WHEN THREE BECOME ONE

Airline mergers and acquisitions continue to gain momentum, with the BA-AA-Iberia tie-up among the latest, but what does it mean for fares and competition? We speak to three experts…

THE INDUSTRY EXPERT

Peter Dunkin, aviation advisor

There are few industries more challenging than civil aviation. Fierce competition, overcapacity, low yields, volatile fuel prices and susceptibility to external events such as terrorism, ash and snow are all among the obstacles to success.

The situation is not helped by some airlines growing too quickly, seduced by the vanity of volume, ahead of the sanity of profitability. This has forced the need for consolidation.

In reality, the immediate drivers behind consolidation have been about survival, cutting costs and shareholder value. According to IATA, the industry lost over $50billion in the last decade with over 100 airlines going bust in Europe alone.

Since the Air France/KLM tie up in 2004, five mega airline groups have formed as a result of consolidation. British Airways has found its long-awaited partner Iberia in the latest merger.

As a result, the oneworld alliance has edged closer in size to the SkyTeam and Star alliances. But the fact that the largest group has over 1,000 aircraft and carries 144 million passengers a year is of little consequence to the corporate traveller.

The move towards a potential oligopoly of five major airline groups is perhaps not what aviation regulators and politicians had in mind.

Is this integration good for corporate customers? If it leads to a more stable industry there will be less disruption to operations due to airline failure. Improved margins will allow further investment in the latest aircraft, products and services. Other benefits can include more convenient choice of flights and departures, and more opportunities to ‘earn and burn’ with frequent flyer schemes.

Corporate negotiations are potentially simpler with fewer suppliers involved. However, the supplier may have more leverage on contracts. While airlines need to increase their prices, there is still enough competition to contain fare levels. Despite claims by airlines, integration will not always lead to more choice of flights. A key attraction of consolidation is surely to reduce duplication and over-capacity.

Other benefits to the airlines include cost savings through economies of scale and buying leverage. Schedules and systems can be harmonised and load factors improved, and duplicated roles can be removed or reduced.

There will always be uncertainty for airline employees over job security during the often lengthy merger and alliance process, and keeping them happy and motivated is key to the customer experience. Ensuring good employee relations will be crucial for British Airways and Iberia, who both have a history of industrial disputes.

BA are confident of achieving £344million savings by year five, improving profitability, and continuing to invest in their product. Access to Iberia’s South American network has been promoted as another benefit of the alliance. Most UK customers would prefer to fly non-stop to South American points rather than via Madrid. However, there will be demand where there are no direct services or a price advantage.

The joint venture and revenue sharing agreement with American Airlines is also a significant move forward for BA, considering the importance of the transatlantic market. BA has more airline acquisitions in their sights. Watch this space!

Airlines work miracles every day by operating safe and punctual services. Those who will prosper are the ones who genuinely put their customers and employees at the centre of everything they do. The profits and longer-term shareholder value will then follow.

THE TMC

Adrian Woodward, director of group supplier and industry relations, HRG

Faced by rising oil prices in recent years, and then a ruthless global recession, there's no denying that airlines have experienced some very challenging circumstances.

It is no great surprise that, against such a backdrop, airlines have fought for revenue, reduced costs and created new income streams as they seek to position themselves for success in an increasingly competitive environment.

Acquisitions and mergers, together with initiatives to maximise ancillary revenues, are all ways in which the airline industry hopes to re-shape and re-size in order to meet the changing conditions.

First up were the airline alliances: oneworld, SkyTeam and Star Alliance. Membership alliances have allowed access to a wider market, synergies in network, product – including loyalty programmes – and support services. Airlines need networks to be as big as possible to benefit economically and meet consumer demand, and for this they need foreign partners.

But – and this is where the problems lie – ownership restrictions do not generally allow for cross-country mergers or takeovers, although this is now starting to change. This is where alliances come in as they provide a way to get around everything from bilateral agreements to licensing and control regulations. Carriers envisage the great blue sky of global free trade in aviation.

To realise greater cost and revenue synergies, the next logical step for airlines is to merge. The BA/Iberia merger (to be called International Airlines Group) will create Europe's third biggest airline after Air France-KLM and Lufthansa, with some 419 aircraft flying to over 200 destinations.

But apart from the financial savings (estimated to be about £350million a year by 2015) the merger will play to each airline's strengths – BA on the North Atlantic and Iberia to Latin America – while also giving the opportunity to both airlines to develop services from their London Heathrow and Madrid-Barajas hubs.

The other new phenomenon that travel managers in North America and Europe will need to deal with is the rise of the transatlantic joint venture. Primarily featuring North Atlantic members of the three global alliances, the joint ventures have secured anti-trust immunity that allows them not only to set schedules and prices but also offer unified agreements to corporate clients.

One such transatlantic joint business is American Airlines, British Airways and Iberia. It is an agreement to share revenue and reduce costs, co-ordinate networks and schedules and co-operate commercially on routes between the European Union, Norway and Switzerland and the US, Canada, Mexico and US territories.

The joint business agreement should improve customer service with better connections, network, frequency and frequent flyer benefits also enabling the airlines to operate more efficiently, reduce costs and increase their ability to invest in new products and services.

Corporate clients should see benefits in enlarged compliance from their travellers and greater coverage of physical locations in addition to joint sales agreements from the three airlines.

Currently buyers have to negotiate with each airline on an individual deal but in the future they will be offered one deal from the three airlines which should reduce duplication, complexity and potentially cost.

Another benefit is combined fares and itineraries where a customer can book one sector on BA and Iberia and another on American Airlines, which gives more choice of schedules and routings as well as more fares.

For example, if the cheapest fare classes are not available on the BA flight on both sectors but they are on the AA flight, a customer will get the benefit of being able to book one-way on one airline and one-way on another.

The challenges for the joint business agreement will be consistency of product across the airlines and unified communication and strategy – the reputation of this joint business agreement could be damaged if the three airlines cannot control or align with each other.

THE AIRLINE

Richard Vaughan, divisional senior vice president commercial operations worldwide, Emirates Airline

Emirates has never belonged to, nor has any plans to join an alliance. We see them as having significant anti-competitive elements and believe that our membership in one would be an artificial brake on our own business plans.

Unless you are the lead participant in an alliance, individual airline members are compromised by their implicit or implied collective decision-making.

In the recent past, there has been consolidation of airlines on an unprecedented scale; the airline map of Europe and the world is being re-made, often with airline alliances being the vehicle or stimulus for this change.

But the speed and nature of this consolidation forces us to ask whether the consequences have been fully thought through. The entry-level for new airlines, for example, is many rungs higher on the ladder now given that so many countries and regions face the prospect of consolidated carriers dominating their markets, irrespective of the so-called 'remedies' agreed to as part of regulatory approvals.

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Airline consolidation also presents a threat to the future of regional or secondary airports. The great hubs of the world – Frankfurt, London Heathrow, New York JFK – will always prosper, but the thinner economics of markets like, say Brisbane, Nice, Newcastle or Stuttgart, can be exposed and impacted by consolidation as airlines coordinate their schedules.

We also find it disingenuous that some leading alliance airlines remain determined to thwart other non-alliance carriers like Emirates from providing fair and reasonable competition through such carriers lobbying for state protection via air traffic rights.

Some quarters in Brussels have told Emirates that there is only room for two or three airline groupings in Europe for example. Emirates disagrees with this statement, but even if it becomes fact, competition from other quarters will be more important than ever.

Fair market access and open competition is good for Emirates, customers and the global economy. In the midst of an unparalleled consolidation of our industry and extraordinary economic times, Emirates argues that the merits of competition are now more important than they ever have been.

THE PARTICIPANTS

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Peter is an industry advisor and accredited executive coach with 30 years experience in international aviation. He has held senior commercial roles with British Airways, Delta Air Lines, and as part of the start up team for Etihad Airways. He is a Fellow of the Chartered Institute of Marketing and has served as a director on the UK Board of Airline Representatives (BARUK). A regular industry speaker, he has many articles published in the travel and aviation press.

ADRIAN WOODWARD
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Adrian began his career with Thomas Cook before joining GTM Travel Management as CEO in 1995. In 1998 he joined HRG as a management consultant before taking up the role of general manager partner operations in 2001. In September 2009, in addition to his partner responsibilities, Adrian became responsible for HRG's relationships with its global suppliers. He is a member of the Institute of Personnel Management and the Institute of Training and Development.

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Richard is responsible for all commercial activities of the airline across its rapidly-expanding global network that presently spans over 100 destinations in more than 60 countries. He joined Emirates in 2004, bringing with him more than 42 years of travel industry experience. Previously he was general manager for the Concorde Group of companies in Western Australia, where he managed the group's various business units, including Concorde International Travel, World Aviation and several local operations of the group.