitors' tickets, easyJet avoids the paperwork of exchanging coupons to get paid for carrying other people's passengers and the need to issue tickets. Mr Haji-Ioannou says, 'Your right to fly comes from the fact that your name is in the computer – not from any document you hold. That's the paradigm shift.' easyJet runs its own call centre and reservation system and does not have to pay to participate in the reservation systems operated by the full-cost airlines.

For similar reasons, easyJet does not pay commission to travel agents; it relies on direct sales made by telephone booking clerks, paid 80p per seat sold. Pursuing the same logic, easyJet emphasizes online booking by customers visiting the easyJet Internet site – the web address is painted on the side of the aircraft in giant orange characters. By the end of 1998 Internet sales were already 10 per cent of total revenue and growing – the company hopes to take 30 per cent of its booking through the web site by the end of 1999. Indeed, Haji-Ioannou plans to open a chain of Internet cafes, easyEverything, which will enable consumers with no home Internet access to book tickets online, as well as accessing e-mail and Internet-based shopping.

In late 1988, easyJet was the first no-frills airline to feature in *Company Barclaycard's* annual survey of business travel. It was rated higher in reliability than BA or KLM and the majority of business travellers in the survey reported that the small airlines gave better service. Of the business travellers who had used a no-frills airline, an impressive 86 per cent said they would do so again.

The aggressive attack on BA's European business travel market by easyJet is illustrated by the copy of a national press advertising campaign launched in November 1998.

**RECESSION?**

In a boom, nobody worries about the travel budget. In a recession everyone with shareholder value at heart should question the cost of flying BA Club Europe. A Harris Poll, commissioned by easyJet, proves that one of the reasons executives refuse to fly with easyJet is that they don't get any air miles. Air miles is just a bribery scheme and the greatest enemy of the travel budget.

**Other excuses used by 'fat cats' can be dealt with as follows:**

1. **The corporate travel agent does not book easyJet!** … because easyJet does not pay them any commission. You or your secretary can book direct over the phone or via the Internet. Alternatively, if your company is big enough, get the travel agent to do it anyway!
2. **Luton is too far away!** It takes about an hour from central London to any of the London airports.
3. **Bookings are not flexible!** Rubbish! First you can buy one way, none of these idiotic minimum stay rules. Also ask for the £10 change fee for a truly flexible fare at one third of Club Europe.
4. **Not enough flights in a day!** 3–5 flights a day on most business routes must be enough.
5. **Surely the aircraft must be old!** An all-Boeing fleet, one of the youngest in the industry. Another 40 brand new ones will be delivered over the next few years.
6. **But easyJet is a Mickey Mouse airline!** So, why did Bob Ayling (the CEO of BA), having failed to buy easyJet, create a carbon copy of it?

**easyJet**
**0870 6 000 000**
**www.easyJet.com**

easyJet's UK operating company lost £3.3 million in 1997, but in January 1999 announced annual pre-tax profits of £2.3 million, based on a 65 per cent increase in passenger numbers producing turnover of £77 million. Haji-Ioannou has no immediate plans to float the company.

### Debonair

Luton-based Debonair flies to and between six European destinations. It mixes direct selling with travel agency bookings, and keeps costs low by contracting out everything from check-in to maintenance. Over half its customers are business travellers. Large companies such as Xerox and Rover routinely book all but their most senior executives on Debonair, if they have a choice of carrier.

***'Large companies such as Xerox and Rover routinely book all but their most senior executives on Debonair, if they have a choice of carrier'***

Debonair is slightly different to the other operators. It offers a free snack and tea and coffee, for which the others charge, and has introduced a business class section. Debonair also operates conventional seat allocation. Chairman Franco Mancassola believes that the European traveller is too sophisticated for the complete 'no-frills' approach and the chairman denies that his company is a 'no-frills' operator. The company is expected to move into full profit in 1998–99 and announced its first quarter's profit in December 1998, after two years of heavy losses.

Mancassola has tried to insulate Debonair from some of the stresses of the low-cost market by signing contracts to fly on behalf of larger airlines, including Lufthansa and Air France. With low operating costs, Debonair is positioning as a subcontractor for conventional airlines, to fly cheaply on low-yield routes.

In 1998 Debonair looked set to double the size of its fleet with an order for 10 new Boeing 717s. Debonair has started a joint venture with AB Airlines at Gatwick and is looking at adding routes to Eastern Europe.

### Ryanair

Ryanair was originally a conventional full-service airline started by Tony Ryan to compete with Aer Lingus, by offering lower prices. The results were a disaster – Ryanair lost £18 million in four years and went through five CEOs. Current CEO, Michael O'Leary, adopted the Southwest model and extended services from Dublin to London to the rest of Britain and now some Continental Europe routes. An aggressive competitor, O'Leary was accused by the Irish premier of 'tooth and claw capitalism'.

***'O'Leary was accused by the Irish premier of "tooth and claw capitalism"'***

Now one of Europe's most experienced low-cost carriers, while easyJet remains a private company, Ryanair shows that low-cost airlines can currently make profits in Europe, showing 1997 pre-tax profits of I£24.5 million on turnover of I£136 million. The airline is renowned for constant 80 per cent load factors. Ryanair has been skilful in avoiding direct competition by taking on underdeveloped routes from Dublin to UK regional cities. Analysts judge that Ryanair has created more of a market than it has taken away from traditional airlines. When it started flying Dublin to London in 1985, the route carried one million passengers a year, but by 1998 this had reached four million at a one-way fare as low as £19.99.

In 1998, Ryanair held an autumn seat sale cutting fares as low as £16.99 one-way to Europe. Floated in May 1997, 1998 saw passenger volumes rise 35 per cent on the previous year. Floatation funded the expansion of the fleet from twelve to eighteen aircraft.

### Virgin Express

Virgin operates from Gatwick and Heathrow and is priced between easyJet and the big carriers and flies from Brussels to seven destinations, including Rome, Barcelona and Nice. A relative newcomer, Virgin achieved break-even in 1996 and a small profit in 1997. Based in Brussels, Virgin partners with Sabena to fly the Belgian carrier's passengers into Heathrow – Sabena sells the tickets and their passengers sit in a separate business class section on the Virgin plane. By 1998, in a drift away from the 'no-frills' concept, Virgin was increasing passenger leg-room and looking at launching a frequent flyer programme. In 1997 the company announced plans to become a publicly quoted company with a dual listing in the USA and Belgium. Plans also involved increasing the fleet to eighteen aircraft by 1998. Virgin Express issued a profits warning in August 1998, and the third-quarter results issued in December that year showed that escalating operating costs (mainly caused by leasing expensive fully-crewed aircraft to overcome pilot shortages) had resulted in a 77 per cent fall in profits. Shares have fallen from $15 to $7.06. The company has applied for an Irish air operator's licence to shift some of its base to Ireland and reduce some operating costs.

In spite of this initial success for the low-cost airlines, industry commentators have been predicting a phase of rationalization and consolidation, as happened in the USA, with the weaker operators closing.

However, the most dramatic event in this sector has been the response of British Airways in launching its own low-cost 'no-frills' airline in 1998 – Go.

## The nightmare begins . . .

Perhaps the most dramatic proof of the impact of the 'no-frills' model is that BA has been forced to respond in a dramatic way, because it was hurting, and in spite of the clear risk to the value of its main brand.

***'BA has been forced to respond in a dramatic way, because it was hurting, and in spite of the clear risk to the value of its main brand'***

As the dominant UK airline, BA's first response to the 'no-frills' operators' impact on its business was to discuss a take-over with easyJet. BA had earlier talked to Ryanair. BA backed off from the easyJet purchase, apparently concerned that move would be blocked anyway by the UK regulators. A possible alliance was also discussed with Debonair.

easyJet reacted with hostility to the rumour BA was entering the 'no-frills' market, apparently concerned that BA would use the information gained in their acquisition discussions and legal action was threatened. Less worried at the rumour was Michael O'Leary, CEO of Ryanair, who simply observed, 'If British Airways think they can set up a discount airline, they must be smoking too much dope.' Debonair and Richard Branson both threatened action on the grounds that entry by BA would be a blatant attempt to destroy the low-cost competition.

***'If British Airways think they can set up a discount airline, they must be smoking too much dope'***

In fact, entering the 'no-frills' market represents a major risk for BA. It faces a difficult industrial relations problem with lower wages and could end up simply cannibalizing its own customer base, i.e. transferring full-fare passengers from BA's Heathrow flights to discounted fares out of Stansted. It could also damage BA's brand and its new positioning unveiled in 1998.

None the less, in November 1997 BA announced the launch of its new European airline offering reduced in-flight service and lower fares at around a 30 per cent discount against BA's regular prices. Initial plans were to fly to Italy, Spain, Scandinavia, France and Germany out of Stansted airport. The new operation is a separate structure from BA, with its own brand, headed by Barbara Cassani, formerly BA's general manager in the USA. From the outset, Go had a different physical location to BA headquarters, to reinforce its 'separateness' from the main airline. Seats can be purchased over the telephone, with no tickets issued, streamlined check-in and no free in-flight food and drink. Rumoured to have been given a start-up budget of £25 million, Cassani described her vision as transforming the low-cost airline business: 'We will be the IKEA of the airline business. What IKEA did to make cheap furniture tasteful, we will do to the low-fare market. There will be more style to this market than has been seen before.' The new brand is Go.

***'We will be the IKEA of the airline business. What IKEA did to make cheap furniture tasteful, we will do to the low-fare market'***

Go attacked the market in May 1998 with a £100 fare to Rome, Milan and Copenhagen. easyJet and Debonair accused BA of subsidizing the new operation, because this level of fare could not make a profit. Go sold 18 000 bookings in its first month. However, Go increased its fares by around 80 per cent within two weeks of launch, to a level where it was more expensive than other operators such as Virgin Express, Debonair and KLM UK on its main routes. Go still faces court action on its possible subsidies from BA.

# The war continues

The result of the Go entry has been to trigger an unprecedented level of competition in this part of the air travel business.

### The commencement of hostilities

BA's Go operation launched in 1998 with a London to Edinburgh flight priced at £70 for a standard return and £100 for a fully flexible return. The result was that this route was competed by five airlines (including BA itself along with the low-cost carriers and KLM UK). On this route the easyJet fares ranged from £68 to £228, KLM UK's fares were between £68 and £288, BA from Heathrow and Gatwick was charging between £69 and £276.

In answer to the question of whether the low-cost airlines can compete with this attack, Haji-Ioannou of easyJet says:

> The short answer is that we can compete with them if they play fair. Fair competition means they are exposed to the same costs and risks of failure that we are. In other words, they get their aircraft, fuel and insurance at the same price, and not BA prices which are substantially lower. The second thing is the pressure to make money. My first reading of the situation is that I don't believe Go is run with the intention of making money. I don't believe that anyone can make money at the prices they have just announced.

easyJet's Stelios Haji-Iaonnou promised that there would be 'the mother of all fare wars' as a result of Go's attack. Some of his aircraft carry the message in giant orange characters along the fuselage: 'Stop BA, Stop GO'. By September 1998 in response to Go's launch and the BA summer sale of tickets, Ryanair hit back with seats from London to Scotland, France, Italy and Sweden priced at £16.99 single, from all UK ports to Dublin at £29.99 single, and from London to other European destinations charging £29.99 single. Michael O'Leary of Ryanair commented, 'If BA wants a fares war, they have come to the right place. We have the financial clout to be able to do this.' The Ryanair seats were priced below cost to fill unused capacity.

The response from KLM UK concentrated on adding additional flights on the routes competed by Go in an attempt to have departures around the Go flights and to increase capacity. Similarly, Virgin Express has started operations from Gatwick (not currently available to Go, which has to use the less convenient Stansted airport), by purchasing Sabre, a charter airline for £8 million in April 1998.

Aggressive advertising by easyJet in the national press focused on antagonism towards BA. For example, one full-page ad included the following copy:

**Does the world's favourite airline really want a low cost carrier?**

1 They will screw it up and lose a fortune
2 They will confuse their customers who won't know what to expect
3 They will cannibalise their main business with passengers switching to the new airline
4 They will turn up the heat with the unions already sensitive from a summer of discontent
5 A direct sales strategy will stir up travel agents who may boycott their long haul flights
6 They will open the door to legal action from existing low cost airlines

**If they're not doing it for the money the only possible reason is to eliminate smaller competitors like easyJet and then put their fares up again!**

Source: *Financial Times*, 28 October 1997.

Interestingly, these messages were clearly designed to reach BA shareholders and airline regulators, rather than customers. Other ads placed by easyJet characterized Barbara Cassani and Robert Ayling as 'Beauty and the Beast', and congratulated Cassani for promotion from BA's 'Dirty Tricks Department' to the 'BA Cheap Tricks Department' (referring to Cassani's alleged role in the BA campaign against Richard Branson and Virgin Atlantic for which BA has been fined by the British courts).

***'ads placed by easyJet characterized Barbara Cassani and Robert Ayling as "Beauty and the Beast"'***

High court actions in May 1998 accused BA of 'classic predatory behaviour' and a 'lack of transparency' in launching Go to kill off the low-cost airlines in breach of European competition rules. easyJet claimed BA was illegally cross-subsidizing Go by guaranteeing its aircraft leases to get more favourable rates and exploiting BA's brand image to associate Go with higher standards of reliability and safety. By October 1998, easyJet was urging the European Commission to bar Go's £15 single fare from London to Edinburgh, because it was a 'cheap trick' subsidized by BA and designed to crush the competition.

Debonair also took BA to the European Commission accusing Go of abusing its dominant position on the London–Rome route by predatory pricing and dumping excess capacity on the route. This claim was rejected by the Commission, but it is just one of many to be decided.

It is interesting to note the exploitation of the European regulators as a competitive weapon. Haji-Ioannou claims that the European regulators are far more prepared to protect the new airlines than were their counterparts in the USA. He says that when the European Commission began investigating his earlier complaints against KLM trying to drive him off the London–Amsterdam route, the Dutch carrier behaved less aggressively towards him. European Commission officials raiding KLM's offices for evidence may explain this. He says 'The European authorities are much more on the ball'.

## What happens next?

The growth of the low-cost 'no-frills' operators in Europe has been highly successful and profit performance has generally been good. The major issue is whether this performance can be sustained.

Certainly the US experience has been that most of the low-cost airlines have failed. While some of the conventional carriers such as Delta have low-cost off-shoots, the only really successful low-cost operator is Southwest. The US transportation department explains that when the new low-cost entrants started services, the large airlines responded by cutting prices and offering more seats. Once the new carrier was forced out of business, the big airline raised prices and withdrew the extra seats. One analyst notes that where Southwest flies, fares are low, but where it does not operate fares are not low. The computerized reservation systems make it relatively easy for an airline to find what competitors are doing and adjust prices accordingly.

***'the moment of truth is approaching for the low-cost operators'***

Sir Michael Bishop of British Midland suggests that the moment of truth is approaching for the low-cost operators. He argues that the low rates they have been offered by airports will end and move to market rates; the profits from duty-free sales are about to end; and several of the low cost carriers will have to buy new aircraft to comply with new EU noise regulations. He picks Debonair as the likely first casualty.

The biggest threat, however, is the BA Go strategy.

In the past, BA has removed independents by acquisition – it took over both British Caledonian and Dan-Air. Attempts to buy easyJet or Debonair floundered. There is no doubt that Go is intended to retrieve the business lost to the 'no-frills' airlines, as well as to participate in the travel market growth that can be achieved by low fare strategies.

***'"When is a no-frills airline, not a no-frills airline?" The answer is: "When it adds the frills back again"'***

In addition, industry analysts are asking the question: 'When is a no-frills airline, not a no-frills airline?' The answer is: 'When it adds the frills back again'. There are several signs that a number of the low-cost airlines are finding it difficult to sustain the 'no-frills' strategy and are drifting back to become cheaper versions of the full-fare airlines.

Many expect that the European experience will follow the US model, with a phase of consolidation, leaving only the strongest low-cost brand as survivor.

Certainly, 1999 opened with special offers and price cuts predicted to lead into the lowest fares ever. Ryanair offered free seats to passengers buying already-discounted tickets – London to Glasgow was discounted to £29.99 – and receive an extra seat for free. Go responded with deep price cuts – bringing the return fare from London to Rome down to £70. Airline executives anticipated that the New Year ticket sales signalled the start of a price war likely to continue through the year. All the budget airlines have new aircraft arriving during 1999 with a lot of capacity to sell at a time of customer uncertainty adversely affecting travel. Rumours of a merger between easyJet and Virgin Express have been noted.

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