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ascend

Taking your airline to new heights

A man in a dark pinstriped suit and tie is smiling and holding a small white model airplane. He is standing in front of a window with horizontal blinds. The lighting is soft, highlighting his face and the model airplane.

World's Happiest Airline

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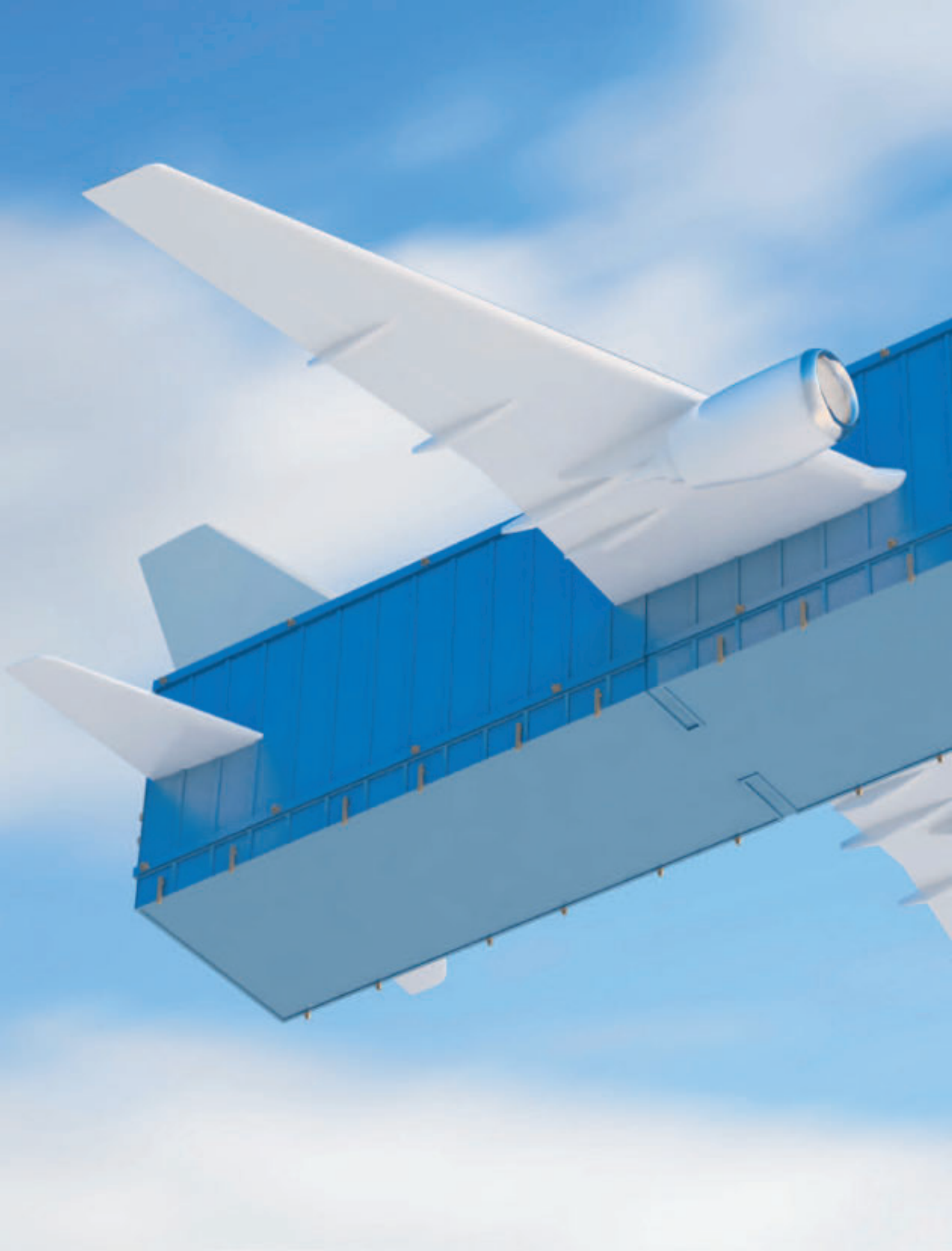
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Effectively diagnosing MRO issues and prescribing solutions





Cargo Infusion

Airlines that implement a sound cargo revenue management strategy coupled with the use of advanced technology and industry best practices will achieve significant financial gains based on the anticipated rapid growth in the air cargo sector.

■ By Mukundh Parthasarathy | *Ascend* Contributor

During the next decade, air freight growth — particularly driven by the demand for time-sensitive services — will outstrip passenger growth at an average annual rate of 6 percent, according to forecasting research conducted by aircraft manufacturers Airbus and Boeing.

Airlines will face enormous opportunities and challenges presented by an increasingly integrated and fiercely competitive cargo environment. Intense competition means air cargo operators will need to be more efficient to maintain and grow their current market position while focusing on optimized capacity management to grow revenues.

Since most passenger aircraft offer belly capacities for air freight, airlines can provide cargo services at low marginal costs. Therefore, competition on a pricing level can easily occur, so effective revenue management principles and systems will become essential for managing capacity and pricing.

Air cargo is an important revenue source for airlines and air freight forwarders. On average, the revenue from cargo is 13 percent of the total air traffic revenue — up to 40 percent for some airlines. The global air cargo market is growing in tonnage and sophistication. Alliances among air carriers, multi-user booking portals, international online booking platforms, new freighter and combination aircraft, time-definite express services and advanced information technology represent significant pieces of the air cargo puzzle.

World air freight is expected to grow more rapidly than mail, averaging annual growth of 6.5 percent through 2021, and world air cargo traffic is expected to exceed 464 billion revenue ton kilometers in 2021. Boeing predicts the global freighter fleet will increase from 1,775 in 2001 to 3,078 in 2021. Medium and large wide-body fleet share will grow from 39 percent to 60 percent during the same period.

Unfortunately, the increase in air freight cargo traffic as measured in RTKs does not necessarily mean increase in profit. According to Mercer on Travel and Transport specialty journal (2004), in the historical period from 1974 to 2001, the average annual increase of 5 percent to 7 percent in air cargo traffic translated to an annual cargo yields decline of 2 percent to 3 percent. According to Boeing analysis, the trend for scheduled freight yields declined 3.4 percent a year from 1985 to 1999, after adjusting for inflation. After 1999, freight yields stabilized and slightly increased by the end of 2001.

Why is it difficult to make a profit in the air cargo business? There are several internal and external factors affecting profits such as overcapacity, demand imbalances, unfavorable cost structure and poor revenue management. There are also other challenges or threats such as globalization, security, rising energy costs and tough competition



A significant revenue source for airlines, average revenue generated from cargo represents 13 percent of the total air traffic revenue, up to 40 percent for some carriers.

from integrators. These challenges limit the ability of certain carriers to effectively compete in the marketplace and survive through tough financial periods.

The industry also has significant opportunities to reduce costs, improve service levels and increase profits. Initiatives such as Cargo 2000 and eFreight as well as the introduction of cargo portals and eBooking focus on improving customer service levels; increasing productivity and efficiency of information processing, transmission, display and storage; and reducing booking response times.

The greatest weakness of the cargo industry is not being proactive in terms of managing challenges and capitalizing on opportunities. Even worse is the high inertia and slow pace in reacting to challenges, adapting to changes and adopting new initiatives and technologies. Even large cargo carriers and their thought leaders have not fully deployed or adopted the International Air Transport Association's Cargo 2000 initiative to implement processes that are backed by measurable quality standards to improve efficiency of air cargo. A number of mid-size carriers still do not have systems or technology to accurately sell space, monitor movement and manage customers.

The key strength of the air cargo industry comes from two key partners — airlines and freight forwarders. These players either work together for success or work separately and fail. This applies to working together on all initiatives that are put forth

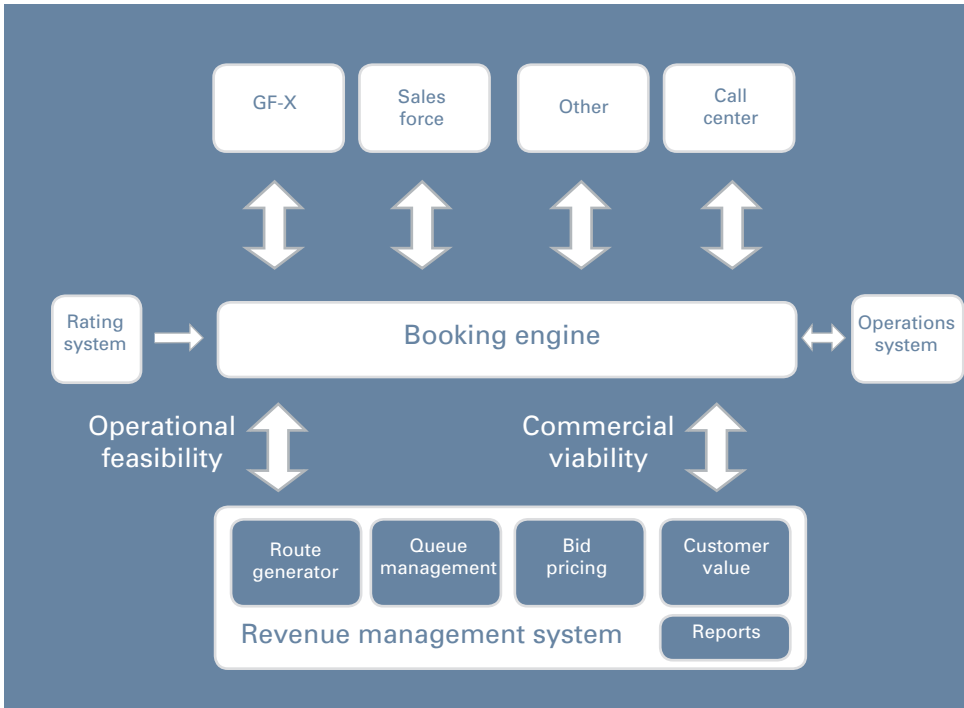
by IATA to introduce efficiency, achieve cost reduction and improve customer service. It also applies to turning around the downward spiraling effect of forwarders demanding lower prices and airlines providing poor services due to diminished yields.

The next key strength for cargo carriers comes from being visionary and taking the first step in improving tools and technologies. These carriers should empower their employees by providing the best operational and decision-support capabilities and tools.

Leveraging these two key strengths could potentially transform a business that is struggling into a win-win situation for freight forwarders and carriers, creating substantial growth potential and outstanding customer service.

Airlines around the world should adopt, automate and streamline business processes to raise productivity levels and improve revenue. Principles of revenue management can help in achieving such goals. With uncertain economic conditions, cargo profitability is increasingly important to air carriers, who have found that if cargo capacity is not managed successfully, revenue opportunities are lost.

Revenue management increases airline cargo profits through effective cargo space management. Extensive computer models can help estimate capacity for each departing flight and determine the most profitable space allocation for various cargo products. Working with real-time



The integrated booking process depicts the workings of a completely automated cargo booking engine and the interaction between the various cargo IT systems and modules.

information, analysts can efficiently manage future flight capacity.

In the early 1980s, revenue management disciplines were first applied in the airline industry as a method to increase revenues resulting from passenger sales. With the success of revenue management to improve passenger revenues, these techniques were applied to other business areas such as cargo, hotel and car rental industries.

During the past five years, air cargo thought leaders, such as Lufthansa Cargo, Air Canada, United Airlines and Virgin Atlantic, have successfully implemented cargo revenue management tools to realize revenue improvement and productivity gains. Airlines benefit from revenue management by selling space at a price that maximizes revenue from various customers based on their willingness to pay, which varies depending on the product they buy from the airline. The reasons and the characteristics of the air cargo business make it a prime candidate for revenue management:

- Cargo carried on passenger aircraft, making it difficult to know available cargo space,
- Different products are offered at different prices based on different customer requirements — same-day express shipping versus second-day shipping, for example,
- Booking behavior of customer in terms of under/over tendering, no shows and cancellations.

An effective cargo revenue management system determines the available capacity on each flight, identifies the amount of each type of product that requires space on each flight and allocates capacities to the appropriate products to maximize profit. Lessons learned from airlines' implementations also emphasize the need for business process analysis

along with automation. If revenue management technology is implemented without proper business process analysis (the solution adoption) trust in system numbers can take a long time reiterating the fact of "junk in, junk out" as with any information technology system.

A standard business process analysis study:

- Identifies business where airlines still maintain some pricing leverage,
- Ensures airlines provide satisfactory service levels,
- Eliminates unprofitable businesses and/or routes,
- Provides products that meet the needs of the supply chain.

There should also be a comprehensive review of cargo practices and performance that should contain multifaceted diagnostic analysis, quick hits and longer-term recommendations, assessing current key performance reporting indicators, reports and decision-support capabilities. The study should also help design an organization structure to support efficient business processes related to good revenue management practices. The final recommendations should include information systems; human resources, roles and responsibilities; policies and procedures; and communications policies related to cargo operations and revenue management practices.

While some carriers grapple with the decision to jump on the cargo revenue management bandwagon, thought leaders are in the process of moving toward the next-generation revenue management solution that includes an intelligent reservations system, or booking engine. The current process of booking shipments in the air cargo industry requires a high degree of manual intervention. Agents will call

or fax airlines (and often different offices at the same airline) to find the best price on a specific route. Once the airline's cargo call center agents receive shipment information, they have to refer to various systems to obtain information on rates, capacity and loadability checks; IATA regulations; and customs and embargo requirements as well as comply with their own internal regulations. Additional calls to the revenue management or marketing departments may be required before obtaining the final acceptance for the shipment request.

A booking engine is one of several components required to support intelligent booking and inventory control. A booking request can originate from several channels such as a GF-X or CPS portal; the airline's call center or website; or messages from forwarders or other airlines. The primary role of the booking engine is to act as the intermediary between the various booking channels and the revenue management system. It also interfaces with the rating and operations systems and facilitates the evaluation of every booking request.

Several key inputs are needed to make a booking decision (to reject or accept). A booking request has to meet both operational feasibility and commercial viability. Operational feasibility is ensured by selecting routes that are feasible in terms of door size, shipment characteristics, terminal characteristics, loadability, service time, etc. Commercial viability is guaranteed by ensuring the rates offered are higher than the hurdle price (bid prices). Hence, the four most important inputs are routes, capacities, rates and hurdle prices. Capacities are stored in the booking engine or the operations system. Routes are typically generated using a route selector that is either part of the booking engine or revenue management system. In some cases, a stand-alone router is also used. Rates are obtained in real time from the rating/revenue accounting system. Hurdle/bid prices are generated by the revenue management system. A booking engine essentially acts as a broker to combine this information to decide on booking acceptance.

The benefits of revenue management solutions are well documented, and the custom is rapidly becoming an industry best practice. The data challenges are still complex in cargo; therefore, the comparison between passenger revenue management techniques with that of cargo is not completely accurate. The current generation of cargo reservations systems is a mirror image of legacy systems and still does not help streamline the air cargo process, making it essential for carriers to incorporate more automation into their revenue management practices. **F**

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