The lethal cocktail of a global recession, higher oil prices, and a drop in demand for expensive seats has hit the airline industry hard. Budget carriers aside, airline companies traditionally made the most of their money from business and first class passengers and commercial cargo. Recently, air freight volumes have declined, and the industry has been rocked by corporate cutbacks and a decline in consumer spending. This has prompted many to question how certain airlines will survive.

Premium travel (first and business class) has borne the brunt of the recessionary impact. Premium passenger numbers have plummeted during the last year by about 20%, which led to a drop in revenue of 30% since the beginning of 2009. This fall is a crucial contributor to the 30% overall decline in industry revenue which led to a drop in revenue of 35-40% since the beginning of 2009. This has prompted many to question how certain airlines will survive.

The rising economic ‘tide’ has lifted all the ‘boats’ but now that the tide has gone out, the heavier, more bloated vessels remain stuck in the silt. In the air transport sector, these companies are typically ‘flag carriers’ or ‘legacy airlines’. These tend to be former or current state-owned airlines, often burdened by accumulated cost obligations and long-standing societal commitments. Unlike their leaner and more agile low-fare or budget airline competitors, these companies have largely failed to get control of their costs.

The world we now live in means that for those who can no longer rely on state support – and even for many of those who still can – cost management and the strategic allocation of resources is a must.

As legendary airline boss and SouthWest Airlines founder, Herb Kelleher, commented: “If the Wright brothers were alive today, Wilbur would have to fire Orville to reduce costs”. By contrast, budget airlines are founded on the principle of streamlining costs so as to maintain above industry norms.

Six steps to successful airline turnaround

Our research and that of other common observations which formed the basis of revising the performance of mature legacy carrier airlines.

1. Maximize profits

A focus on profit maximisation is the foundation of turnaround. This may seem like a simplistic conclusion and it has often been rather neglected by legacy carriers in favour of political and social concerns. The airlines we considered did not act like ‘flag carriers’. ‘Flag carriers’ typically behave as unofficial representatives of their home countries and maintain loss-making routes for the sake of their prestige.

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2. Turnaround

With the world’s airlines suffering from high fixed costs and the reliance of legacy carriers on price neutral premium traffic, the turnaround process has become crucial. This has prompted many to question how certain airlines will survive.

3. Legacy carriers

Legacy carriers everywhere have to wake up to the new reality. Many still refuse to do so or are hampered by governmental or military demands that are divorced from commercial reality (as is the case in many developing countries). However, some companies faced up to reality several years ago. These success stories provide some indication of how mature airlines can remain competitive and forge their own strategic pathways in this era of budget airline dominance.

4. Nimble, ultra-lean business models

The nimble, ultra-lean business models of the lowest cost competitors often make the legacy carriers look cumbersome, old-fashioned and financially unappealing. This raises legitimate questions: is there a future for the mature legacy carrier in an industry which is undergoing rapid change; and where further consolidation is predicted by some as the only way mature airlines can hope to survive? Can the legacy carrier survive by organic growth alone? If so, what strategy can they adopt, not only to survive, but to once again be forerunners in a very crowded market?

To answer these questions, we conducted a research project to identify and analyse mature airlines that have moved from disappointing financial performance to consistent growth and, in doing so, have managed to remain powerful competitive forces in liberalised markets. We examined five prominent airline turnarounds that occurred prior to the current recession. The airlines were Aeroflot (Russia), Air Canada, All Nippon Airways (Japan), LAN Airlines (Chile) and TAM Airlines (Brazil). We also drew insights from the successful strategies of Thai Airways International and Turkish Airlines. All of the turnaround airlines we looked at had engaged in simplifying their businesses by reducing costs as much as possible across the entire cost structure of the airline. This appears to have been a universal approach in response to high oil prices and increased industry rivalry from low-fare airlines. However, none of the airlines studied had chosen to reposition themselves as a low-fare carrier. All five continue to operate as full service airlines known primarily for quality service over bargain basement pricing.

5. Organisational culture

The unstoppable growth and expansion of budget airlines across the globe leads many observers to ponder the future of legacy carriers.

Bonairi’s CEO, Willie Walsh, has already made his decision. He sees a structural shift in the industry away from high fixed costs and the reliance of legacy carriers on price neutral premium traffic. He faced these same challenges when boss of Irish carrier Aer Lingus, and oversaw its transition from a state-owned, high service cost-maker to a publicly listed, lower cost and occasionally profitable company. The challenge this time around is much greater given BA’s size and status and it often militates against senior management interests. Legacy carriers everywhere have to wake up to the new reality. Many still refuse to do so or are hampered by governmental or military demands that are divorced from commercial reality (as is the case in many developing countries). However, some companies faced up to reality several years ago. These success stories provide some indication of how mature airlines can remain competitive and forge their own strategic pathways in this era of budget airline dominance.

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6. Business strategy

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The airlines we studied were motivated by generating as much profit as possible. This involves aggressive cost-cutting exercises (referred to by some of the airlines as ‘simplifying the business’), revenue-maximising initiatives and strategic investment in IT.

2. Quality of service
Quality of service should not be compromised. All of the turnaround airlines in our study were committed to high service standards and placed reliability and quality as central to their brand’s identity. Although cost-cutting has taken place at all of these airlines, this has not usually directly affected the level of service offered to customers. The cost-cutting is limited to ‘behind the scenes’ activities not directly facing the customer. Indeed, rather than cutting back on service, the airlines studied are constantly trying to raise their standards through innovation and greater customer focus. Clearly, morphing into a budget carrier has not been the preferred turnaround strategy.

3. New leadership
New leadership plays a key role in achieving successful turnaround. In the study, all the airline improvements were shaped by strong and effective leadership. For four out of five of the cases, new leadership was brought in to turn around the whole organisation. This impacted the airline in respect of both technical and cultural aspects of the business. For the other turnaround airline (LAN), focused and innovative leadership helped define its success.

Most of the airlines’ leadership teams have adopted clear vision statements that help define and embed their strategic objectives across the company. Excellent communication and people skills were evident in the leadership teams of the airlines studied. This is not ‘ivory tower’ leadership conducted from a distance and in a very hierarchical fashion, as has often been the case at legacy airlines.

4. Alliance network
Membership of an alliance network acts as a turnaround catalyst. Four out of the five airlines studied were members of one of the three big global alliances and spoke of membership in very positive terms. Membership of an alliance has the potential to assist turnaround by cutting costs through economies of scale generated by the alliance’s purchasing power and the sharing of good practices and information technology. It also enhances the customer value proposition by providing increased routes and global service and boosting the reputation of member airlines’ brands through association. It should be noted of course that joining an alliance is not a guarantee of business success.

5. Regional consolidation
Regional consolidation can contribute to turnaround. Two of the airlines studied (LAN and Aeroflot) claimed that regional consolidation was a key aspect of their strategy - overwhelmingly so in the case of LAN. New markets can be served and therefore new revenues generated by pursuing liberalisation of the regional industry and moving into lucrative but poorly served territories.

6. Staff training and communications
Investment in staff development and management-employee relations underpins turnaround. All of the turnaround airlines studied invested in improving relations with their staff and in providing comprehensive training for employees in technical skills, customer service and change management, especially revised corporate culture and strategic aims. Several have dedicated training academies, exclusively devoted to training and staff development. Excellent communication between airline management and staff during times of strategic change within the airline characterised the turnaround airlines.

Together, these six observations provide a powerful set of principles and practices that can be weaved together into a successful turnaround strategy. With or without the recession, air transport competition is intense across the world and legacy carriers have struggled to adapt to cost pressures, increased customer expectations and new competitor threats. Some have successfully managed this transition, providing a ray of hope for legacy airline managers everywhere and illustrates how not only to keep pace with but move ahead of budget airlines and other new entrants in the struggle for passengers, markets and profits.

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