Airline alliances & Low-cost airlines

The two opposite powers of the contemporary airline industry

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Executive Summary

The airline industry is a subject that is often reported in the media these days. Especially in the last years, a lot of mergers and accessions to alliance have taken place. What is more, a strong competition of low-cost carriers is going on in which cheaper fares are offered with less service on board. The aim of this paper is to analyse to what extent it is advantageous to join an airline alliance and to examine what differences exist between these regular airlines and low-cost airlines.

In the first chapter, the main reasons for the admission of an airline to an alliance are given. Besides, an evolution of airline alliances is given, also stating the alliances that are currently active in the airline market. Furthermore, various types of alliances will be explained. It can be concluded that three alliances currently dominate the alliance market. Besides, it can be said that various types of alliances exists. These types vary from simple agreements to intensive cooperation's.

The second part focuses on the advantages to join an alliance. This chapter is divided into two parts. First, the benefits for the airline company are discussed. Second, the benefits for the customers are argued. It can be concluded that saving costs by cost sharing and increased passenger traffic are the main advantages for airline companies. Besides, it can be said that an extended network with many route possibilities and seamless connections are the most important advantages for customers.

In the third chapter, a comparison between 'full-service' allied airlines and low-cost carriers is given. It can be concluded that a considerable number of differences are seen in various fields, such as in fare management and in communication management. Besides, big contrasts are observed in airline operations, like in airport choice and catering service on board. However, it is also seen that there are a couple of similarities between the two types, for example, in terms of fuel procurement and safety.

The last part focuses on the evolution in terms of passenger traffic and on the future of both types of airlines. As for the evolution of passenger traffic, it is seen that 'die-hard' low-cost carriers are better able to maintain passenger growth these days than regular carriers, even in the event of a financial crisis. One of the current trends that can be observed in the airline industry is consolidation between airlines. As the future of the airline industry is concerned, it can be said that airline alliances will be more heterogeneous in the future. That is to say, focussing more on local markets by including local *feeders* in their alliance. Consequently, more smaller airports will be served and itinerary possibilities for customers are extended. Moreover, it is seen that a more exclusive network will be important in the future in order to offer destinations that other alliance do not offer. It can also be concluded that 'die-hard' low-cost airlines will not offer full service on board. Besides, it can be said that low-cost alliances are not to be created in the nearby future.

Table of content

Introduction

As from the 1960s, travelling by airplane has started to become popular. Over the past 50 years, the number of passengers that go on a journey by airplane has increased tremendously. Also the number of airlines that operate across the globe has grown enormously during the last decades. These days, more than a thousand airlines exists across the world. However, as some people do not directly see differences in types of airlines, it can be said that not every airline is the same. Differences are seen in various fields of the airlines' strategy: from on-board catering to the procurement of aircraft.

In this paper, the most opposite types of airlines will be investigated and compared. On the one hand, regular airlines that are in an alliance and, on the other hand, low-cost airlines. In order to investigate the differences, desk research is used. With the purpose of getting the largest view possible, it was of high importance to use as many different sources as possible. By using of books, online magazines, annual reports and various websites, it has become clear how these two types of airlines are opposed to each other and what trends currently exist in the present airline market. As the airline market is a contemporary topic, a lot of information is found on this subject.

This paper is divided in four chapters. In the first chapter, it will be investigated which airline alliances are currently active in the airline industry and what types of alliances exist. Secondly, it will be argued what the advantages are for an airline to join an alliance and, subsequently, to what extent it is advantageous for customers. In the third chapter, it will be investigated what the differences are between established and low-cost airlines in terms of business strategy and airline operations. Last, it will be argued what the current trends are in the airline industry and what can be expected in the future of both regular and low-cost airlines.

Eventually, an answer will be given on the following research question: *Why should an airline join an alliance and to what extent do these airlines differ from low-cost airlines?*

Chapter 1: Introduction to Airline Alliances

1.1 Introduction

In this chapter, an introduction will be given on airline alliances. First, a definition will be given for the term: 'alliance'. Second, the evolution of airline alliances in the world will be explained. Last, an overview of the different types of alliances that exist will be given.

1.2 Definition

As a basis for this chapter, a definition will be given of the term 'alliance'. According to Stanford-Smith, Chiozza & Edin (2002), a strategic alliance can be defined as *"Any form of long-term co-operation between two or more organisations, where the 'parent' organisations remain separate legal entities, which is intended to fundamentally change the product or service, or its production/delivery method, in a given business unit"* (p. 958).

1.3 Evolution of airline alliances

The first international airline alliance was signed in 1986 in which Air Florida provided a passenger feed for British Island's London-Amsterdam route (Vasigh, Fleming & Tacker, 2008, p. 166). However, this was just a simple version of an alliance, which is called a 'code-share agreement'. This enables an airline to transfer a passenger of a flight of one airline, to a flight of the cooperating airline. There are code-share agreements that simply cover one or a few routes of both airlines, e.g. Amsterdam-Paris and Paris-Madrid. However, there are also code-share agreements that cover the entire network of both airlines. These code-share agreements can be considered as the foundation of the global airline alliances these days. The first major transatlantic airline alliance, including a wide code-share agreement, was signed by KLM Royal Dutch Airlines and Northwest Airlines (USA) in 1992. In 1993, the alliance gained its authorisations by the US government, which enabled both airlines to manage their operations between the United States and the Netherlands (KLM Corporate, 2011b).

After some successful and non-successful creations of code-sharing agreements, the next stage was the creation of global alliances. There were a couple of main reasons for the creation of

such global alliances. First, it can be said that an important factor in the decision is the increase of ticket prices as from 1996, due to higher costs and taxes.

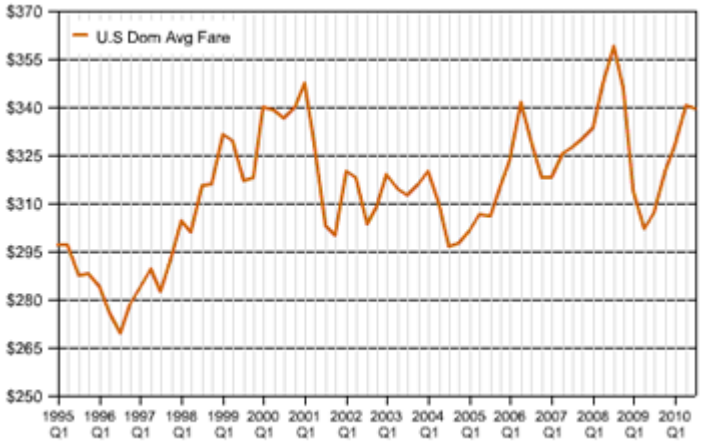

Figure 1.1 Average Air Fares USA: 1995 Q1 to 2010 Q3

Source: Baxter (2011)

As can be seen in figure 1.1, the average air fare in the United States started to increase as from the year 1996. As a consequence of the increased ticket fare, the demand of air tickets decreased. Besides, as can be seen in figure 1.2, more and more airline became active on the market in the 1990s. Consequently, the existing airlines had to compete constantly with these airlines by offering lower prices. Especially the rise of low-cost airlines made it extra hard for regular airlines to survive the market. In order to sustain, airlines had to adjust their cost structure. A solution was found in which they decided to cooperate with other airlines across the world to share costs.

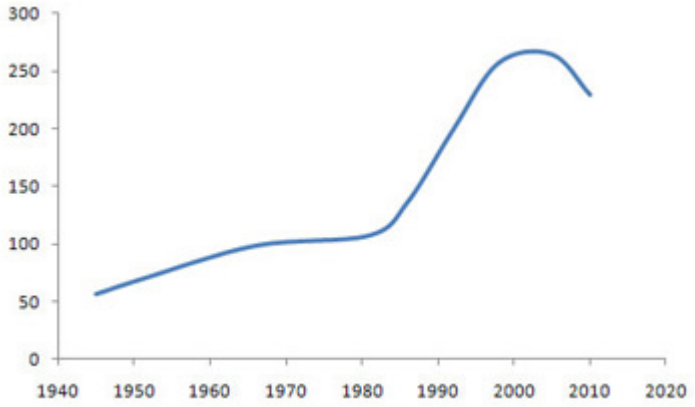

Figure 1.2 Evolution of IATA Membership (Airlines)*

Source: Davies (2011)

* Note: IATA is an international trade body in aviation (IATA, 2011a).

The first truly global alliance was formed in 1997 between United, Lufthansa, SAS, Air Canada, and Thai Airways. This alliance was called the Star Alliance and was shortly followed by similar global alliances (Vasigh, Fleming & Tacker, 2008, p. 167). As from this point, alliances have been adding more and more airlines in order to jointly reach destinations that are located all over the world. Airlines were – and still are – very keen to join an alliance because of the many advantages. These advantages will be pointed out later on in this paper.

These days, three major global alliances exist: Star Alliance, Oneworld and SkyTeam. In the following subsections, these three airline alliances will be briefly illustrated.

1.3.1 Star Alliance

Star Alliance has been created in 1997 by five airlines: Air Canada, Lufthansa, Scandinavian Airlines, Thai Airways and United Airlines. The alliance, based in Frankfurt am Main (Germany), serves over 1,100 destinations in more than 180 countries worldwide, including now – in 2011 – 27 member airlines across the globe. All members together transport over 600 million passengers, having a total revenue of 150 billion US-dollars.

Figure 1.3 Star Alliance member airlines

Source: European Geosciences Union (2011)

According to the website of Star Alliance, their mission is: *"Executing leadership in managing a portfolio of alliance products and services using an agreed process"* (Star Alliance, 2011a).

1.3.2 Oneworld

Oneworld has been founded in 1999 by American Airlines, British Airways, Cathay Pacific, Canadian Airlines and Qantas (Oneworld, 2011b, p. 17). The headquarters of Oneworld is located in Vancouver (Canada), although there are plans to relocate the alliance's central team from Vancouver to New York's Manhattan during 2011 (Oneworld, 2011b, p. 8). The alliance now consists of 14 airlines that fly to more than 750 destinations, spread over almost 150 countries. Together, the member airlines fly over 330 million passengers a year, having a total passenger revenue of a little more than 90 billion US-dollars a year in 2010 (Oneworld, 2011c).

Figure 1.4 Oneworld member airlines
Source: Quotoba Valley (2011)

All member airlines that represent the Oneworld alliance have as common vision: *"To generate more value for customers, shareholders and employees than any airline can achieve by itself"* (Oneworld, 2011, p. 2).

1.3.3 SkyTeam

The SkyTeam alliance was created in 2000 by Aeromexico, Air France, Delta Airlines and Korean Air. The alliance currently consist of 13 member airlines, having its headquarters located at Amsterdam Schiphol Airport, the Netherlands. Within the alliance, a joint-venture exists between Air France, KLM and Delta Airlines, which was formed in May 2009. This joint-venture takes possession of a quarter of all transatlantic flights. That is to say around 200 flights a day between

Europe and the United States, offering about 50,000 seats (Nu.nl, 2009). All 13 airlines that are currently in the alliance serve almost 900 destinations, over 170 countries worldwide. In 2009, the alliance transported around 385 million passengers, having a total passenger revenue of 89 billion US-dollars on a yearly basis.

Figure 1.5 Skyteam member airlines

Source: Contrails North NZ (2011)

1.4 Types of alliances

As stated in *Managing Strategic Airline Alliances* by Kleymann and Seristö (2004), an airline alliance consist of several different types of cooperative links. Nine forms of cooperation can be distinguished.

First, there are *cost sharing ventures*. In the case of a cost sharing venture, two or more airlines collectively purchasing equipment, for example purchase aircraft simultaneously at a manufacturer. Two or more airlines agree on common design of the aircraft, including the interior and engines. However, it could be difficult for airlines to jointly decide on the design, because each airline has its own preferences. In the late 1990s, three Latin American airlines collectively purchased almost 100 Airbus A318/A319 aircraft. In 2003, four Star Alliance members had the intention to bulk purchase up to 200 standardised regional aircraft (Doganis, 2006).

Second, *asset pools* are another form of cooperation. This type of cooperation can often be found in maintenance, in which two or more airlines jointly share reserve parts which they warehouse at outstations or joint warehouses. For instance, in 2009, Garuda Indonesia Airlines and

KLM decided on an agreement that offered KLM the occasion to outsource the maintenance of fan cowls to *AeroAsia*, Garuda Maintenance Facilities (KLM Corporate, 2009).

A third form of cooperation is a *pro rate agreement*. This is one of the most basic forms of agreements between airlines. A real world example is the agreement between Caribbean Star Airlines and Air Jamaica which was signed in 2006. First, the two airlines agreed on improved connectivity. The two airlines' schedules were adapted in order to create more transfer possibilities and to reduce the waiting time of passengers on connection flights. Second, the airlines agreed on improved pricing while offering lower fares when connecting from one airline to the other. This allows passengers, who start their journey in the Caribbean, to have a cheaper ticket when connecting in Jamaica to, for instance, the United States (Caribbean Press Releases, 2006).

Fourth, another basic form of cooperating is a *code share agreement*. In this type of agreement, for example, KLM sells a flight under its own airline designator code (KL), although the flight is operated by another airline, for instance Air France. According to Kleymann and Seristö (2004), the advantage for KLM – in this case – is that it can serve much more destinations, without having its aircraft operating there. The advantage for Air France – in this case – is that it has more passengers to be carried on a specific route, namely with its 'own' passengers and those of its code share partner KLM (p. 13). Figure 1.6 shows the code-share network of KLM.

Figure 1.6 KLM's code-share partners

Source: compiled by the author; data source: KLM Corporate (2011a)

Fifth, an agreement that is often seen is a *feeder*. A feeder is a special form of code sharing which tends to be more hierarchical than a normal code-sharing agreement. An independent regional airline, for example, can operate a code share to a larger airline's hub. For instance, CCM Airlines is a separate French airline based on Corsica. On some routes they also operate under Air France's

designator code (AF), such as on flights between Calvi (Corsica) and Paris' largest airport Charles de Gaulle. However, besides these flights that CCM Airlines operates for Air France, they still operate flights under their own airline designator code, 'XK' (CCM Air Corsica, 2011).

A sixth form of cooperation is a *marketing alliance*. A marketing alliance can include three activities. First of all, joint advertising, in which airlines profit of reduced costs for advertisements, because costs are divided among the participating airlines. Second, joint sales, which makes it easier and cheaper for passengers to combine itineraries between airlines, and which is eventually financially beneficial for both airlines. And, finally, joint frequent flyer programmes, in which two or more airlines combine their frequent flyer programmes. This allows their passengers to gain 'miles' at the airline's partner(s) as well. An example of a joint frequent flyer programme is *Flying Blue*, a programme of Air France and KLM (KLM, 2011a).

Seventh, there are *joint ventures*. According to Kleymann and Seristö (2004), one of the main advantages of joint ventures is that the airline can attain a certain situation in which they create a sort of merger on particular markets. Besides, this joint venture offers the airlines to intensify their collaboration and to avoid any sort of ownership matters without having support of shareholders (p. 14). So, it can be said that these joint ventures are an opportunity for airlines, because they can decide to merge on just one of a couple of all activities, instead of merging on all areas.

The eighth type of agreement is an *integrated feeder*. This form of cooperation is different from a 'regular' *feeder*, which is stated before. As in a *feeder* agreement, the regional airline is operating independently, so only operating under the larger carrier's designator on some routes. However, in an *integrated feeder* agreement, the regional airline is operating completely under franchise to provide for its partner airline. An example is the French regional airline *Régional*. This airline operates the regional French network for Air France, which mainly operates to and from domestic and some international airports within Europe. Even though it has its own brand name, the airline belongs for 100 percent to the Air France Group. Therefore, *Régional* operates with the Air France designator code (AF) on every flight in their own network (Régional, 2011b).

Finally, the last form of agreement between airlines are *equity stakes*. In this case, a rather large airline exercise control over one or more smaller partner(s). Nevertheless, this does not necessarily mean that control of the larger airline will be exercised on all partner's activities. An example is the investment of Lufthansa in the regional airline Eurowings, in which Lufthansa influenced the regional airline's operations in terms of sales, route network and fleet planning (Kleymann and Seristö, 2004, p. 11). However, in order to achieve a certain amount of power over the operations of its partner airline, it is stated that equity investments by larger airlines have to be big enough.

1.5 Conclusion

To conclude, airline alliances have been rapidly growing in the last two decades. The first 'real' agreements between airlines were formed by code sharing. After numerous airlines applied this type of agreement, these were – in some cases – transformed to global alliances. After the first global alliance was created in 1997, more and more airlines were willing to join these type of cooperation's. As a consequence, networks of alliances continued to grow, causing alliances the ability to offer their passengers over 500 destinations worldwide. Over the years, new alliances were created and nowadays, three major airline alliances exist. That is to say Star Alliance, Oneworld and SkyTeam. These three together a little more than 1.3 billion passengers a year.

Besides, it can be concluded that nine types of alliances can be distinguished. First, *cost sharing ventures* in which airlines purchase equipment together, profiting from bulk reductions, in order to save costs. Second, *asset pools* in which two or more airlines share maintenance parts. Third, *pro-rate agreements* in which one airline pays the other airline when it carries its passengers on the other airline's routes. Fourth, *code sharing agreements* in which an airline's flights are also operated with a partner airline's designator code. Fifth, *feeders* in which a fully independent (most regional) airline operates routes on a larger airline's network, using their designator code. Sixth, *marketing alliances* which includes joint activities between airlines, most in the field of advertising or sales. Seventh, *joint ventures* in which airlines merge a couple of activities, such as the application of joint pricing or shared revenue. This enables the cooperating airlines to create a sort of merge, while avoiding ownership problems. Eighth, *integrated feeders* which are likely the same as *feeders*, however the operating (regional) airline operates exclusively for the larger airline, as part of its big network. Finally, *equity stakes* in which a larger airline invests in a smaller airline in order to exercise control over its operations. In short, there exist various sorts of alliance agreements that are applied these days in global airline alliances.

Chapter 2: Advantages of joining an airline alliance

2.1 Introduction

In this chapter, it will be explained to what extent joining an airline alliance is advantageous. First, the advantages from a company's perspective will be given. Thereafter, the benefits for passengers that choose to travel with an airline that is part of an alliance will be explained.

2.2 Advantages for airlines

The first reason for an airline to join an alliance is for saving costs. Costs can be saved by sharing facilities, such as maintenance, like the example of KLM and Garuda mentioned earlier in this paper. Also buying materials, or even aircraft, together – like the example of the four Latin American airlines – can reduce the total costs because of bulk discounts. Besides, the joint use of catering and airport facilities can often help in bringing down the costs for airlines (Bissessur & Alamdari, 1998).

The second reason to join an alliance is the increased passenger traffic. This increase is created by the extension of an airline's network, mostly by code sharing (Bissessur & Alamdari, 1998). As said before, the advantage of code sharing counts for both the 'selling' airline and the 'operating' airline. The selling airline, the one that sells the ticket of the operating airline under its own designator code, has now access to new markets without using their own aircraft. The operating airline, that executes the flight physically, also on behalf of the selling airline, takes advantage of carrying passengers that booked through the selling airline.

Third, a study of Oum, Park and Zhang (2000) pointed out that another reason to join an alliance is the Central Reservation System (CRS). A CRS can be described as: *"A system containing information about availability, rates, and related services, and through which reservations can be made"* (Cvent, 2011). The study argues that code sharing flights are recorded twice in the system. Normally, one flight is recorded as one flight. However, due to the two (or more) designator codes of the airlines, two records will be added to the system. As a consequence, the flights in the CRS will be placed on top of the result list when an inquiry is be made by a travel agent. Therefore, it is more likely that these code share flights will be chosen more often by a travel agent than other flights (Oum, Park and Zhang, 2000).

2.3 Advantages for passengers

Besides the advantages for the airline companies, there are some benefits for passengers that travel with an airline that joined an alliance. A study of Goh and Uncles (2002) shows five advantages for this specific passenger group.

First, a greater network access is available by the airline. These days, travellers prefer to fly an airline with a big network (Driver, 1999). It is therefore of great value that the range of an airline's network is well-extended. By e.g. code sharing, an airline can have a much broader network and can therefore offer much more route options to its customers.

Second, seamless travel is offered between collaborating airlines. Bissessur and Alamdari (1998) state that when passengers transfer on an airport from one airline to the other, a seamless connection is desired. As mentioned before, this is mostly accomplished by a code share agreement between two or more airlines. Within an alliance, this often means that the passengers are able to transfer quickly without spending too much time at the airport. However, quick transfer times could also have a risk. That is to say, missing one or more connections, or even the loss of luggage (Veldhuis, 1997). Nevertheless, these risks are often eliminated, because of the close control between the airlines in an alliance. Apart from this, flexibility is also seen as an advantage in terms of seamless transfers. Because of the great variety of routes, schedules and operators that the alliance's network cover, it can be said that the passenger has the choice of various possibilities in case of itinerary changing.

Third, a transferable priority status is available. In the case when a passenger has a priority status at one airline, this status can be easily transferred to another airline in the alliance group. A passenger who has a priority status can profit from several benefits. For example, a Star Alliance "Gold" membership offers its travellers priority status for check-in, extra baggage allowance and priority boarding (Star Alliance, 2011b).

Fourth, passengers are offered extended lounge access. As a special service to their members, lounge access of all airlines in the alliance will be granted worldwide. Before the accession of the airline, travellers having a "member status" could only access the lounges of the airline where they had this "member status". However, when this airline joins an alliance, passengers having a "member status" at one airline will now have access to all lounges offered by airlines in the alliance. At this moment, in 2011, SkyTeam offers its members access to more than 415 lounges (SkyTeam, 2011b), while Star Alliance offers access to 970 lounges worldwide (Star Alliance, 2011c).

Fifth, benefits are offered for passengers participating in the alliance's Frequent Flyer Program (FFP). Before, when an airline was operating on its own, frequent flyer points and other benefits could not be transferred to another airline. However, when an alliance is joined by an

airline, FFP benefits can be transferred between all airlines in an alliance. As a consequence, frequent flyer points can be obtained faster than before.

2.4 Conclusion

To summarise, there are eight advantages of an alliance in total, of which three advantages as from an airline's perspective, and five from a customer's perspective. As from an airline's perspective, first, costs can be reduced by e.g. sharing facilities as maintenance. Second, passenger traffic is increased by allowing code sharing. Third, because of the code share agreement, every additional designator code will be entered in the CRS, which increases the chance to be selected by a travel agent.

Besides, from a customer's perspective, first, a greater network is available to travel. Second, seamless travel is offered by quick connections and a wide range of alternatives. Third, a priority status at one airline is applicable at all member airlines. Fourth, lounge of all alliance's members are accessible. Last, frequent flyer points can be obtained more easily, because these can be gained on all flights within the alliance, instead of only flights of one airline.

It can be concluded that there are possibly more advantages for passengers, than for the airlines themselves. However, it can be seen that most of those advantages are only applicable for frequent flyers ("members"), like priority status and FFP possibilities. Nevertheless, this does not alter the fact that 'regular' passengers can profit from some advantages, e.g. quick connection times and the wide range of destinations that are offered. After all, all the extra benefits for frequent flyers are promoted on a large scale in order to attract prospective customers. Therefore, it can be said that the benefits for the customers are indirectly an advantage (and opportunity) for the alliance to acquire new frequent flyers.

Chapter 3: Differences between regular and low-cost airlines

3.1 Introduction

As stated in one of the previous chapters, an airline joins an alliance because of several reasons. It can be argued that, as forces of several airlines are combined, the accession to an alliance results in a better market position as a group, rather than when an airline operates on its own. A question that arises is: why can low-cost airlines survive really good on their own, while – in some cases – established airlines join an alliance in order to better endure the contemporary airline industry? In this chapter, low-cost airlines and established airlines will be compared in terms of business strategy and operations, focussing on the success of low-cost airlines. In order to illustrate the theory, examples will be given, mostly comparing KLM and the Irish low-fare airline Ryanair.

3.2 Introduction to low-cost airlines

In order to elaborate on the subject of low-cost airlines, a definition of the term "low-cost airline" is needed. In *Handbook of Low Cost Airlines*, Groß & Schröder (2007) state that: *"low cost airlines organise all business activities under the aspect of optimising or reducing costs in order to achieve a strategic success position, and, thus, competitive advantages"* (Groß & Schröder, 2007).

In 1971, Southwest Airlines (USA) was the first low-cost airline to operate in the aviation market, which turned out to be a immense success. This concept was later on moved to Europe, where businessman Michael O'Leary started the first European low-cost airline in the early nineties, called 'Ryanair'. After the start of Ryanair, lots of other low-cost airlines commenced serving destinations in Europe and other continents for low prices, such as the famous orange-coloured airline Easyjet.

3.3 Business strategies compared

In their book, Groß & Schröder (2007) state five main conditions exist for an airline to save costs. First, the implementation of lean and cost-effective company structures. Second, a minimum complexity in operations. Third, a high cost transparency. Fourth, a concentration on the company's core competencies. And last, the outsourcing of strategically non-relevant tasks.

In the following subsections, it will be explained – according to Groß & Schröder (2007) – how operations of low-cost airlines differ from established airlines, like KLM. Besides, it will be argued how low-cost airlines save money on different levels.

3.3.1 Fare management

Probably the most important factor of a low-cost airline is the 'fare management' of the airline, which is by far different from regular airlines. First of all, the way tickets are sold by low-cost airlines is different. Regular airlines, mostly in a case of code-sharing or alliance, sell their tickets through the complete network. For instance, if a ticket from Amsterdam to Sydney is searched on the website of KLM, several itineraries are offered to reach the final destination. As KLM has a code-share agreement with Malaysia Airlines, customers will be offered a route via Kuala Lumpur (Malaysia), the base of Malaysian Airlines. Unlike regular airlines, low-fare airlines only sell one-way tickets. So, a return tickets is seen as two one-way tickets (KLM, 2011b). Therefore, low-cost airlines do not offer any transfer possibilities, only A to B connections.

Not only heavy competition between established and low-cost airlines exist. Also among low-cost airlines exist competition as they constantly (try to) underprice each other. Moreover, different marketing stunts are executed, which can sometimes build up the competition between airlines as can be seen in picture 3.1.

Figure 3.1 Two examples of competing messages of Ryanair to its competitors
Sources: Hendriks (2007) and Kunadt (n.d.)

Especially Ryanair has published some advertisements which were seen as quite offensive and seen as 'rude'. An example is an advertisement of Ryanair that was published in 1996. "It's amazing what lengths people will go to, to fly cheaper than Ryanair" was the headline of the advertisement (Creaton, 2007, p. 176).. This advertisement was issued in the newspaper a few days after a hijacked plane of Sudan Airways had flown to London Stansted Airport. This was seen as a

severe hijack, which caused a lot of traumatised travellers, as the hijackers sat on the airport's apron for more than 20 hours, threatening passengers to shoot them. This statement of Ryanair shocked a lot of people and was paid much attention to in the media (p. 176). This is just one of the examples that shows Ryanair's competitive approach to its competitors.

Moreover, low-cost airlines are regularly in the news, being accused of misleading selling strategies. Fares that are placed on their websites and in their advertisements are published as 'final prices'. That is to say, the total price that customers eventually have to pay. However, taxes and other surcharges are mostly not included in these prices. As a consequence, customers get confused and are surprised when encountering these extra costs at the end of the booking process. To illustrate this situation, an example will be given according to figure 3.2.

Figure 3.2 First step of booking process Ryanair.com

Source: compiled by the author

Figure 3.2 shows the first phase of the purchase of a return ticket to Dublin on the website of Ryanair. The published fares, which are the two fares marked in yellow, are the ones that are seen first in the booking process. However, when proceeding to the next steps of the booking, more costs will be added to the original price. As can be seen in the figure, the total price that the customer has to pay, including all taxes, levies and other fees, is nearly 65% higher than the published fare. Moreover, the baggage fee for taking a suitcase with you is not included as this is charged separately. The charge for a suitcase can take up to 35 euro's for a one-way trip. This depends on the weight of the luggage, travel period (off-peak or holiday season) and destination

(Ryanair, 2011c). In Appendix A, the booking process on the website of KLM can be found. It can be seen that, unlike at Ryanair, the total fare is directly displayed upon the first booking phase. Even though, the only fee that is charged by KLM in a later stage is the booking fee of 10 euro's.

3.3.2 Distribution strategy

As stated before, airlines that join an alliance have various channels through which their tickets are sold, for example travel agents and CRS applications, like Amadeus. Low-cost airlines, on the other hand, generally do not have this variety of distribution channels as they prefer to pull the strings their selves. For example, Ryanair has only two main distribution channels through which they their tickets are sold. On the one hand, their own website and, on the other hand, several central call centres spread over Europe (Groß & Schröder, 2007, p. 46). As opposed to bookings that are made through their website, Ryanair 'penalise' their customers when booking via one of their call centres, charging a "Call Centre Reservation Fee" of 20 euro's (Ryanair, 2011c). So, unlike established airlines, no other distribution channels are used by Ryanair like complex reservation systems or selling through intermediaries (e.g. travel agents), which can save costs on technology investments and commissions.

As opposed to Ryanair, some low-cost airlines do sell their tickets through distribution channels like travel agents and CRS applications. Two airlines that do so are the German operators Air Berlin and TUIfly (Groß & Schröder, 2007, p. 46). As said in the chapter on airline alliances, publication of ticket fares in one or more CRS can create an extended brand awareness. This allows to get in touch with new potential customers.

3.3.3 Communication strategy

Just as the communication strategy of established airlines, the strategy of low-cost airlines is set up to inform customers about the various services that are offered. Public relations by low-fare airlines is mostly done by organising special events. As a result, public interest is increased. Most of the times, sales promotions are included in gaining free publicity. Giving away free tickets is one of the various types of promotions that are regularly done. For example, in 2005, Ryanair offered around 4 million free tickets. Only the additional taxes had to be paid, so rather the 'basic' fare was at no cost (Travel Inside, 2005).

Besides online promotions, also real life events are organised to boost public interest. For example, in October 2009, Easyjet organised a huge event at Amsterdam Schiphol Airport, which was set up because of the introduction of two new destinations: Rome and Madrid. At this event, an orange-coloured mini-zeppelin was flying above the square in front of the airport's terminal,

containing dozens of free tickets. It was a very busy event, where hundreds of persons were present in order to secure the free tickets (RTV Noord-Holland, 2009).

In addition, offline publicity (e.g. newspaper advertisements) is also a part of the communication policy of a low-cost airline. In order to hold down on costs to the maximum, Ryanair publishes most of the time in black-and-white, to avoid the costs of colour-printed advertisements (Allvoices, 2011). Besides low-fare airlines, established airlines are also active on offline publicity. Airlines like KLM often publish advertisements in newspapers or advertise through billboards along the road.

Advertisements of low-cost airlines include most of the time *basic fares*. That is to say, the total price excluding taxes and surcharges, such as airport tax. These fares are generally displayed on the bottom of the advertisements. As stated before, these published fares have caused a lot of misunderstanding among customers. In contrast with low-cost airlines, established airlines include more and more *all-in fares* in their advertisements. By publishing these fares, it is shown that there are no hidden additional costs that could appear in the booking process.

Figure 3.3 Differences between Ryanair and KLM advertisements
Sources: U Talk Marketing (n.d.) & KLM (2011b)

Besides these promotional events and advertisements, there are some indirect ways to create brand awareness. For example, the British airline Easyjet gained a lot of popularity through the TV-series *Airline*. In this series, employees and passengers of Easyjet were followed in the terminal and

during the flights. The series were very popular in the United Kingdom, where it was seen by millions of British inhabitants. Because of this success, it was also sold to other countries, such as the Netherlands, Japan and even New Zealand (Groß & Schröder, 2007, p. 48). Nevertheless, not only low-cost airlines had their own TV-show. Around 2002, the Dutch airline *Dutchbird* had the same type of TV-show in the Netherlands (Airborne Dutchbird, n.d.).

Furthermore, the brand design of an airline is also an important publicity factor for the company. In the past, the aircraft of Hapag Lloyd Express (which is now TUIfly), were well-known for their characteristic "taxi style" colour schemes. This colour scheme fitted very well with their slogan: "Fliegen zum Taxipreis", which is German for "Flying for a price of a taxi" (TUIfly, 2011). Besides low-cost airlines, airline alliances also "advertise" for their alliance by painting their members' aircraft in the colour scheme (livery) of the alliance. For example, Skyteam has currently 20 aircraft that are painted in the livery of its alliance (SkyTeam, 2011c).

So, it can be said that, as far as communication policy is concerned, not only differences, but also similarities can be found.

3.4 Airline operations compared

On the field of airline operations, difference and similarities can be seen as well. As seen in the previous paragraph, low-cost carriers are having a more cost-efficient strategy than regular airlines. In this paragraph, it will be investigated to what extent the cost-efficiency of low-fare airlines differ from established airlines in terms of operations.

3.4.1 Aircraft procurement and design

Airlines can acquire their aircraft by many different ways. They can decide whether to purchase or lease an aircraft. Furthermore, they can choose whether they buy a newly manufactured or a second-hand airplane. In order to save money, leased aircraft are mostly used by low-cost airlines. One of the main advantages of leasing aircraft is that it holds down costs significantly. After September 11th, 2001, the airline industry collapsed and many airlines suffered of the low passenger rates, which has led a lot of airlines into bankruptcy. As a result, lots of airlines sold their aircraft at very low prices. This was, however, a chance for low-cost airlines, as they had the opportunity to purchase a lot of second-hand aircraft with great discounts (Groß & Schröder, 2007, p. 35).

Another way a low-cost airline can save money on buying aircraft is the option of purchasing less-equipped aircraft (Groß & Schröder, 2007, p. 36). Established airlines, like KLM,

have seat pockets in the back of the seats (for e.g. safety cards and in-flight magazines). However, airlines like Ryanair do not include these seat pockets in their configuration, because this involves extra costs. The airline simply puts a sticker with the safety instructions on the back of the headrest part of the seat.

Besides, low-cost airlines can save a lot of money when they bulk-purchase aircraft, receiving discounts of the aircraft manufacturer. In the past, airlines like Ryanair and Easyjet have bulk-purchased a lot. Whereas EasyJet focussed more on Airbus A319's, Ryanair concentrated more on the purchase of Boeing 737-800's. For instance, in 2001, Ryanair ordered up to 150 new Boeing 737-800's at the same time (Value Investigator, 2003).

Moreover, money can be saved by having a 'uniform fleet' (Groß & Schröder, 2007, p. 35). This means that an airline's fleet only consists of one type of aircraft. Established airlines, like KLM, have a lot of different aircraft types to have adapt quickly on demand. However, all these types of aircraft cost a lot of money. By having the same type of airplane, money can be saved on training of cabin crew of maintenance employees, as they have to be trained for one aircraft only.

Furthermore, established airlines, have multiple types of classes included in their aircraft's seat configuration (KLM, 2011d). Most known class types are the regular 'economy class', the more expensive 'business class' or even a 'first class' which is available in some aircraft only. A typical characteristic of a low-cost airline is to operate on a single-class operation, which means that the airline's aircraft are only equipped with 'economy class' seats. As these 'economy class' seats have less leg room than the 'business' or 'first' class seats, more seats can be placed in the aircraft. As a consequence, seat availability is increased. What is more, in most low-cost airlines' aircraft, the seat pitch is even more reduced in order to insert an extra seat row. For example, KLM's Boeing 737-800 has a seat capacity for only 171 passengers (KLM, 2011c). However, this same type of aircraft of Ryanair has a seat capacity for 189 passengers (Ryanair, 2011b), which means an extra number of 18 passengers can be transported.

3.4.2 Airport selection

Besides aircraft, airports form as well an essential factor in the business strategy of a low-cost airline. In order to offer the passenger the lowest fare as possible, low-cost airlines are more likely to choose 'secondary airports' when creating new routes (Creaton, 2007, p. 181). These airports are mostly located on a reasonable distance of city centres, offering less facilities than regular airports that are located closer to a large city and mostly served by regular airlines. Because less aircraft facilities are offered, the costs for the airline are substantially lower. In addition, secondary airports are favourable for low-cost airlines because most of these airports are less congested than 'regular airports' like Amsterdam Schiphol. As a result, waiting in long queues in front of a runway holding

point for take-off is avoided. Also, the time that is spent on the apron by an aircraft is reduced, because of the ability of the ground handling agent to operate more quickly when the apron is less occupied. When less time is spent on the apron, a maximum use of aircraft can be achieved by an airline, performing up to 6 flights a day. Besides, because the airport apron is less utilised, the chance that an aircraft has to wait for an available gate is also minimised, which means that there is less chance for delays (Groß & Schröder, 2007, p. 60-61). Apart from the ground operations, discounts on taxes may apply for airlines that operate from and to these smaller airports. Usually, regular airlines do not visit these airports and, therefore, possible positive (indirect) economic effects for the region (e.g. tourism) around the airport can be created. For instance, Ryanair operates to Paris Beauvais Airport (Ryanair, 2011a), which is situated approximately 80 kilometers north of Paris. A disadvantage for the passenger is that they still need to take a shuttle bus to the city centre of Paris, which costs about 15 euro's per trip per person (Aéroport Paris Beauvais, 2011). There have been various complaints against Ryanair, because, for example, the destination 'Paris' was published on advertisements, instead of 'Beauvais' which caused people thinking that direct flights to Paris' main airport were offered (Creaton, 2007, p. 180-181).

3.4.3 Outsourcing of ground operations

Outsourcing is another important element in the business strategy of a low-cost airline. By outsourcing services, e.g. the maintenance of aircraft, additional fixed costs can be avoided. Most of the times, companies that are specialised in taking care of, for instance, maintenance can execute the tasks with a better cost-effectiveness than when an airline does it itself (Groß & Schröder, 2007, p. 36).

Outsourcing of passenger and ground handling is often the case in aviation, even by established airlines. In this case, the tasks are outsourced to – so called – "ground handling agents", e.g. Aviapartner or Servisair (Schiphol Group, 2010). These organisations take care of every process of the aircraft's presence at an airport, such as passengers check-in and baggage handling. When outsourcing ground handling to third parties, money can be saved on own personnel costs as for ground staff. Established airlines mostly have their own ground handling subsidiary, like KLM having "KLM Ground Services" (Schiphol Group, 2010).

In contrary to ground handling, information desks in an airport's terminal are mostly not outsourced and therefore equipped by the airline's own staff. Moreover, large waiting rooms and extended lounge services (as can be seen in the chapter about airline alliances) are not needed for low-cost airlines, as they only perform "A to B" flights, so not offering any transfer flights like most established airlines (Groß & Schröder, 2007, p. 36).

Furthermore, cleaning of the aircraft is usually – that is to say at most airlines – done by either a subsidiary or an external cleaning company, for example Lavos (Lavos, 2011). However, at Ryanair, tasks that are normally done by either own or outsourced ground handling, are executed by the cabin crew themselves (Kapferer, 2008, p. 345). For instance, waste collection and cleaning are included in the range of duties of the cabin crew. As a consequence, money can be saved on internal or external ground handling costs.

In the last decade, flight bookings via the World Wide Web have developed rapidly. However, since a couple of years, online check-in for a flight is made possible. Through the website of an airline, it is possible to select a preferred seat and print the boarding pass at home. Besides, self service check-in machines have also been developed. All these new ways to check in are most profitable for airlines, because less personnel is needed for check-in desks. However, there are still passengers that prefer to check in via the regular desks. Both established and low-cost airlines take advantage from this new technology. Since 2009, Ryanair only offers online check-in and abolished the 'traditional' check-in desks. Only baggage drop-off desks are open for passengers travelling with hand luggage (Op Reis, 2009). If the passenger does not want to check in online, a fee of 40 euro's must be paid at the Ryanair drop-off counter (Ryanair, 2011c).

3.4.4 Cabin crew management

Not only money can be saved on ground operations, also a smart planning of the airline's cabin crew can lead to more efficient flight operations, which, in some cases, can lead to a cost reduction. According to Bley & Büermann in Groß & Schröder (2007), an efficient cabin crew operation can be achieved by a couple of actions.

First, savings can be made on accommodation and transportations costs. Established airlines offer their crew, usually after an evening flight to a destination outside the crew's home country, an accommodation where they can stay the night and then flying home the next morning. As some cabin crew compositions can go up to 12 persons per flight, these regulations involve a lot of costs for airlines. Therefore, low-cost airlines have a different approach regarding the planning of their cabin crew. A crew will always return to their base after their last flight in the evening. This avoids the costs of overnight accommodations, transportation and the daily allowances at one of the airline's destinations (Groß & Schröder, 2007, p. 61-62).

Second, by assigning a crew to an aircraft for a whole day, the risk of distortion of the daily operations is reduced to a minimum. For example, a KLM-crew starts with a return flight to Manchester in the early morning. When they return at Amsterdam Schiphol, they often need to change to another airplane for their next flight, which is located at another gate. In the case that the first flight from Manchester is delayed, the crew is delayed as well, causing for irregularities in the

operations of the next flight(s). To avoid these inconveniences, low-cost airlines crews are often assigned to one plane, which they will be following during the whole day, without transferring to another (Groß & Schröder, 2007, p. 62).

3.4.5 Catering

As a part of the 'low-cost formula', catering service is not offered during flights, unlike most established airlines that generally offer (hot) meals on board. However, instead of this meal service, low-cost airlines offer their customers drinks and snacks on payment. This is beneficial for the airline because the catering costs are almost reduced to a minimum. Moreover, the extra income that is made is also favourable for the airline, as the products are sold against reasonably high prices. The British low-budget airline easyJet even claims about 13% of its ancillary revenue (per seat) on in-flight services (Groß & Schröder, 2007, p. 58). On the other hard, because of limited catering services, the so-called 'turn-around-time' – the time that the aircraft is on the ground between two flights – is also reduced. There is hardly any catering truck needed to provide the airplane for meals, as this is the case with regular airlines.

3.4.6 Similarities

So far, only differences between regular and low-cost airlines have been discussed. However, some factors can hardly – or cannot – be influenced by an airline. A reason could be that an airline cannot operate without is, or because of strict regulations in aviation law.

One of the factors that airlines – or in this case aircraft – are most dependent on is fuel. As fuel is essential for the operation of aircraft, barely any savings can be made on this domain. However, the amount of fuel that is necessary for an aircraft to operate on a route also depends on the weight of the aircraft. The less the weight of the aircraft, the less fuel is needed. Therefore, by the abolishment of extra catering services, like established airlines offer, that often result extra weight, less fuel is needed for a plane to perform its flight. Also, the elimination of cargo services can help reducing the aircraft's weight. As a result, minor savings can be made on fuel (Groß & Schröder, 2007, p. 37). In addition, the so-called 'fuel hedging system' might also help in saving costs. This system implies a contract between a fuel supplier and an airline in which they agree on a fixed price for fuel. Mostly, a 'medium-term contract' is concluded which generally lasts five years. However, fuel costs can only be saved if the market price of fuel eventually rises above the contracted price (Groß & Schröder, 2007, p. 37).

A second point on which no savings can be made is safety. Some people feel hesitant about booking a ticket at a low-cost carrier, as they expect old aircraft that might not meet the safety

standards (Groß & Schröder, 2007, p. 32-33). However, if fleet ages are compared, it can be seen that the average fleet age of Ryanair is 3.3 years (Airfleets.net, 2011b), while KLM's fleet has an average age of 10.3 years (Airfleets.net, 2011a). Therefore, on the basis of these data, this prejudice can be objected. Besides, low-cost airlines have to accept the rules that are set by the international and national governments. If it turns out that an airline does not comply with all the rules, it could risk high fines and a loss of the airline's image in the market (Groß & Schröder, 2007, p. 32-33). Especially when violations of safety are published in the media, severe consequences could follow, as passengers consider air safety of paramount importance.

3.5 Conclusion

It can be concluded that there are a considerable number of differences between regular airlines (allied or non-allied) and low-cost airlines. First, in terms of fare management, differences can be seen in the selling structure. As allied airlines mostly sell their tickets through a complete network, low-cost airlines tend to offer only 'A to B connections' without transfer possibilities. Also the way the fares are published is different in terms of the hide of additional charges.

Another difference between the two types of airlines is the type of ticket distribution. Established airlines often use complex reservation systems, because of the large network and transfer possibilities. However, low-fare carriers often tend to use their own systems – which are simpler and cheaper – because of their fares are based on one-way fares, without any transfer possibilities.

As far as the communication strategies of regular and low-cost airlines are concerned, it can be concluded that not many differences exist. Both airlines focus these days on free publicity, in order to create brand awareness. Besides, real life events with offering free tickets and fly-on-the-wall TV-series are organised to promote their brands. What is more, brand design has also become an important part of their brand promotion. Both low-cost airlines and allied airlines paint their aircraft in various eye-catching liveries in order to create brand awareness.

As for the airline's operations, differences can be noted as well. First of all, low-cost airlines tend to lease aircraft more often instead of buying, unlike regular airlines that generally purchase their aircraft directly. What is more, different from established airlines, low-fare carriers are more likely to purchase less-equipped aircraft, as this reduces costs on aircraft design. Moreover, unlike regular airlines, low-cost airlines generally have a uniform fleet, which results in saving money on maintenance and training of cabin crew. Besides, a difference can be observed in on-board classes. As regular airlines have multiple class types, low-cost airlines only have an economy class, often including a reduced seat pitch. As a consequence, more seats can be placed

because of more space. Another difference is the use of airports: as established airlines generally serve main airports, low-fare carriers are more likely to choose for ‘secondary airports’. These airports are located on a considerable distance of a large city. However, less fees are charged by the airport and the airports are less congested which reduce the ‘turn-around times’ and minimises the change of delays.

Furthermore, it can be concluded that outsourcing is a feature that is often used by airlines, as external companies can perform tasks with a better cost-effectiveness. Outsourcing is mostly done in terms of ground handling and cleaning. As both regular and low-cost airlines make use of outsourcing, in some cases low-cost airlines make more use of it. However, at some low-cost airlines, cleaning is in some cases even done by the cabin crew their selves, in order to save even more costs. As airline alliances have extended lounge services that are offered to their members, low-cost airlines do not include this feature, because of cost-savings and because no transfers are offered.

What is more, there is a different between the two types of airlines in terms of cabin crew planning. Different from regular airlines, low-fare carriers assign their crew to one aircraft for a whole day, so that they return at their base by the end of the day. As a consequence, savings are made on accommodation as no overnight stays are planned. Besides, because the crew do not has to change aircraft at airports, the risk of delay of the daily operations is minimised.

Besides, one of the main differences between regular and low-cost airlines is the catering service. Regular airlines often offer meals and drinks included, while low-cost airlines do not include this service. However, drinks and sandwiches are offered at reasonably high prices, in order to create extra income. Additionally, less on-board catering means there is hardly any catering truck needed, which reduces the time that is spent on the ground.

Eventually, there are also some similarities between the two types of airlines. First, fuel prices are more or less the same for every airline, so hardly any savings can be made on this domain, except for fixed-priced contracts. Second, safety is a matter of which every airline has to accept the rules that are set, so, on this point, no savings can be made by any of these airlines.

To conclude, it can be said that there are many differences between regular airlines and low-cost airlines, in terms of management and operations. In addition, it can be concluded that on many fields, low-cost airlines reduce the costs by applying a different strategy than regular airlines. However, it can be concluded that cost-savings cannot be made on any field in aviation.

Chapter 4: Future perspective

4.1 Introduction

In the last decades, a lot of airlines joined different alliance groups and lots of new low-cost airlines were created. Therefore, it might be interesting to see how these two groups will develop in the future. In this chapter, first, the evolution of passenger traffic until now will be discussed. Besides, current trends in the airline industry will be discussed. Furthermore, the future of both airline alliances and low-cost airlines will be argued. Moreover, it will be discussed whether low fares and full service can be combined. Last, it will be argued whether low-cost alliances can be expected in the future.

4.2 Evolution in passenger traffic

Figure 4.1 shows the evolution of passenger traffic of low-cost airline Ryanair and of Air France/KLM Group (AF/KLM Group).

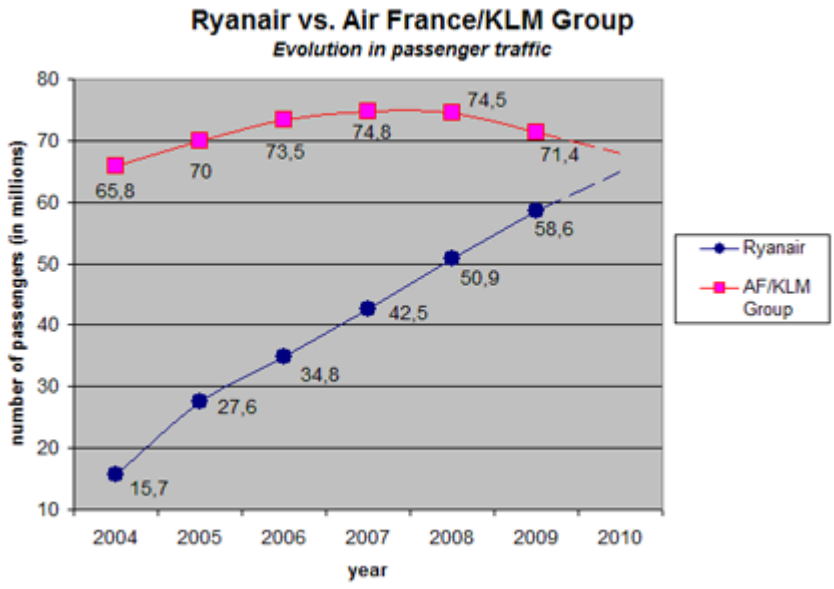

Figure 4.1 Evolution in passenger traffic of Air France/KLM Group and Ryanair
Source: compiled by author; data source: Ryanair (2011d) & Air France-KLM (2011)

It can be seen that the AF/KL Group had an increase in passenger traffic from 2004 to 2007. However, after 2007, a decline in the number of passengers can be observed. In contrary, it can be seen that, in the same period, low-cost airline Ryanair remains having a constant passenger growth. It can be concluded that low-cost airlines, such as Ryanair, are operating more prosperously than regular allied airlines, such as Air France/KLM. It can be said that the main reason for this tendency is that flying has become more affordable because of low-cost airlines. Therefore, passengers that cannot afford to fly regular full service airlines, choose to travel with low-cost airlines. Furthermore, it can be argued that low-cost airlines are better able to cope with a financial crisis, for example the one that started in 2008. This can be clearly seen in the curve of AF/KLM, which starts to decline in 2008, while the curve of Ryanair remains progressive. What is more, the striped lines show the expected results on 2010 if the decline or progression will have the same percentage as over 2008-2009. It can be seen that, if the described case proved to be true, the two lines might cross each other in the coming years. So, it can be said that passengers have been more and more attracted to the 'cost-efficient' business model of low-cost airlines.

4.3 Current trends in the airline industry

Since a couple of years ago, there is a clear trend of consolidations between airlines. It is seen that consolidation of airlines is mostly taking place on a regional basis. Especially in Europe, Latin America and North America, there are a lot of consolidations taking place these days. In the United States of America, large consolidations have been created, especially in the last five years. First, in 2008, Delta Airlines took over Northwest Airlines (Adams & Reed, 2008). Two years later, in 2010, United Airlines and Continental Airlines started a merge under the parent company name *United Continental Holdings, Inc.* (Milmo, 2010). And, some months later, Southwest Airlines took over Air Tran, which gave Southwest Airlines broader access to Atlanta Hartsfield-Jackson's airport. According to Helane Becker, analyst at Dahlman Rose & Co., consolidation of airlines is *"a positive development, instead of growing organically. The airlines are […] consolidating […] in order to preserve profitability"* (CNBC, 2010). Also in Europe, several consolidations have taken place. Probably the most known airline consolidation is the merger of the Dutch airline KLM and the French airline Air France in 2004. After this merger, Lufthansa followed quickly by an acquisition of Swiss Airlines in 2005 (Lufthansa, 2010).

Besides this trend of consolidations, an alliance could have an added value, according to Jaan Albrecht, CEO of Star Alliance. *"[…] the added value of the alliance is to be like a bridge over these areas where they [the airlines that consolidate] are not consolidating. […] our alliance*

is still like the umbrella that brings initiatives together and allows the carriers to offer a seamless product" (Business Traveller, 2010b).

4.4 Future of alliances

In the article *Future Developments in the Structure of Airline Alliance Networks*, by Birgit Kleymann (n.d.), the future of airline alliances is discussed at various points.

First of all, it is stated that alliances are to become even more heterogeneous in the near future. That is to say that alliances do not only contain airlines that operate transatlantic or long-haul flights, but include more local and regional operators. In the chapter on alliances, *feeders* and *integrated feeders* are discussed. These type of airlines, that 'feed' a larger airline, are more and more joining the alliance instead of only applying code-sharing, in order to extend the possibilities in the route network. That is to say, serving local airports in order to connect these with a larger hub, so that passengers can easily connect on other (intercontinental) flights with the larger carrier (Kleymann, n.d.).

Furthermore, a remarkable feature is the exclusiveness of a network. For example, in the past, there has been a code-share agreement between the Brasilian airline Varig and Japan Airlines. This code-sharing was focussing on the main routes between Brazil and Japan. However, when Varig joined Star Alliance in 1997, the code-share agreement between the two partners could not be maintained. This is caused by Star Alliance that wanted to have an exclusive route network. As Japan Airlines was not a member of Star Alliance at that time, the code-share agreement between the two airlines was suspended (Kleymann, n.d.).

4.4.1 Local markets without alliances

Not all large airlines in various markets in the world are part of an alliance. One of the few countries that does not have an alliance included in its market are the Arab Gulf States. One can ask oneself why these airline are not included in an alliance. A reason for the behaviour of Gulf airlines as Emirates or Qatar Airways, is that they have competitive business strategies. Jaan Albrecht, CEO of Star Alliance, argues that these airlines *"are building hubs in the desert with huge investment in infrastructure to try to connect South East Asia and Australia to Europe and the US"* (Business Traveller, 2010b). Furthermore, he argues that these are exactly the routes that alliances like Star Alliance are intending to connect and that they therefore take the passenger traffic from the regular airlines (Business Traveller, 2010b). Albrecht clearly states as well that there is no point in adding these airlines to an alliance, like his', as these carriers remain to have a

competitive point of view on other airlines. Albrecht comments: *"So why should we enter into this form of collaboration helping them to expand and get their brands known on a worldwide basis?"* (Business Traveller, 2010). Mauro Oretti, Skyteam's vice president of sales and marketing is of the opinion that the Gulf carriers are not interested. He claims that his alliance's strategy is *"to provide a complementary network solution to all our members, so we try not to have members whose networks overlap"* (Business Traveller, 2010). Besides, Oretti is of the opinion as well that Gulf airlines do not have a home market and that they only connect passengers between regions outside their home market. So, it can be said that there is no reason for airlines of the Arab Gulf States to join an alliance. On the one hand, because they have a different business strategy than is required for an alliance. On the other hand, because they compete on the same routes an alliance already has, because of the lack of a real home market. Therefore, it can be argued that there is no added value in having these airlines in alliances for now.

4.4.2 Solutions for non-allied carrier

It is said that some problems could occur for the non-allied carriers in the future. It could be possible in the future that all competitors of a non-allied airline have joined an alliance. In that case, all competitors offer a much broader route network than the non-allied carrier. As a consequence, this airline is almost forced to join an airline alliance in order to survive the (local) market. Kleymann (n.d.) discusses two niche strategies that can be considered in order to endure the competition.

The first niche strategy is *geographical specialisation.* That is to say, focussing on a specific geographical area to operate, away from any alliance competition. However, this is easier said than done, because an alliance airline can easily penetrate the market in which the non-allied carrier is operating. Allied airlines can even add a 'hub' and enter the routes on which the non-allied airline is operating. As the allied airline has connections to outside the local market area, routes to outside the market (and beyond) are offered. As a consequence, passengers are more likely to choose the allied airline, because of more route possibilities. So, it can be argued that the non-allied airline still cannot avoid the competition by using this strategy. Figure 4.2 shows this niche strategy in four phases. In the first phase, the non-allied airline (blue lines) starts its geographical specialisation. In the second phase, the allied airline (green lines) starts operating to the hub of the non-allied airline. In the third phase, the allied airline starts using the non-allied airline's hub also as its own hub. Eventually, in the fourth phase, the allied airline completely takes over the network of the non-allied airline. Even though, the only opportunity for the non-allied airline to be effective in this situation, is to join the alliance. Consequently, it will be the 'local

champion' of the alliance, as Kleymann (n.d.) describes. That is to say, serving the alliance in a specialised geographical market.

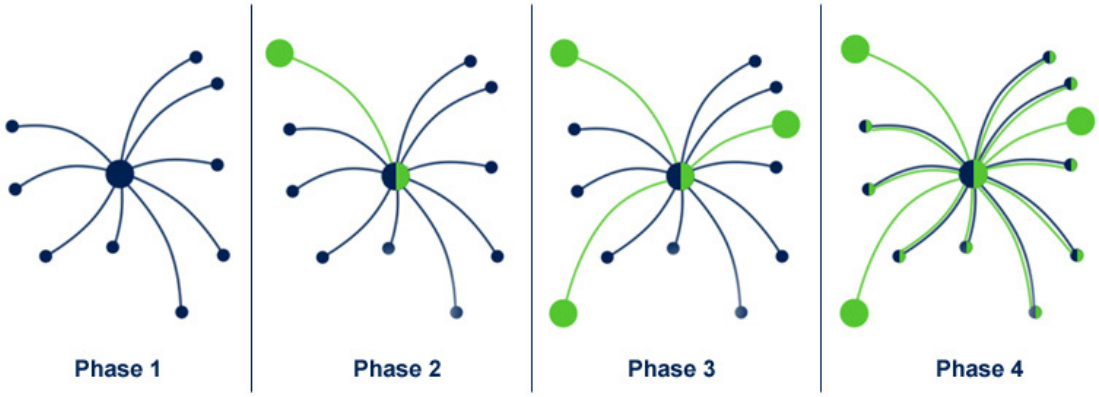

Figure 4.2 Intrusion of geographical specialisation
Source: compiled by the author

A second niche strategy, according to Kleymann (n.d.), is to apply *functional differentiation*. That is to say, changing the core concept of the airline. For example, changing to a low-cost structure with no-frills service, as low-cost airlines of this type, such as Easyjet or Ryanair, are not yet active in the alliance market. As said before in the chapter on low-cost carriers, a homogeneous price structure is needed in order to be competitive to the established airlines that are active in an alliance.

4.5 Future of low-cost airlines

Different point of views exist as the future of low-cost airlines is concerned. In Barbot (n.d.), according to a study of Alamdari & Mason (2006), it is argued that more concentration and fewer airlines are likely to be a trend in the future. In 2015, a growth of over 50% is expected of the demand for flights within Europe. Moreover, it is argued that only two or three low-cost airlines will dominate the market. That is to say, a market in which Easyjet and Ryanair control; the latter having a very powerful position.

According to Bhatti et al. (2010), it is estimated that there will be more investment in the low-fare business. Besides, low-cost airlines are likely to become more attractive for business travellers, because of the attractive low fares. Moreover, it is argued that low-cost airlines will continue to increase a positive cultural and social change in the future, because of the increase of destinations (Bhatti et al., 2010). That is to say, because of the lower fares that are offered, more

people get the opportunity to see more cultural aspects of the continent and are more easily connected to each other. Furthermore, it is said that low-cost airlines are likely to spread more the entire world. Especially Asia Pacific, Middle East and South Asia are currently experiencing a rapid growth in the number of low-cost airlines (Bhatti et al., 2010). What is more, a clear direction can be seen in the future of low-cost airlines, according to Bhatti et al. (2010). Customers are more and more likely to choose low-cost carriers, or for airlines that have a comparable marketing policy (Bhatti et al., 2010).

4.5.1 Ryanair: a future perception

It might be interesting to see how low-cost airlines will develop and change their services in the coming years. In order to demonstrate this, the Irish low-cost carrier Ryanair will be taken as an example.

As seen before, a considerable number of fees are used by low-cost airlines, especially by Ryanair. The company's CEO, Michael O'Leary, argues that fees are needed to keep the prices of seats low. What is more, he is of the opinion that, within a couple of years, all of the seats on board are free. However, he states that, on the other hand, passengers will be charged for various things, such as 'gambling on board' and in-flight entertainment (Telegraph TV, 2009).

Furthermore, Ryanair has the intention to remove two of the three toilets in the back of the aircraft, in order to insert an extra row of seats. According to Michael O'Leary, when six extra seats are placed in the back of the airplane, the ticket price can drop by 4% for every passenger. O'Leary argues that it is of high importance to get fewer people that are making use of the toilet. He states that the only solution for this problem is to charge people for making use of toilets. As a consequence, people are more likely to go to the toilets which are located in the airport terminal before their flight, which averagely does not last more than one hour and fifteen minutes (Telegraph TV, 2009).

Besides, the Irish airline also has the intention to insert a standing room at the back of the aircraft, with only handrails. During a press conference he explained that some days of the week these places will be free of charge. Even though, on some days, for example around the weekends, the price for travelling in the standing room will not be higher than five pounds. However, it is argued that it is a risky operation, involving many safety facets. The European Aviation Safety Agency (EASA) claims that this plan is in contravention of the aviation laws. The agency argues that a seat is required for each person that is aged two years or more (Breaking Travel News, 2010). Besides, the UK's Civil Aviation Authority (CAA) states that the safety conditions of the EASA include rules on restraint during take off and landing and during turbulences (Breaking Travel News, 2010).

Until now, low-cost airlines are mostly fixed on short haul operations, that is to say flights up to four hours. According to Francis et al. (2006), there are two main reasons for limiting to the short haul market. First, because of the regulatory circumstances of long haul services. Second, because some low-cost features are less suitable with long haul flights, e.g. food services, seat pitch and entertainment (Francis et al., 2006). In the United States, there are a number of long haul flights that are operated these days. Trans-USA flights, e.g. San Francisco – New York, are operated by US low-cost airlines Southwest Airlines, which last more than four hours (Southwest Airlines, 2011). Ryanair has also the intention to operate long haul flights in the future. However, during a press conference in Germany, Michael O'Leary states that, unlike on short-haul flights, there will be a two-class configuration on long-haul flights. On the one hand, this configuration consists of an economy class, which is expected to cost not more than 10 euro's. And, on the other hand, a business class will be included, which will be considerably more expensive. What is more, O'Leary argues that low-cost and no-fills service by itself will not work: *"there will always be 10 or 15% of the market who will pay whatever it costs for a business class service with a wide seat"* (Flightmag TV, 2008). Furthermore, it is said that Ryanair will, as it already does in Europe, serve secondary airports across the Atlantic in order to save costs (The Times, 2007).

4.6 Full service for lower fares

One can ask oneself whether it is possible to combine low-cost ticket fares and (full) service. Even through it seems like a 'mission impossible', there exist low-cost airlines that include service in their low price, for example Air Berlin. This German carrier offers full service – that is to say, free meals and free drinks – while offering low ticket prices, which is quite a unique combination (Air Berlin, 2011). Besides, in the past, there has been a Dutch airline called 'V-Bird' that offered low-fare flights with a full flight service. Their philosophy was: "Combining service, comfort and friendliness with low-fare tickets". That is to say, the airline's aircraft were equipped with seats that had a leg room of 32 inch, instead of the regular 28 inch. However, this implies less seats that can be placed in the aircraft and, thus, fewer passengers that can be transported. Besides, the airline only flew to 'primary airports', unlike other low-cost airlines that mainly serve 'secondary airports' (Hogeschool Rotterdam, n.d.). Nevertheless, the airline did not sustain very long. As it started its operations in October 2003, its flights were suspended exactly one year later, in October 2004 (Economy Point, 2006). So, there are only a few examples of airlines that operate (or have operated) this type of full-service strategy.

4.7 Low-cost alliances

Apart from low-cost airlines offering full services, it can be argued whether low-cost alliances, with the same base as regular alliances, will be created in the nearby future. According to Kleymann (2006), there is currently no necessity for a low-cost alliance. First of all, because all extra services that come across with an alliance, are not expected by customers that fly low-cost airlines. Passengers expect the service to be as simple as possible, just to a ticket from A to B. Second, simple and cheap reservation systems are used by low-cost airlines. In most cases these systems only comply with the desires of one airline, so there are many different unique reservation systems. In a case of an alliance, all these separate systems have to be combined, which can cost considerable sums of money (Kleymann, n.d.).

Even though, there are low-cost airlines that join an existing alliance. For example, Air Berlin joined the Oneworld alliance in 2010 (Oneworld, 2010). However, as said before, Air Berlin is not a full low-cost airline, as it offers a regular service on board. Besides, it has a network that mainly serves primary airports, as opposed to Ryanair. In addition, Air Berlin also has its own frequent flyer programme, which is now integrated in the alliance (Oneworld, 2010). It can be said that Air Berlin is not a real low-cost airline, but a 'semi-low-cost airline' that only offers low fares. So, it can be argued that 'die-hard' low-cost airlines are not likely to join an alliance in the nearby future, because of their unique selling structure that will not fit competing airlines.

4.8 Conclusion

It can be first concluded that a clear trend of consolidations exist between airlines, especially in Europe, North America and South America. As for airline alliances, it can be said that these are likely to become more heterogeneous in the future by including feeders and integrated feeders in the alliance. As a consequence, more routes are offered, especially to regional airports. Furthermore, it can be argued that alliances wish to have a more exclusive network, so that routes are proposed that are not offered by any other alliance. Besides, it can be concluded that not all airline markets are willing to join airline alliances or are wanted by alliance to join their group. The main reasons are, first, the non-allied airline's competitive business strategy and, second, the overlapping route network. So, at this time, it can be said that there is not added value for alliance to include these types of alliances. Moreover, it can be argued that non-allied airlines will suffer from allied airlines in the future. However, by applying functional differentiation, non-allied airlines can isolate from airline alliances. As far as the future of low-cost airlines is concerned, more concentration and fewer airlines are likely to be a trend. Besides, it can be said that low-cost

airlines will be more attractive for business travellers as this group will be focussing more on advantageous ticket fares. It can be concluded that more low-cost airlines will be created across the globe and that customers are likely to choose more for this group of airlines. Furthermore, it can be argued that 'die-hard' low-cost airlines will not add full-service features to their strategies, as it does not fit in the carrier's. However, it is seen that an all-inclusive service is offered by some 'semi-low-cost airlines' while proposing a low ticket fare. As for low-cost alliances, it is not likely that these groups will be created in the nearby future. First, because there is no demand for these groups. Second, it would be a large investment, as only because of the unique reservation systems that low-cost airlines have. So, it can be concluded that airline alliances will have more local airlines included in the future to extend their network on a local basis, affecting the business of the non-allied airlines. Besides, as far as low-cost airlines are concerned, it can be concluded that, in the future, the number of low-fare carriers on a continental scale will decrease. Even though, these types of airline will be seen more and more across the world. Last, it can be concluded for low-cost airlines that neither low-cost carriers providing full service, nor low-fare alliance can be expected in the nearby future.

Conclusion

The findings in this paper show that airline alliances have been growing rapidly in the last twenty years. After the creation of the first global alliance in 1997, more and more airlines were eager to join this type of cooperation. These days, three major airline alliances dominate the airline industry: Star Alliance, Oneworld and SkyTeam.

It can be concluded that nine types of alliance agreements can be distinguished. Some of these agreements are focussing more on just one specific part of the business strategy. However, other agreements imply the entire business strategy of both airlines.

Besides, it can be concluded that there are eight advantages to join an alliance. Three from a company's perspective and five from a customer's perspective. It can be argued that sharing facilities and the increase of passenger traffic are the most important advantages for an airline to join an alliance. Customers benefit as well when an alliance is joined by an airline. An enlarged network and seamless connections are seen as the most significant benefits for customers. What is more, frequent flyers of an airline that joins an alliance will profit from lounge access and from 'miles programs' of other airlines that are connected to the alliance.

Since the start of low-cost airlines in the USA in the 1970s, low-cost airlines have been created rapidly. It can be concluded that there are several differences between established airlines, whether these are allied or non-allied. As low-cost carriers focus more on cost-efficiency, costs are saved as much as possible. This effects their business strategy in various ways. It can be said that the main difference between established and low-cost airlines lies in terms of fare management. As established airlines offer an extended network with transfers possibilities, low-fare carriers only propose 'A to B connections'. Moreover, it can be said that regular airlines more often show their all-inclusive prices than low-cost airlines do. The latter does not generally show more than their basic fares, displaying the extra charges at the end of the booking process. Furthermore, the use of secondary airports, the outsourcing of handling, a one-class configuration and the abolishment of included catering are one of the other fundamental cost-saving techniques that are used by low-cost airlines. Besides all these differences, it can be said that fuel prices and on-board safety are one of the factors that cannot (or hardly) be influenced.

As far as the future of the airline industry is concerned, an obvious trend of consolidations between airlines can be observed. Airline alliances are likely to become more heterogeneous in the future by including more regional airlines into their alliance. As for low-cost airlines, more concentration and fewer airlines due to competition are likely to be a trend in the future. The creation of low-cost alliance is likely to be out of the question. Moreover, the idea of 'die-hard' low-cost airlines offering full service seems to be excluded.

So, it can be concluded that there are plenty of reasons for an airline to join an alliance. Not only this is beneficial for themselves, but also for their customers. Besides, it can be concluded that airline alliances offer numerous advantages in order to make the customer's journey as complete as possible. However, it can be said that low-cost airlines are operating more cost-effectively on many fields than established airlines in order to offer the customer attractive prices.

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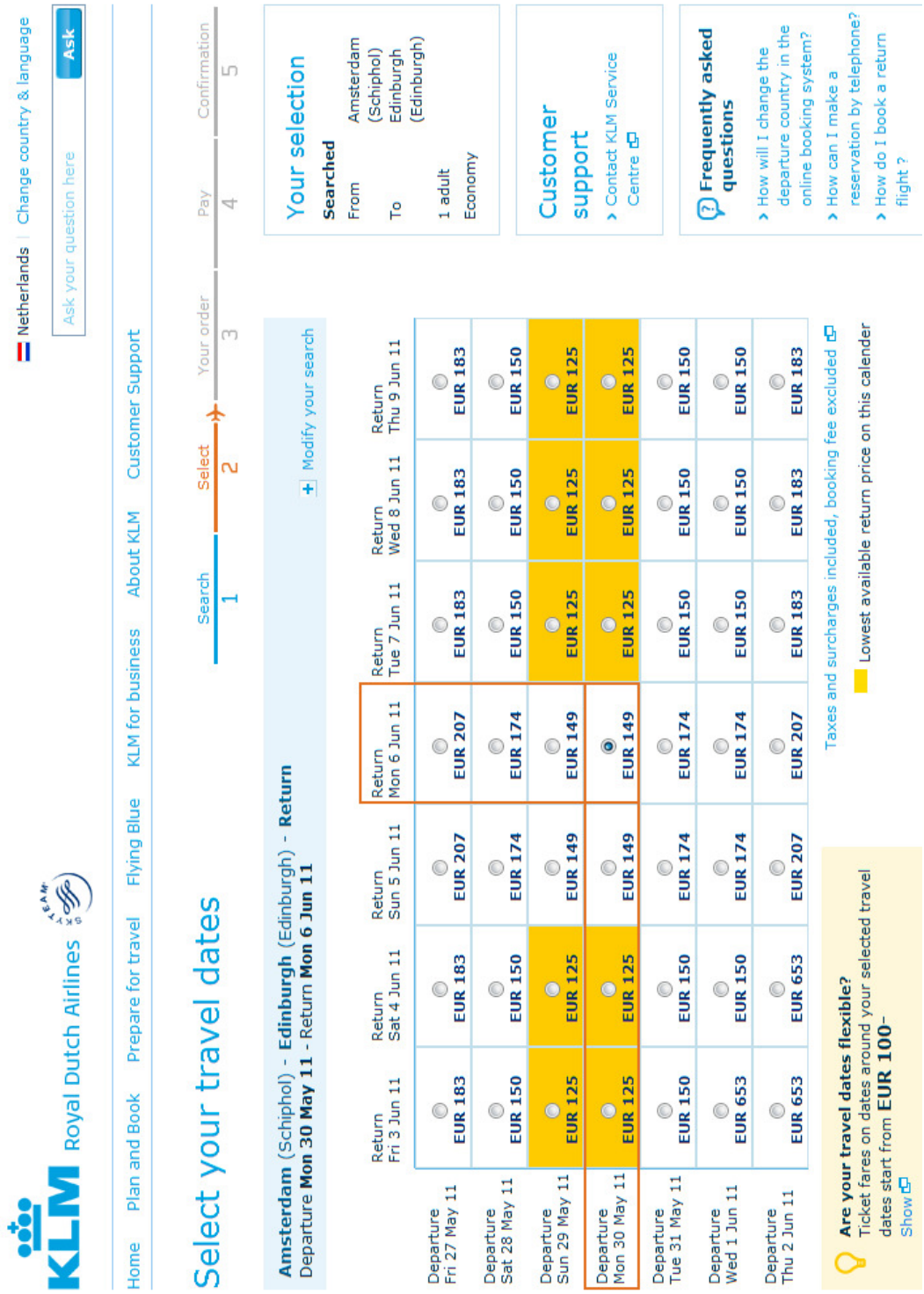
Appendices

Appendix A: KLM Booking process



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Select flights

Search 1 | Select 2 | Your order 3 | Pay 4 | Confirmation 5

Amsterdam (Schiphol) - **Edinburgh** (Edinburgh) - **Return**
Departure **Mon 30 May 11** - Return **Mon 6 Jun 11**

Modify your search

Saved flights

Departure Monday 30 May 2011

Show flights: All departure times

Price	Departure	Arrival	Travel time	Operated by	Flight number	
EUR 139	08:05 Amsterdam	08:30 Edinburgh	1h25	KLM	KL1277	Details
	Please note: only 2 seat(s) available at this price					
EUR 81	10:00 Amsterdam	10:25 Edinburgh	1h25	KLM	KL1279	Details
	Please note: only 3 seat(s) available at this price					
EUR 106	12:25 Amsterdam	12:50 Edinburgh	1h25	KLM	KL1281	Details
EUR 81	15:15 Amsterdam	15:40 Edinburgh	1h25	KLM	KL1285	Details
EUR 139	17:15 Amsterdam	17:40 Edinburgh	1h25	KLM	KL1289	Details
EUR 81	21:10 Amsterdam	21:35 Edinburgh	1h25	KLM	KL1293	Details

Taxes and surcharges included, booking fee excluded

+1 Next day Lowest price on this page

Return Monday 6 June 2011

Show flights: All departure times

Price	Departure	Arrival	Travel time	Operated by	Flight number	
EUR 78	06:05 Edinburgh	08:35 Amsterdam	1h30	KLM	KL1276	Details
	Please note: only 3 seat(s) available at this price					
EUR 171	09:10 Edinburgh	11:40 Amsterdam	1h30	KLM	KL1278	Details
	Please note: only 2 seat(s) available at this price					
EUR 136	11:15 Edinburgh	13:40 Amsterdam	1h25	KLM	KL1280	Details
	Please note: only 3 seat(s) available at this price					
EUR 171	13:35 Edinburgh	16:00 Amsterdam	1h25	KLM	KL1282	Details
	Please note: only 1 seat(s) available at this price					
EUR 171	16:35 Edinburgh	19:05 Amsterdam	1h30	KLM	KL1286	Details
EUR 136	18:25 Edinburgh	20:55 Amsterdam	1h30	KLM	KL1290	Details
	Please note: only 3 seat(s) available at this price					

Taxes and surcharges included, booking fee excluded

+1 Next day Lowest price on this page

More information about the fare structure
A low fare or greater flexibility? The choice is yours.

Price departure flight	EUR 80,57
Price return flight	EUR 77,51
Total price for 1 adult Taxes, surcharges and booking fee included	**EUR 158,08**

Your selection

Searched
From: Amsterdam (Schiphol)
To: Edinburgh (Edinburgh)
1 adult
Economy

Selected dates
Departure: Mon 30 May 11
Return: Mon 6 Jun 11

Do you need more time?

Take an option on a flight and fare for a maximum of 14 days.

For **EUR 10,00**

Time to think

Customer support

› Contact KLM Service Centre

Frequently asked questions

› Can I check departure and arrival information on the website?
› Can I track flights on the KLM website?