Squeezing the lemon

As growth in mature markets falters, the low-fare sector needs to look again at its costs. But are there any further savings to be made? **Ian Putzger** reports

In October, Spirit Airlines elicited a collective gasp from passengers and observers alike with the announcement that it would charge an eye-watering $100 for a carry-on bag if a traveller had not paid a fee for it before arriving at the gate. That marked an increase of more than 100% from the painful $45 it levied before – a juicy margin by anyone's standard. However, according to its own explanation, this is not what the carrier is after.

"Spirit doesn't want customers to pay $100 for a bag at the gate," its press release was headed. It went on to explain that the fee was set deliberately high to encourage passengers to pay for their carry-on items earlier in the process and thereby avoid slowing down aircraft boarding.

"It is fascinating how they pitched that. They said, 'we don't want the additional revenue, and here is how you can avoid paying it,'" remarks Michael Smith, managing partner at Airline Information.

After years of cutting costs, carriers are still streamlining all facets of their business, trying to wring out more efficiencies and costs, belying claims that there are no further cost savings to be had.

"The lemon has not been squeezed dry," is the verdict of John Strickland, director of JLS Consulting. He points to the latest results published by Ryanair and easyJet, which show strong gains in profitability.

"Cost control is not some beautifully named campaign. It has got to be going on the whole time. Cost containment has got to be part of the DNA, not a special campaign," he adds.

However, Ben Jacques, commercial manager at IBA Group, cautions against a narrow focus on cost-curbing efforts. "Pinpointing one cost optimisation is often a false economy. You can bring down the cost of X, but what impact does this have on other aspects? You can save $100,000 here and shoot yourself in the foot," he warns.

Given the painful impact of fuel costs on the bottom line, this aspect has produced some strenuous efforts, remarks George Hamlin, president of Hamlin Transportation Consulting. "Delta's decision to buy a refinery is an interesting step, but I doubt it will find many followers," he quips.

Ryanair's CEO Michael O'Leary has been making noises – this time about a major aircraft deal – but not at any price, as he put it. On top of competitive aircraft prices, this would bring in better fuel economies to boot, but few operators are ready for this option. Maintenance cycles, inspections and re-deliveries, on the other hand, offer more ubiquitous opportunities to optimise costs, observes Jacques, adding that engine maintenance management can also generate significant savings.

There are a number of opportunities to tackle costs when a plane sits on the tarmac, reckons Andy Dobson, EMEA partner in Aviate Consulting. How power is provided to the plane – via a fixed power line or from a generator – can make a considerable difference in cost, he remarks.

New developments in de-icing technology also promise potential savings besides environmental benefits, particularly the use of forced air, Dobson notes. The concept has been trialled with a few airlines, but it remains to be proven on a large scale, he says.

Outsourcing, one of the central tenets of cost optimisation efforts since the beginning, continues to figure prominently in many endeavours. The relationship between airline and handler is expanding towards greater involvement of the latter as it takes on additional functions. "Airlines are looking to the ground handling company to manage certain operations that have traditionally been done by the airline,"

Airpas offers software which can manage direct operating costs and steer processes *(photo: Airpas Aviation)*

Dobson: take a look at tarmac time
(photo: Aviate Consulting)

Spirit's decision to introduce a $100 baggage fee for unbooked bags has hit the headlines. But the carrier says it is trying to change customer behaviour rather than make additional revenues *(photo: Spirit Airlines)*

observes Dobson. For instance, a handler may organise buses to move an airline client's passengers through the airport after a disruption that affects their scheduled itinerary. He adds that the way handlers represent their airline customers has changed and will likely change further.

Since carriers registered in the European Union have the right to perform their own handling, they can enter into a joint venture with a handling partner, an entity that would be licenced by the carrier, Dobson says.

"It is a win for the airline on cost and often on service, and it helps the handler get a foothold in a market where it has had no presence before," he concludes.

Theoretically, relationships between airlines and their suppliers should form a win-win scenario, but the grim pressures of recent years have taken their toll and ushered in more adversarial constellations, some consultants find. Jacques discerns a more recent shift in airlines' approach though. The early reaction of many carriers to the downturn was characterised by battening down the hatches and squeezing suppliers, but over time this has given way to more consideration about service providers' ability to sustain their activities and survive, he says.

In some sectors of business, such as the logistics industry, there has been a growing chorus of voices calling for greater cooperation not only between service providers and clients, but also between customers.

While there has been a trend of low-cost carriers joining hands with airline alliances and forging codeshare deals with other carriers, Smith doubts that many LCCs are ready to team up with competitors to achieve joint savings. "Cooperation is not yet in their DNA. Some of them are not at a point of their growth cycle to be ready for this," he reflects.

Most cost savings have sprung from detailed analysis of established processes. Stephan Wilde, director of sales and business development at Airpas Aviation, argues that airlines can achieve further savings through scrutiny of irregular elements, for instance delays or AOG situations, and their processes to deal with these. Technology can play a huge role here, such as a compensational delay management tool that handles coordination of items such as meal vouchers and hotel vouchers for stranded passengers. This helps prevent abuse while simultaneously working towards better passenger satisfaction, he says.

Airpas, whose client list spans LCCs and network carriers as well as leisure airlines and cargo operators, offers a software suite to manage direct operating costs and steer their processes. Currently a particular focus is on irregular or sporadic elements that are more difficult to capture and document. The basic elements of the software are contract management and tender management tools, and automatic invoice checking. Further modular functionalities include route profitability analysis, financial planning and risk management, which are based on the cost data generated, Wilde says.

"As soon as you have combined contractual with operational data, you gain transparency and can evaluate these costs. You can also use this for modelling and forecasting," he remarks.

Building up the data is not a problem, but getting providers to move to electronic invoicing has been an issue, he reports. "Driving the number of electronic invoices as high as possible is a challenge for us and for the industry," he adds.

Wilde finds it amazing sometimes how little awareness airlines have of incorrect invoicing. "Of course, they do some checks, but when we take a closer look it is surprising how big the room for cost optimisation still is," he says.

Jacques notes that transparency is growing in supplier relationships. "Customer relationship management is much about transparency. Companies are aware that they need more partnerships," he says. ▶

Jacques: beware false economies
(photo: IBA Group)

Strickland: cost containment should be part of the DNA *(photo: JLS Consulting)*

Airpas is planning to use mobile devices so cabin and flight deck crews can capture data on board during turnarounds. "Ideally they should get a signature from the ramp agent immediately to prove and document services provided," Wilde says.

British Airways has moved in that direction, giving iPads to cabin and cockpit crews, observes Jacques. "I don't hear much there from LCCs. The capital cost is potentially prohibitive," he adds.

Mobile equipment is also proliferating inside terminals, as airlines seek to move away from common use environments and bypass airport equipment with their own mobile devices, remarks Dobson. "There is certainly a drive to do it," he says. Aviate is working on trials along these lines with a large airline customer, but it is too early to draw any conclusions, he says.

He also sees much activity around the check-in process. While a combination of approaches coexist at the moment, the trend has gone to internet-based check-in and boarding passes on mobile phones rather than in paper form, and luggage ending up at bag drops at the airport. Airlines have begun to automate the bag drop, Dobson says.

The second large trend around luggage is the effort to keep bags off the plane altogether through disincentives along the lines of Spirit's shock fees for cabin luggage, Strickland notes. He points to Ryanair's efforts to induce passengers to show up at the airport without check-in luggage.

However, this can backfire by pushing passengers to increase their cabin luggage, which can impact the operation, Dobson remarks. "It is a delicate balance," he comments. He expects charges for cabin luggage to gather momentum, saying that this is now beginning to show its face in Europe.

Some recent activities suggest that a number of carriers are trying to find a new balance between cost optimisations and steps that add services for passengers. Strickland mentions easyJet's decision to embrace seat allocation, which runs counter to getting passengers on the plane as quickly and as cost-efficiently as possible *(see Easy does it, p14)*.

"Purely from a cost optimisation perspective, you can get people on board

> "Cost control is not some beautifully named campaign. It has got to be going on the whole time"
> John Strickland, JLS Consulting

quicker if you have no reserved seating," comments Smith. "EasyJet has a strong focus on business travellers. I think that's part of the reason why they are going towards reserved seating."

Hamlin sees large question marks over the ideal balance between premium passengers and high load factors achieved through aggressive pricing.

"Load factors have gone above 80%. How far can they go?" he wonders. "Where does the balance work between low-cost customers who book long in advance and high-yield business travellers, who book at short notice? When do you get to the point where you have not enough leeway to accommodate high-yield passengers who make the low prices possible?"

Smith also discerns a shift in strategy. "Can you have ancillaries that improve the customer experience on a low-cost flight? Some carriers are now offering a premium meal, which you can order in advance. The feedback so far suggests that this seems to be working well," he says.

So although growth in mature markets might be limited, it would seem that further cost and revenue opportunities are still available. ■

EasyJet's decision to introduce allocated seating could mean passengers board more slowly, which might add cost to the operation *(photo: easyJet)*

Wilde: look at irregularities *(photo: Airpas Aviation)*