

ascend

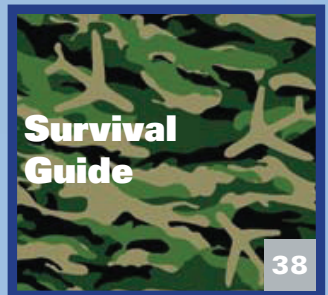
Taking your airline to new heights

A Clear Vision

A Conversation With ...
Sean Durfy, Chief Executive
Officer, WestJet Airlines,
Page 16.



Special Section



8 Japan Airlines takes steps to improve its environmental performance

21 Delta Air Lines/Northwest Airlines merger impacts regional carriers

44 Airlines have three basic options to raise capital



Looking Back For Tomorrow

Even in times of economic difficulty, certain carriers seem to have a knack for making the best of their situations. And they set the bar high for everyone.

■ By Phil Johnson | *Ascend* Staff

The airline industry will always pose challenges to carriers striving to achieve profitability year after year. And some of those challenges come in the form of adverse economic circumstances that no one can accurately predict, but everyone has to address and overcome.

There was, for instance, the severe economic slowdown resulting from the terrorist attacks of 9/11, and there have been tsunamis, typhoons and hurricanes as well as major worldwide or regional health scares such as severe acute respiratory syndrome, or SARS. And now, the world's airlines face a global economic bloodletting — the full extent of which is yet to be determined.

Nonetheless, a very select few carriers seem to have the ability to survive critical challenges ... and even thrive in times of economic turmoil and uncertainty.

Among those carriers, for example, is Southwest Airlines, which long ago established a standard of low-cost excellence that many envy but few have been able to successfully emulate.

But other carriers around the world are blazing their own trails to success in spite of sometimes-adverse circumstances, and it's useful to carefully analyze how they've done it. If nothing else, there may well be something to learn from those carriers — something that could prove of future value to another carrier during difficult times.

Besides Southwest Airlines, some other carriers that have exhibited remarkable resiliency in spite of difficult circumstances are Etihad Airways, which maintains its headquarters in Abu Dhabi, United Arab Emirates; LAN Airlines, headquartered in Santiago, Chile; TAM Airlines, headquartered in São Paulo, Brazil; and WestJet Airlines Ltd., headquartered in the western Canadian business hub of Calgary, Alberta, Canada.

WestJet, in fact, is often mentioned along with Southwest Airlines as a carrier that

has found similar success using a low-cost strategy. Extending the two carriers' similarities, they've announced plans to establish codesharing between them (and at the same time, Southwest Airlines is moving toward codesharing with Mexican low-cost carrier Volaris).

Incremental moves such as these codeshares (see related article on page 47), of course, serve to strategically extend these carriers' brand reach throughout much of North America. And in terms of potential for growth under uncertain economic circumstances, the "incremental," meticulously measured growth strategies are often the approaches that prove to be the wisest and most sustainable over the long term.

The shareholders of public companies, after all, expect and demand at the very least an incremental return on their investments. And codesharing among like-minded, cost-conscious but highly service-oriented carriers such as Southwest Airlines, WestJet and Volaris allows these carriers to achieve incremental, measured growth without requiring any of the carriers to make a huge investment in infrastructure.

Looking at the bigger picture, then, what are some of the common factors that have enabled carriers such as Etihad in the Middle East, LAN and TAM in South America, and WestJet and Southwest Airlines in North America to not only survive but fundamentally prosper, regardless of the extraordinarily difficult obstacles that all carriers come up against in challenging and volatile economic times?

While it's impossible to brood brush each carrier with single strokes that link their individual strategic moves to one another, there are some larger generalities that seem to be fairly common among them (as well as among select highly successful companies in every industry).

The first characteristic of success is dynamic leadership. No company shines eco-

nomically without a healthy dose of leadership that is inclined to think innovatively and, after careful and thoughtful analysis, act decisively.

Another characteristic to be found scattered broadly among these successful carriers is a willingness to "break the mold" — even a historically successful mold — to achieve positive results by differentiating themselves from their competition. Just because "nobody else" has ever done something doesn't mean it's a bad idea. But it must still be carefully evaluated for financial viability — and to make sure it lines up with the carrier's business model and service promise to its customers. And only at that point, the carrier may proceed, with caution, but also without hesitation.

In somewhat the same vein, another characteristic of success is these carriers' application of a "no-fear" principle — they appear to have no fear when it comes to doing what they believe is right even if it's different from what the rest of the industry is doing. In other words, there's no fear to venture into business territory that these carriers feel — based on their thoroughly researched and thought-out business assumptions — may prove to be very fruitful.

A fourth success characteristic among these tenaciously forward-thinking carriers is a basic institutional awareness that nobody in the industry holds a "silver bullet." This principle basically means there's no substitute for hard work and an optimistic approach — service with a smile and working with a "fun" perspective, but the fun must be accompanied by an ultimate willingness to work extremely hard to overcome every obstacle and outpace every competitor.

Fifth among these carriers' successful characteristics is the ability of each carrier to take its situation, whatever the specifics, and make the best of it. It may be easy to complain that budgets are short and means are lacking, but whatever situation prevails, these successful carriers have managed to

turn it into an overall positive and come out on top.

One more characteristic of all of these successful carriers is a fundamental realization that they live, breathe and compete each and every day in a service industry — and that industry first, foremost and always is all about the customer.

“It’s a customer-centric model that they have been able to build,” said Kannan Ramaswamy, Ph.D., a professor of management at Thunderbird School of Global Management in Glendale, Arizona, who specializes in aviation strategy research.

“Among the things using this customer-centric model means is that when I am incurring cost, I don’t automatically assume that it can be passed along to the customer,” said Ramaswamy. “And that, in turn, means that even though I’m differentiating my product, I’ll have to keep my costs in check in order to be able to afford the ability to give the customer a good experience. In the most basic terms, I need to be able to give my customer more for less.

“So this is all about the customer experience — and Southwest [Airlines] is a very good example,” he said.

Some of the techniques Southwest Airlines has been able to successfully apply over the years — such as flying a single aircraft type — are aimed directly at keeping its costs of doing business reasonably low to be able to pass lower fares on to its fiercely loyal customers.

Again, however, situations arise that affect every airline, yet every carrier doesn’t necessarily handle those situations advantageously. In that case, what’s the difference that opens up avenues to success?

“As an industry, there are always challenges,” said James Hogan, chief executive officer of Etihad Airways, in a March 2007 interview with the Australian Broadcasting Corp. “There are so many factors out of our control, whether it’s SARS, tsunami, war, fuel.”

All these things have presented significant challenges that have affected every carrier that operates where these factors have been present. And, as Hogan said, “We’re in a business where there are so many variables that can take you off track.”

Still, Hogan, who was formerly CEO of Bahrain-based Gulf Air, fully realizes that Etihad has the ability to seize certain advan-

tages if it chooses. And in a presentation to the Wings Club in New York City, New York, last September, Hogan explained the basics of the Etihad approach.

“The ‘magic three’ factors of location, investment and vision have combined to create an opportunity never seen before in the industry,” he said. “In less than 10 years, Abu Dhabi, Doha and Dubai have gone from serious players in regional aviation to major players on the global stage.

“Abu Dhabi’s location offers an ideal position from which to set off to the rest of the world, placed perfectly between East and West. Indeed, if you were going to launch a new global airline, there are few better places you could choose.”

In addition to geographic positioning, equipment type presents another critical factor in Etihad’s ability to succeed year after year.

“Another important catalyst is the investment we have made in new equipment — and particularly in the latest aircraft technology,” Hogan said. “The new breed of long-haul and ultra-long-haul aircraft make nonstop travel from our region to all four corners of the world a comfortable and convenient reality.

“Because we are ‘new’ carriers [Etihad only started flying in 2003], we are able to invest in modern, efficient and environmentally friendly aircraft, with none of the ‘legacy’ issues affecting the more-established industry players today.

“And finally, we have vision: the vision of Abu Dhabi’s leadership not just in creating a travel hub, but in developing a focal point for the wider aviation industry — all part of the ongoing effort to diversify our economy in the future.”

In the same speech, Hogan addressed several other questions about issues Etihad has faced during its mounting successful climb to prominence.

“Let me explode a few urban myths,” Hogan said. “We do not receive government subsidies or guarantees, and neither do we benefit from free or discounted airport and fuel costs. We hedge fuel. We borrow money from financial markets. There are no ‘free kicks.’

“Our shareholders — the investors of this region — demand accountability, a return on investment and a well-run business. And we have a real and genuine commercial mandate — a mandate that will see us break even over the coming years despite heavy investment in new aircraft and on new routes.”

Those routes include some of the most exciting possibilities in the world of air transportation today, such as one-stop trips from Australia through Abu Dhabi to London, or the same single stop from Australia to New York. The globally central location of the Middle East — and the massive investment in aviation infrastructure that is occurring there — provide Etihad a solid foundation to achieve multiple



Photo courtesy of Airbus

Despite many serious challenges facing the airline industry during the last decade, Abu Dhabi-based Etihad Airways stands out as being one of the world’s most prominent airlines that continues to weather the storm.



Photos courtesy of Airbus

business goals, but those goals can only be reached through a bold determination to follow through.

Likewise, TAM Airlines in Brazil and LAN Airlines in Chile have constructed successful corporate experiences based on solid management and innovative leadership, sound financial underpinnings, a customer-centric model and a service promise that sees these carriers striving to deliver genuine, memorable value to each and every customer on every trip.

TAM, for example, has been the recipient of a steady pattern of lavish industry praise for superior delivery on its customer-service promise, which fits right in with the carrier's own internally developed mandates that the company refers to as "pillars of action": management excellence, technical-and-operational excellence and, quite logically, service excellence.

Having won a decades-long battle against national carrier Varig for Brazilian superiority (debt-riddled Varig was bought by low-cost Brazilian carrier GOL Linhas Aéreas Inteligentes a couple years ago), TAM now stands as South America's largest airline and has announced its intention to join the global Star Alliance (essentially replacing Varig, which was dropped from the Star Alliance in 2006).

And similarly to TAM, LAN has concentrated on setting a consistent standard of excellence, steadily building its brand among the South American countries in which it has sunk deep roots, and the airline effectively has extended its reach globally not only through its membership in **oneworld**, but also through codeshares with specific **oneworld** partners including American Airlines and British Airways.

LAN also maintains codeshares with other prominent carriers such as Alaska Airlines, AeroMéxico and Mexicana. And, not insignificantly, LAN has an ongoing codesharing relationship with TAM — once again illustrating that an incremental codeshare strategy, partnering with like-minded, highly reputable companies, can be hugely beneficial beyond its relatively minimal cost.

Both LAN and TAM have also established sound, realistic plans for a future in which a return to reasonable, incremental, measured growth is not simply hoped for ... it's inevitable.

But, first things first — and in an industry that had already significantly downsized its capacity to deal with fuel prices that appeared to be going nowhere but up, air carriers in general are now positioned much more favorably to be able to ride out the current economic maelstrom that threatens to devour other industries.

That doesn't excuse any carriers from the necessity to think creatively and act innovatively — always looking toward the best



South American carriers LAN and TAM have plowed through the industry's many obstacles with powerful leadership, a strong financial foundation, a true customer focus and a sound service promise.

ways to bring strategic logic to bear on every business decision, large and small.

"In strategy, we talk about 'blue-ocean' thinking, which is basically thinking outside the box," Ramaswamy said. "This is a business model that says you have to be creative in what you offer and how you offer it.

"And there are several questions we suggest companies should be asking," said Ramaswamy, who has conducted extensive studies of several carriers including Singapore Airlines. "One of those questions is, 'Where did we fail?' This revolves around the fact that we tend to take things for granted — meaning we tend to believe that the drivers that drive performance in an industry are static.

"We say, 'Industry has always done A, B and C — so in order to succeed today, I should also be doing A, B and C.' This is basically the 'herd' mentality. But the important question we should be asking ourselves is: Are we really testing the assumptions? Are we evaluating the perceived wisdom of the industry? Or are we just following for the sake of following?"

"Another question is: What can we do without? What can we do without that my industry takes for granted? And at the same time, you ask yourself: What are some additional factors we can add to the mix that others have not thought about?"

"Here's where Southwest [Airlines] and some of these other companies gained some key advantages in things like flight frequencies, offering people a low-cost fare with more flights and more choices in flying from Point A to Point B. That's what customers want: on-time arrival, and the service experience you can provide. And in that regard, always treat your customers with the utmost respect.

"Each of these elements is very critical."

During its three-and-a-half-plus decades of stellar performance, Southwest Airlines has, in fact, managed to create a business model that is universally admired not just within aviation circles but in the greater business community. What is now broadly recognized as "the Southwest Airlines model" is not just airline-focused, it's people-focused.

To be sure, the Southwest Airlines model is based on common sense — and that common sense, as well as ever-present good humor, has been easy to detect through Southwest Airlines' leadership from original boss and co-founder Herb Kelleher through current Southwest Airlines CEO Gary Kelly.

In between, Jim Parker occupied the Southwest Airlines CEO's chair, and Parker has since written a book entitled, *Do the Right Thing: How Dedicated Employees Create Loyal Customers and Large Profits*.

In a January 2008 interview with the *Fort Worth Star-Telegram*, Parker said, "It's so common these days for companies to say that people are their most important asset. But they don't really believe it, because they don't really

give their employees the chance to feel like they're part of something meaningful.

"That's something we always tried to do at Southwest [Airlines]," Parker said. "And the reality is that people who enjoy their work are going to do a better job than people who don't."

Parker went on to heap effusive praise on Southwest Airlines' "front-line" leadership.

"Most companies don't really realize that the most critical area of leadership is the front line," Parker said. "That's where a company most interacts with its own employees and the public.

"We always put a lot of focus on our front-line leaders and their understanding of their mission and role," he said. "You have to focus on the value of the individual — at every level — and make it part of your culture."

Perhaps, then, it would be most logical to conclude that the real key to success of the air carriers that usually seem to find it — carriers such as Southwest Airlines, WestJet, TAM, LAN and Etihad — is a culture of service, combined with a capability to see the value of every individual within the bigger picture.

And those individuals include both customers and employees, because every individual's experience is truly critical in a people-driven business such as the movement of travelers around the world — in a true sense of giving and receiving fair and genuine value.

"The bottom line should be a consequence of good business decisions you make — it should not be the driver of decisions," Ramaswamy said. "For Southwest [Airlines], it goes all the way back to Herb Kelleher, when he was running the company.

"And I'm paraphrasing, but he said something like, 'If I take care of my employees really well, the assumption is that the employees will take care of my customers well. Because I cannot be taking care of every customer myself, I'm relying on my employees to do that.'

"I think it makes a lot of sense. And it also illustrates the amount of effort that is required to make that work."

Obviously, several of the world's premier carriers are making it work. Among other things, it simply proves that working hard truly can be fun, and for these successful carriers, the fun is most evident at the bottom line.

Southwest Airlines has long been known for the self-effacing humor upon which it bases much of its advertising. The carrier is afraid neither of making fun of itself nor of its entire industry. And that says a lot about its greater corporate psyche.

It says, more pointedly, that Southwest Airlines is a carrier that's psychologically comfortable in its own corporate skin. And occasionally, the carrier may fail. Its fuel-hedging strategy, in fact, led to recent losses when fuel prices nosedived.

But in the longer run, Southwest Airlines, WestJet, TAM, LAN, Etihad and a handful of other carriers around the world know that they are on an exciting, innovative journey toward a future that holds the broad possibility of becoming even more successful. And that's the type of corporate confidence that can be observed as a lesson to many other companies — in multiple industries — as the future unfolds.

"A customer-centric business model means attention to detail — making the customer feel comfortable and going out of their way to help customers," Ramaswamy said. "And if you compare that with carriers that have not necessarily done well, most of them treat people like cattle.

"You will never see that happening with Southwest [Airlines]. Southwest [Airlines] and these other successful carriers are going through the same issues of security and loads and the delays — all of that — but still, they have a smile on their face. And they're able to make fun of themselves."

It's all reflected in the service promise, a promise that says the customer is entitled to reap the benefits of an appreciation and respect that only customer-centric businesses are willing to apply on the job every day.

"That's why I think carriers have to go back to the basics," Ramaswamy said. "They have to understand what kind of business model they've put in place and what the components of the business model are. They need to respect the customer's intelligence and treat the customer with respect.

"And you have to decide: What's your vision in terms of how you're going to be able to differentiate yourself in the marketplace? In many instances, people are selecting their airlines simply because they don't have a choice."

Yet when competition abounds, certain carriers consistently prevail. And those are the carriers with vision, with determination, with insightful and innovative leadership, and with employees who understand that the customer is their true boss.

These are the carriers that will be pacesetters long into the bright future of air transportation worldwide. ■

Phil Johnson can be contacted at wearelistening@sabre.com.