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Taking your airline to new heights



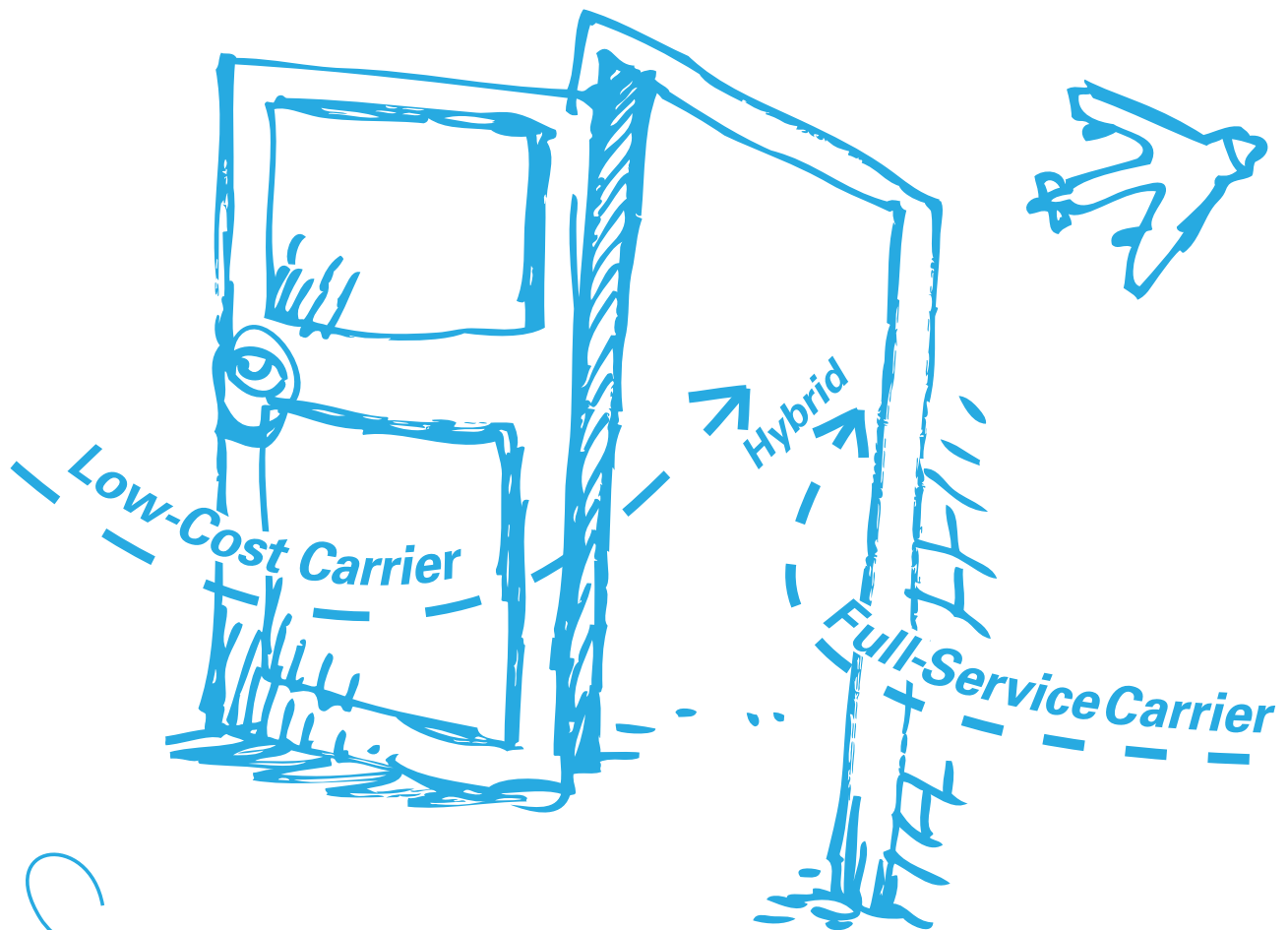
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Simplify the evolution

As pure low-cost carriers evolve to a hybrid model, their key concern is how to add sophistication to their model without adding complexity and cost to the business, i.e. how to implement more sophisticated solutions that are able to increase revenue without adding processes and infrastructure to the business that would increase their cost base. To that aim, the airline evolution needs to be supported by future-ready technology that is flexible enough to enable the right and necessary new business processes.

■ By Alessandro Ciancimino | *Ascend* Contributor

Low-cost carriers have grown at a tremendous pace during recent years, and some of them have enjoyed healthy financial performance relative to the industry average. This success was originally and primarily due to the exploitation of latent demand for low-cost travel.

LCCs' success is based on a steady profitable revenue growth that ensures a continuous growth of their share value. If at any time the growth is clouded by events such as an unexpected decrease in load factor, then immediately the financial community issues a profit warning.

Originally, about 75 percent of LCC passengers were due to stimulation of new traffic — passengers that did not previously consider flying as a travel option. It is clear though that such stimulation cannot continue indefinitely and that LCCs, to keep filling planes, have to find alternatives to fuel the growth.

Beyond an inorganic growth, which has not been seen much among LCCs so far, what is prevalent in the industry are basically two macro-options by which LCCs can sustain a continuous organic growth: expanding in terms of the geographical footprint covered by the airline or increasing the customer base — addressing different customer segments rather than just the pure leisure one.

Both options deviate from the pure original LCC business model. In fact, to grow the geographical footprint, LCCs must increase the average stage length of their network, which means flying longer routes that they did not initially or intentionally choose.

Longer average flight times translate into less-competitive advantage in terms of aircraft utilization against the incumbent traditional carriers as well as not being able to “flood” such markets with many daily frequencies as LCCs typically do when they serve particular markets.

Ryanair is a prime example of a low-cost carrier that pursues this avenue to sustain growth, and, recently, the airline started serving markets that require nearly a four-hour block-time sector that originally did not fit into its business model. This means, of course, increasing the cost base and, hence, having less competitive advantage versus the incumbents. There are actually a few LCCs that are successfully pursuing this option beyond Ryanair, such as AirAsia and Wizz Air.

On the flipside, other LCCs, such as Air Berlin, easyJet, JetBlue Airways, Norwegian Air Shuttle, Vueling Airlines and WestJet Airlines, are achieving growth by increasing their customer base. This requires them to obtain new passengers in addition to those achieved through stimulation by cheap travel. In doing so, they must have an advantage, aside from low fares, over the competition, which presents a new challenge for LCCs.

Until a couple of years ago, LCC direct competition was based on less than 10 percent of capacity because these carriers were able to avoid, for the most part, competition within the



Straying from the original low-fare business model, AirAsia and Wizz Air, as well as low-cost carrier Ryanair, have increased the average stage length of their network – flying longer routes that weren't part of the initial plan – to successfully grow their geographical footprint and sustain growth.

low-cost sector. But now that further growing opportunities in potential LCC “virgin” markets are drying up, these carriers are beginning to compete for market share.

At the same time, winning passengers from traditional, full-service airlines is not easy because they are fighting back by attacking their cost base and trying to emulate, with different levels of success, some features of the LCC business model such as unbundling products and boosting revenue through ancillary sales.

This strategy is based on successfully winning traffic from the incumbents, which, even if it seems strange, was not originally the foundation of the LCC strategy and success.

In either case, the ultimate goal is to increase the available number of revenue sources (through ancillary services obtained by intelligently unbundling products) or the revenue-generation capability (through innovative revenue management coupled with customer-centric functionality)

while at the same time keeping the cost basis under tight control.

Many LCCs and hybrid carriers keep reminding that, first and foremost, they need to keep or even strengthen their cost-basis advantage (“cost is king”) and then focus on revenue improvement.

However, in many instances, the LCC cost base has already “scratched the bottom of the barrel” or, in other instances, some LCCs, due to their smaller size compared to others, cannot achieve the same cost basis due to different economies of scale that can be realistically achieved. So while keeping the cost basis to a minimum is necessary for success, it is not sufficient. In addition to maintaining the low-cost structure, these carriers must also focus on revenue generation.

When two LCCs with a similar cost basis, which cannot be substantially improved further, compete in the same markets, long-term

success will be awarded to the carrier that is able to:

- Offer a more-lucrative product to the customer,
- Better distribute the product through multiple channels,
- Better revenue manage the market,
- Offer the right product to the right customer,
- Codeshare where appropriate to offer a wider network reach without investments,
- Provide more-effective customer care that ultimately translates into a better customer experience and improved loyalty.

To a certain extent, LCCs will have to focus more prominently on actions and imperatives that are well known by the incumbents: finding new sources and diversification of revenue, developing new business processes around pricing and revenue management as well as customer care and, of course, keeping tight control on costs, all of which ultimately translates into using traditional paradigms in a non-traditional and innovative way.

At first sight, these initiatives may appear to be a mission impossible, but they are not. Provided that airlines approach the hybridization (or sophistication) process continuously, with a sound strategy in place, it's all well within reach.

Offering a more sophisticated product means redesigning some business processes and implementing technology that will support them. Key challenges include:

- Avoiding any "over" redesign, re-engineering only the processes that would deliver a quick and substantial ROI where the investment is minimal or nonexistent,
- Continually changing processes upon changing market/competition conditions,
- Implementing robust, flexible technology that can easily adapt to changing conditions well into the future with little or no incremental costs.

To achieve this, airlines must apply a customer sales and service approach that includes forward-thinking technology built around the capability of an airline to shape its business model according to its own tailored strategy. Important technology elements include open architecture as well as adaptive capabilities. Any solution should offer a futuristic design that will accept relatively easy customization and changes as the strategy and the business model of the airline evolves, even in a way completely unthinkable at present. To that aim, having a solution that can be easily modified through the implementation of natural language-based business rules without having to revert each time to the technology provider is definitely the way forward.

This also means service-oriented architecture must isolate individual capabilities of an application so they can be used in multiple ways and combined with other services to create new functionality deployed across a service bus that facilitates easier integration and



Some low-cost carriers, such as Air Berlin, easyJet and Norwegian Air Shuttle, are increasing their customer base to achieve growth. To do so successfully, these carriers must have an advantage that transcends low fares and sets them apart from their competition.

communication among different applications of different providers.

In line with the conventional LCC strategy to outsource non-core operations, solutions need to be provided on a Software as a Service (SaaS) basis as the most effective/least expensive method to source solutions.

Keep in mind the demand of new technology has to be driven by changing business processes requiring new enablers, and not vice versa. Additional key success factors include:

- Evolving processes around a carrier's own strategy,
- Redesigning processes in a manner that minimizes or avoids additional resources/infrastructure,
- Outsourcing initial business process re-engineering activities at the time the new solution is implemented to the solution provider since this typically delivers the most effective outcome at the lowest cost,
- Investigating the possibility to partner with the solution provider on an ongoing basis to outsource the performance of some recurring business processes (e.g. maintenance of the business rules) to avoid adding resources and infrastructure in house when this proves to be economically ineffective.

The sophistication of the pure LCC model is likely unavoidable and highly recommended. The key to success for a low-cost airline is to tailor the sophistication around its own strategy, redesign some business processes accordingly and source technology solutions that support the new processes in the most effective, efficient way. This indicates that solutions providers will have to play an even more central role in the industry since they will support airlines not just from a pure technology standpoint but also, and maybe primarily, from a business advisory and business support perspective.

To that aim, a true partnership between airlines and solutions providers is clearly the most successful way forward. **F**

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