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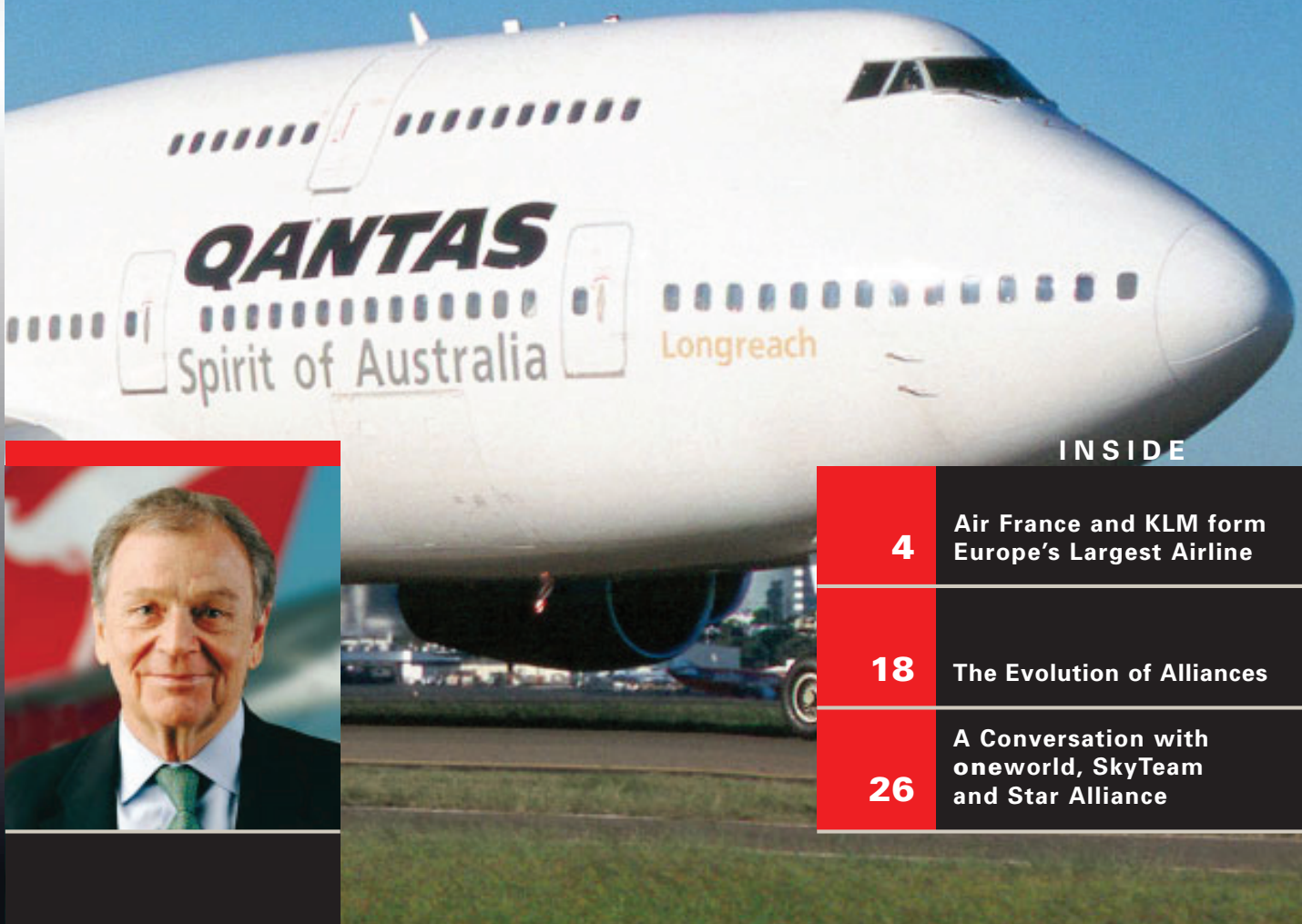
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Taking your airline to new heights

AN ALLIED FRONT

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and Star Alliance



The French –

Photo courtesy of KLM





Dutch Connection

Through their merger, Air France and KLM have formed one of the world's largest airlines, potentially taking the first step in reshaping the airline industry.

■ By Christian Gossel | *Ascend* Contributor

Does Sept. 30, 2003, mark the beginning of a new era in the airline industry?

Air France and KLM Royal Dutch Airlines believe it just might.

On the date the two airlines announced they would merge into a single entity, forming Europe's largest airline and the world's third largest in terms of passengers carried, officials hailed the agreement as the first step in a needed industry consolidation.

"We have always been convinced of the necessity of consolidation in the airline industry," said Jean-Cyril Spinetta, chairman and chief executive officer of Air France as well as the combined organization. "Today, we announce a combination with KLM that will create the first European airline group, which is a milestone in our industry. This will bring significant benefits to customers, shareholders and employees. Capitalizing on the two brands and on the complementary strengths of both companies, we should, within SkyTeam, be able to capture enhanced growth opportunities."

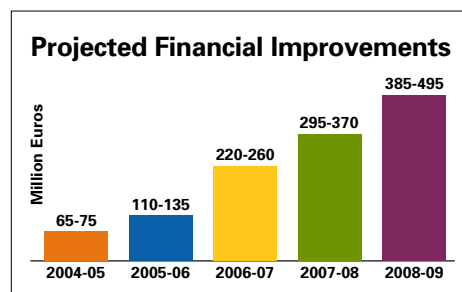
The combined group will become the world's largest airline in terms of revenue, with estimated annual turnover of 19.2 billion a year (US\$23.4 billion). The group will also serve 226 destinations worldwide with a fleet of about 540 aircraft and employ about 106,000. And it will be the world's largest non-consolidator cargo airline in terms of revenue ton kilometers.

By launching the first cross-border airline merger in Europe, the two carriers may have paved the way for other airlines to follow suit, bringing to a close the days when every

country had its own flag carrier. Such a fragmented industry, with multiple airlines competing for the same markets more as a matter of national pride than as a rational business approach, is "an inheritance from a former era," the two airlines said in announcing their merger.

"The need for structural changes and consolidation in Europe is widely accepted, but has not yet commenced as a consequence of regulatory and political constraints," the airlines said in a statement. "The [merger] is the first significant move in this context and will create a leading airline group in Europe."

The airlines said a changing regulatory framework, with the European Commission given the authority to negotiate open skies agreements on behalf of all European Union countries, has opened the door for a consolidation of the continent's airlines. Experts also



Consolidation between Air France and KLM is projected to improve the group's combined operating income by 385 million to 495 million (US\$603 million to US\$469 million) by 2009.

"We have always been convinced of the necessity of consolidation in the airline industry. ... This will bring significant benefits to customers, shareholders and employees."

believe a consolidation would benefit other regions, particularly in North America, where competition among several major carriers has resulted in excess capacity and, therefore, a lack of pricing power.

The two airlines made for logical partners. Their route networks overlapped minimally. Air France, with its strong network in southern Europe, fit nicely with KLM, which is strong in northern and northeastern Europe. Together, the airlines will be able to expand their positions in central and eastern Europe. The two airlines also have strong, complementary hub operations at Paris Charles de Gaulle and Amsterdam Schiphol, two efficient operations with room for additional development.

The two airlines, which officially combined June 1 following approvals from European and U.S. regulators, will maintain their separate identities under a single holding company, Air France-KLM. Although the individual airlines will still operate under their current brands, they will be more closely integrated than airlines in one of the global alliances.

"If commercial alliances have contributed over the past years to initiate the first

Air France-KLM Synergies

Main actions		Financial improvement (million Euros)	
		Year 3	Year 5
Sales/distribution	Harmonizing sales policies Coordinating sales forces Reducing sales, catering and ground handling costs	40	100
Network Revenue management Fleet	Optimizing networks and schedules Harmonizing revenue management Optimizing fleet management Coordinating management	95-130	130-195
Cargo	Optimizing networks Coordinating sales policies Sales cooperation	35	35
Maintenance	Purchasing Insourcing of subcontracted work Pooling of spares	25	60-65
IT systems	Gradual converging of IT systems	20	50-70
Other	Joint purchasing	5-10	10-30
TOTAL		220-260	385-495

By leveraging synergies such as shared maintenance operations, combined sales and marketing strategies, joint purchasing, and cooperative cargo operations, the Air France-KLM group expects significant financial improvements during the next five years.

steps toward consolidation, deeper cooperation is now needed to generate significant and sustainable synergies," according to the airlines' statement.

Indeed, Air France and KLM expect their new organization to have a positive impact on the consolidated operating income of at least 385 million to 495 million (US\$469 million to US\$603 million) by the fifth year of the group's joint operations. Airline officials have said 60 percent of the financial benefits will be derived from cost savings, the rest from additional revenue. The combined group will offer three core businesses: passenger transport, cargo and maintenance.

“Through this innovative partnership with Air France and our participation in the SkyTeam alliance, we are confident that we have secured a sustainable future for our company.”

Officials expect the financial impact to result from synergies in several areas:

- Sales and distribution — The combined organization has an improved global presence and will also be able to offer passengers a wider range of products. The group will cut costs by coordinating the sales structures of the two component airlines.
- Network, revenue management and fleet — By codesharing, harmonizing the flight schedule and optimizing revenue management policies, the two airlines offer more destinations and a larger number of more convenient connections for passengers.
- Cargo — Through a more extensive network, combined with coordinated freighter planning, the merged airline can improve its product offering, resulting in a revenue increase. The group can also reduce costs through a more efficient handling of its cargo hubs.
- Maintenance and engineering — The group will jointly purchase spare parts as well as create centers of excellence in engineering and optimize the use of existing M&E platforms. The group will also coordinate production schedules and combine facilities.
- Information technology — Converging the IT applications used by the individual partners will reduce costs.
- Other — The group will optimize and

Photo courtesy of KLM



On May 5, Air France Chairman and CEO Jean-Cyril Spinetta (center left) and KLM President and Chief Executive Officer Leo van Wijk (center right) celebrate the consolidation of the two airlines during a press conference at the Paris-Charles de Gaulle Airport.



Photo courtesy of KLM

Deemed the world's largest carrier in terms of revenue, with estimated annual returns of 19.2 billion (US\$23.4 billion), industry giant Air France-KLM, operates a combined fleet of about 540 aircraft, serving 226 destinations around the world.

THE HIGH • LEVEL view

News Briefs from Around the Globe

Who

Aerolineas Argentinas, ATA Airlines, Frontier, Aeroflot and Jet Airways

What

Implemented Customer Insight and Customer Data Delivery capabilities to enhance service levels and retain passenger loyalty. Features of the *SabreSonic™ Passenger Solutions*, the new-generation technology is designed to help

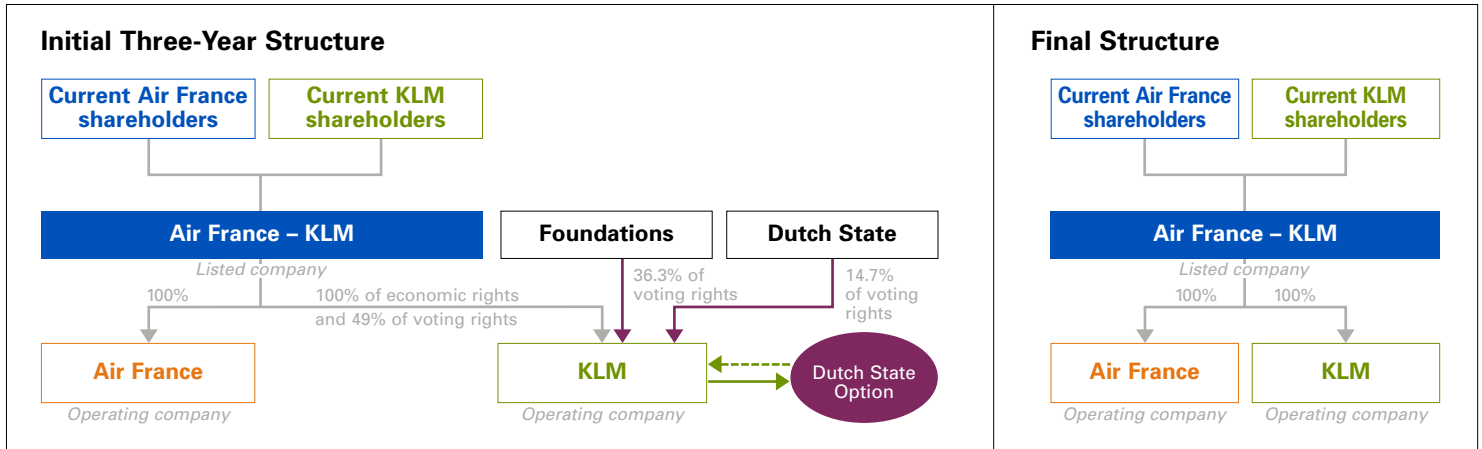
airlines personalize service for their individual passengers and provide real-time marketing opportunities.

Why

“With Customer Insight, all of our call center personnel now have access to the Aerolineas PLUS frequent flyer information,” said Claudia Toldeo, call center manager for Aerolineas Argentinas. “The call center personnel have all the

information needed to make a reservation, provide account balances, exchange points for tickets and issue tickets, all without having to transfer the customer to another area.”

Sean Menke, Frontier’s senior vice president of marketing said, “One of the key reasons we chose the *SabreSonic* solutions over other competitors was for the ability it will give us to distinguish ourselves through service.” [E](#)



During the first three years as a cooperative airline, the Air France-KLM group will perform under a strategic operating structure outlined by Air France general shareholders. After the initial three years, the operating structure will be further refined to meet the needs of the merged airline.

harmonize other activities such as simulator utilization, joint purchasing of goods and jointly negotiating with vendors such as caterers and ground handlers, delivering additional cost savings.

The combined group also offers several customer benefits, including an expanded network, access to shared airport lounges, competitive fares and enhanced onboard service. The merged airline may also grow further. It has already held discussions about adding Italian flag carrier Alitalia.

Leo van Wijk, president and chief executive officer of KLM and vice chairman of AirFrance-KLM, said the merger was instrumental for the future success of the Dutch airline.

“KLM has been pointing out the need for consolidation in light of the challenges facing our industry, and we have not made it a secret we were looking for a strong European partner,” van Wijk said. “Through this innovative partnership with Air France and our participation in the SkyTeam alliance, we are confident that we have secured a sustainable future for our company. Our valuable Schiphol hub will be an integral part of the dual-hub strategy of the new airline group, allowing us to build on what KLM and its staff have achieved over nearly 85 years.”

The merger also has implications for the SkyTeam alliance — which previously included founding member Air France along with

Aeroméxico, Alitalia, CSA Czech Airlines, Delta Air Lines and Korean Air. With its merger with Air France, KLM became a member of SkyTeam, which also added KLM’s long-time partner Northwest, and Continental, which had a relationship with Northwest.

The impact of the Air France-KLM merger has just begun, but the ripple effect could hold the promise of creating waves of change for the airline industry. **E**

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THE HIGH • LEVEL view

News Briefs from Around the Globe

Who

China Eastern Airlines

What

Based on recommendations made by Sabre Airline Solutions Consulting, the airline will open a centralized system operations control center in Shanghai, China, to consolidate its movement control, flight dispatch, load planning, crew coordination and

scheduling functions. As part of the two-year agreement, an SOC expert from Sabre Airline Solutions will be assigned to China Eastern Airlines for the duration of the agreement to ensure the new facility is optimally implemented and functioning.

Why

“We are confident we will see excellent results by implementing

the recommendations made by our valued Sabre Airline Solutions partners,” said Yu-Lin Wu, vice president for China Eastern Airlines. “We expect that the new efficiencies we will achieve through the operations control consolidation will heighten our performance in this highly competitive marketplace.” **E**