Airline Business Models: Cooperation – Consolidation – Integration?

Panel 2

Dr. Andreas Wittmer

Content

• What are business models?

• Development of airline business models

• Cooperation – Consolidation - Integration
The Concept of Value-Based Business Models

Value Proposition
What kind of offer creates customer value?

Value Development
How the core logic of value creation could be elaborated that sustainability of the business model is secured

Value Creation
How these values can be created in an organization?

Value Dissemination
How values are distributed within the organization?

Value Capture
How the created values can be transformed into profits?

Value Communication and Transfer
How the created values will be communicated and assigned?

A business model describes the logic of how an organization creates value!

Quelle: Bieger & Reinhold (2011)

Putting business models in place

<table>
<thead>
<tr>
<th>Normative Company Policy</th>
<th>Legitimation of company</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Development of vision, mission statement, code of ethics, etc.</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Strategy</th>
<th>Creation and maintenance of a sustainable success</th>
</tr>
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<tbody>
<tr>
<td></td>
<td>Development of strategies (company, business segment, competition)</td>
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<table>
<thead>
<tr>
<th>Business Model</th>
<th>Creation and skimming of value</th>
</tr>
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<tbody>
<tr>
<td></td>
<td>Development of value mechanisms</td>
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</table>

<table>
<thead>
<tr>
<th>Operative Planning</th>
<th>Operative process control and securing financial liquidity</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Development of budgets, processes and structures</td>
</tr>
</tbody>
</table>

Quelle: Bieger & Reinhold (2011)
Content

- What are business models?
- Development of airline business models
- Cooperation – Consolidation - Integration

Airline Business Models

- Mega-Carrier
- Flag-Carrier
- Regional Carrier
- Charter
- Low Cost

- Networks
- The wet lease/niche market
- Point to Point airline
Sucess factors

<table>
<thead>
<tr>
<th>Network/Hub Airlines</th>
<th>Wet Lease (Regional carriers)</th>
<th>Point to Point: Low Cost</th>
<th>Point to Point: Charter Airlines</th>
</tr>
</thead>
</table>
| - Extensive market coverage and growth due to network effects  
- Alliances  
- Ability to adopt homogeneous processes and quality | - Niche destinations  
- Flexible cooperation in alliances  
- Cost efficiency  
- Dominance on regional markets | - Easy processes  
- Cost efficiency  
- High flow of traffic | - Relation to/integration in tour operators  
- Cost efficiency  
- Integrated management of capacity |

Quelle: Bieger 2005

Development of Market Shares between the different Business Models

Source: Delfmann 2005
Example LCC: Consistent business models are characterized by self energizing circulation (driver)

Quelle: Casadesus-Masnell & Ricart (2011)

Cost Differences from Legacy to Low Cost Carriers

Source: IATA Economic, December 2006

savings vs. network effects
Content

• What are business models?
• Development of airline business models
• Cooperation – Consolidation – Integration

Internalisation of net effects by airlines

Net Gains/ Synergies

Type of integration

- adjusted timetable
- code share
- integrated network structure
- lounge access and combined frequent flyer arrangements
- integrated pricing
- and integrated operations
- procurement
- synergies
- fleet management
- financing

cooperations
strategic alliances
mergers
Revenue side of net effects

Percentage of the total income synergies* through alliances/mergers

- New connection regional
- New connection international
- S-Curve effect
- Restriction of the net
- FFP
- Total Income Synergies

- \(\text{Netbased utility} = 20\)%
- \(\text{New connection regional} = 20\)%
- \(\text{Restriction of the net} = 20\)%
- \(\text{New connection international} = 15\)%
- \(\text{S-Curve effect} = 13\)%
- \(\text{FFP} = 100\)%

\(\text{"Win-lose"-Synergies, which seem often only feasibly by a complete merger}\)

\(\text{"Win-win"-Synergies, which are feasible in an alliance}\)

*) Source: estimation according to McKinsey

Cost side of net effects

Percentage of the total cost synergies through alliances/mergers

- A/C rental fee
- Pax Service
- Station en
- Fuel
- Flight/ cabin crew
- Technique
- Landing fees
- Distribution
- Overhead
- Handling
- En-route
- Advertisement
- Others**
- TTL Equivalent cost reduction

\(\text{Cost synergies of an Alliance} = 32\)%

\(\% \text{ of operational costs}\)

*) Source: Aviation Strategy, 32, 1999, CE Analyse

**) Source: Publication Airlines, CE Analyse, P/KA

Source: Döring 2006
Example Swiss Network

72 destinations, 39 countries

... and Star Alliance

daily almost 18'000 flights to 965 destinations in 162 countries
Example: British / Iberia – Network Fit

- Complementary transatlantic networks
  - BA currently a leading long haul North Atlantic carrier
  - Iberia currently a leading long haul South Atlantic carrier
- Highly complementary worldwide fit

Source: Presentation Merger announcement BA and Iberia, 12.11.2009

Expected Synergies of Integration

Breakdown of synergies and expected timing

<table>
<thead>
<tr>
<th>Year</th>
<th>Synergies</th>
<th>Implementation costs</th>
</tr>
</thead>
<tbody>
<tr>
<td>Year 1</td>
<td>50 (100)</td>
<td></td>
</tr>
<tr>
<td>Year 2</td>
<td>126 (100)</td>
<td></td>
</tr>
<tr>
<td>Year 3</td>
<td>250 (100)</td>
<td></td>
</tr>
<tr>
<td>Year 4</td>
<td>375 (58)</td>
<td></td>
</tr>
<tr>
<td>Year 5</td>
<td>400</td>
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Source: Presentation Merger announcement BA and Iberia, 12.11.2009
Conclusions

- Business Models combine the strategy with the operative planning.
- Networks are a main source for success of business models.
- Success of integration depends on network fit.
- Further integration from alliances creates significant synergies.

Many thanks for your attention! Questions?

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