A MAGAZINE FOR AIRLINE EXECUTIVES
2006 Issue No. 1

ascend

Taking your airline to new heights

Focus on India

Seeking Gold

India's booming economy benefits airlines around the world

page 20

INSIDE

wearelistening@sabre.com

Low-Cost Carriers Gain Altitude

While low-cost carriers have left a considerable imprint on India's aviation industry in recent years, some debate whether or not more entrants will lead to consolidation in the long term.

By Steve Dumaine | *Ascend* Contributor

Fueled by rising disposable incomes and coupled with globalization and partial deregulation, the domestic aviation market in India is witnessing an unparalleled proliferation of new entrants, the majority of which are low-cost carriers.

Low-Cost Carrier Growth

India's aviation sector enjoyed a healthy 11 percent increase in domestic passengers from 2003 to 2004, which further grew to an exceptional 25 percent in 2005, coinciding with the launch of Air Deccan, India's first LCC. The impact of Air Deccan can be clearly seen on its Guwahati-Delhi route. After the carrier began serving the route in October 2004, the average daily passenger load increased from 162 to 215 while fares declined from an average of 6,000 rupees (US$135) to 4,000 rupees (US$90).

Domestic Air Passenger Growth in India 2002-2005

Year	Passengers (millions)	% change
2002-03	14.5	9.6
2003-04	16.0	10.9
2004-05	20.1	25.0

Low-cost carriers in India have gained a more prominent position in the past three years, fueling a significant increase in air travelers.

Source: Indian Ministry of Civil Aviation

The clear correlation in the demand and the price of air travel in India reenforces what has been observed in other sectors — that India is a price-sensitive market with huge sales potential at low prices. This especially bodes well for the growing ranks of India's low-fare airlines.

While the rise in gross domestic product and a changing urban lifestyle is leading to a higher propensity to travel, much of the growth of air passengers driven by the LCC segment is coming from the conversion of rail passengers (see related article on page 29).

"Approximately 20 percent to 25 percent of all our passengers are first-time flyers," said Gaurav Agarwal, head of marketing for Air Deccan. "We grow the market in part by lowering prices on established routes and getting the train customers to fly. In each of our

India's low-cost carriers, such as Kingfisher Airlines and Air Deccan, are growing their market share by winning business from the country's railway system. Approximately 20 percent to 25 percent of Air Deccan passengers are first-time flyers, many of whom have previously traveled via rail.

Photo by V. Ganesan/The Hindu

Photo by Dana Ward/Shutterstock

Photo by Dana Ward/Shutterstock

Photo by G. P. Sampath Kumar/The Hindu

Photo by Jan Kertzscher/PlanePictures.net flights, we get at least 40 to 50 passengers who get off the trains."

India has a significant indigenous travel market; the state-run railway network accommodates roughly 5 billion total passenger trips, of which approximately two billion are long-distance domestic trips, while the number of domestic air passengers is only 15 million. Every day, 800,000 passengers travel by first- and second-class air conditioned rail, compared to just 40,000 airline seats available. At the right price, some railway passengers, those traveling in the more elite classes, are likely to shift from rail to air travel.

"What we do is price between two spectrums," said Sanjay Kumar, general manager of sales and marketing for SpiceJet. "Our highest fare is around 20 percent to 40 percent lower than the normal economy fare of full-service airlines, and our lowest fare is close to the air conditioned fare on Indian Railways."

It is no surprise that the Ministry of Civil Aviation estimates air passenger numbers to grow to 59 million by 2010. Low-cost carriers, which will transport an expected 5 million passengers in 2005 and 2006, or approximately 20 percent of total domestic passengers, are also ramping up capacity to prepare for further growth based on fleet orders already placed with aircraft manufacturers. The market share of low-cost carriers is likely to approach 30 percent by next year.

Business Models

In India, similar to other regions of the world, LCCs with a mix of business models are emerging. Air Deccan, for instance, approaches the market as an add-on retailer.

"We make no efforts to lure high-end passengers; our target is the smart traveler who values his money," said Air Deccan's chief executive officer and founding managing director, Capt. G R Gopinath, in a recent issue of *Express Travel and Tourism*.

How does the carrier do it? It offers some of the lowest cost alternatives on key routes.

In October, Air Deccan launched an in-flight shopping scheme called "Brand for Less" with AVA Merchandising, part of the Indian arm of the global merchandising group Envision Merchandising.

"This will also help us get incremental revenue, which will help us reduce fares further," said Capt. Gopinath.

Other new startups are incorporating a pure-play strategy by focusing on their air product with low fares and low costs. SpiceJet's stated goal is to be "a low-fare, no-frills airline that aims to make air travel accessible to everyone."

"We are looking at purely a low-cost model," Kumar said.

Likewise, GoAir expresses its desire to be "commoditizing air travel" and promises "a quality-consistent, quality-assured and time-efficient product through affordable fares."

Recent trends focus on development of more hybrid business models in India. Paramount, for example, represents an upscale pure-play business model and aspires "to provide world-class designer products and unparalleled comfort, giving true value for money."

The airline targets the business travel market and offers premium-class services on its flights but not economy class.

Kingfisher Airlines, on the other hand, has adopted many characteristics of traditional full-service carriers. The carrier's motto says it all, "The Kingfisher class experience aims to take air travel beyond just getting from here to there." This includes seatback in-

Low-Cost Carrier Business Models

A global study of low-cost carriers by Sabre Airline Solutions *identified five predominant business models, which represent a continuum. There are many carriers that use a hybrid of these models, but they generally represent the unique strategies observed in the industry.*

Business model	Description	Global prototype	Indian example
Add-on retailers	Demonstrate a singular focus on managing costs and being the lowest-cost player in the markets they serve. Offer a highly basic product and rely on very aggressive low fares to stimulate demand. Rather than targeting a specific customer segment, these carriers seek to attract a broad base of customers through low fares. Developing ancillary revenues (on-board sales, fees for baggage) are critical for building profitability and further subsidizing even lower fares.	Ryanair	Air Deccan
Pure plays	Build brand based on an "every-day low-price" concept and offer a basic product. Utilize low fares to stimulate new demand, but profitability is driven predominantly by air travel as opposed to ancillary revenues.	Southwest	SpiceJet GoAir
Upscale pure plays	Maintain cost-conscious approach but provide a more sophisticated product that often includes frills such as larger seats, in-flight entertainment and business-class seating. Brand is based on customer experience, while pricing reflects value versus other similar product offerings in the marketplace.	jetBlue	Paramount
Transitional	Represent a hybrid between low-cost carriers and traditional carriers. Make tradeoffs involving complexity of their business model and costs such as developing a network route structure rather than point to point and forming alliances with other carriers through codesharing or interlining.	Gol	Kingfisher Airlines
Charter hybrid	Charter operations represent a majority of their business. However, these carriers also sell scheduled seats on charter flights to augment their business with higher-yield passengers. Many exist in Europe and came about as a reaction to the consumer travel trends and LCC competition.	Air Berlin	

Despite uncontrollable costs such as jet fuel and landing fees, the Centre for Asia Pacific Aviation estimates that low-cost airlines in India can lower costs significantly more than traditional carriers by following a simplified business model.

Photo courtesy of The Boeing Company

Photo courtesy of GoAir

Photo courtesy of Embraer

Photo courtesy of Airbus

flight entertainment, extra-wide seating, pre-assigned seats and meal service. In addition, Kingfisher Airlines confirmed orders for 20 ATR 72-500 turboprops, which Nigel Harwood, Kingfisher's chief operating officer, describes as "feeder aircraft" for the carrier's Airbus routes. This clearly implies a network route structure as Kingfisher Airlines grows.

Similar to their global brethren, Indian LCCs have embraced long-held marketing strategies: price competition and differentiation. Although business models in India may be closely related to their global counterparts, Indian LCCs have uniquely adapted themselves to their market. Some aviation leaders in India dispute that the country's LCCs really have a cost advantage.

"With two-thirds of your fixed costs that you can't touch — be it fuel, navigation charges, landing fees, pilots' salaries — it doesn't make sense to me," said Naresh Goyal, chairman and founder of Jet Airways in a recent *Airline Business* article.

However, LCCs still are able to achieve numerous benefits due to their busines model. Kapil Kaul from the Centre for Asia Pacific Aviation estimates that Indian LCCs can reduce their costs by 15 percent to 20 percent versus legacy carriers by adhering to a simplified business model. SpiceJet's Kumar is even more optimistic.

"What is controllable with us? Staff utilization, distribution costs, operational issues, high density [route] and [aircraft] utilization benefits, and manpower capabilities such as multi-tasking," he said. "With that kind of structure in place, you could probably realistically achieve cost differentiation of 20 percent to 40 percent versus a full-service airline such as Jet Airways or Indian Airlines."

To contain costs, Air Deccan doesn't even provide free newspapers because it would require more time for attendants to clean the aircraft between flights.

LCCs in India are also highly innovative in managing their sales and distribution channels. Like other developing economies, Internet and credit card penetration is characteristically low. However, rather than relying largely on traditional distribution channels, LCCs have developed new sales channels to reach the broadest possible customer base. In March 2005, Air Deccan entered a partnership with Hindustan Petroleum Corp. Ltd., a petroleum refiner and retailer with 4,400 retail outlets, which enables the carrier to sell tickets through HPCL's gas stations. In addition, Air Deccan has recently implemented technology giving its customers the ability to book flights via mobile phones using NGPay's mobile payment platform.

The future appears bright for LCCs in India. Yet, while air travel is expected to grow by more than 20 percent a year in the coming years, many believe that India, like the more mature LCC regions in the world, will eventually see more consolidation. Kaul predicts that by 2010, there will be just three large LCCs in India, with another three or four smaller regional players.

Steve Dumaine is a senior principal in airline strategy and planning for the Sabre Holdings™ *business. He can be contacted at steve.dumaine@sabre.com.*

Expected Low-Cost Carrier Fleet Growth in India

Airline	Start date	Expected fleet size	Time frame
Air Deccan	August 2003	75	2010
Kingfisher Airlines	May 2005	65	2010
SpiceJet	May 2005	20	2008
Paramount	October 2005	10	2010
GoAir	November 2005	36	2009
Magicair	Announced	20	2008
East-West	Announced	40	2010
IndiGo	Announced	100	2012
Indus	Announced	10	2007
Air One	Announced	—	—
Total		**376**	

The liberalization of the Indian air transport market has created opportunities for new airlines, many of which have adopted a low-carrier operating model and have announced aggressive fleet-growth plans. If the airlines carry through on their announced plans, almost 400 additional aircraft will be filling the skies over India.

Source: Center for Asia Pacific Aviation
(Data does not factor in some carriers that have plans to fly but have not announced fleet details.)