

Shift in Picks and Shovels

During the gold rush in the nineteenth century not the gold diggers but the suppliers of the picks and shovels were making the money. When drawing a parallel to the aviation industry there can be said that everybody in the industry is able to make money but the airlines. At the moment there are several developments in the industry, which can make a shift possible that can be favourable for the airlines.

By Jasper Spruit

In both the United States (US) and Europe is the hub and spoke system in the early evening of a transformation. This is mainly caused by a situation where the hub carriers are witnessing losses and the point to point operators (mainly low-fare and regional airlines) manage to make profits. In the US deregulation led to hubbing, where in Europe hubbing is originated due to the regulation. But both in the US and in Europe developments are disturbing the effectiveness of hub and spoke system.

Without trying to be complete two influential developments will be mentioned. First, the growth of the number of low-fare airlines. In both the US and Europe are the feeding and defeeding operations of hub operators among other things influenced by the rise of low-fare airlines. These airlines serving short distances for low fares on the main continents and "disturbing" the (de)feeding markets of the hub carriers. It is well known that the hub carriers are loosing money on the short (feeding) operations. The second factor are the developments in regional aviation. These developments are twofold. First the technical development of the regional jet, which makes it possible to fly longer distances at a higher speed. Due to the technical development hub bypassing is more effective than it was a few years ago. This causes the second effect, business passengers are more and more realising that flying via a hub is more time intensive than using smaller regional airports with less

congestion (both in the air and on the surface), smaller terminals, etc. Several American analysts noticing that despite the crisis, regional jet flying continued to grow. Airlines are more and more seeing the pros of using smaller regional jets. An example was given in the May edition of *Airline Business* (May 2003): Delta Airlines was loosing on one route approximate \$ 1600.- per flight operating a 118-seat Boeing 737-200, carrying on average 76 passengers. When the Boeing was replaced with a 50-seat regional jet, the result was an average load of 43 passengers and a \$ 721.- per segment (from a to b) profit.

The ticket price went up and the 33 passengers not accommodated at the flight were going to the low-fare airline serving the same route. The benefits for this one route extend to three parties: Delta Airlines, the regional airline and the low-fare airline.

In Europe several airlines also discovering the possibilities of regional aviation. Swissair noticed for example the possibilities a few years ago. In order to lower the costs of the feeding operations Crossair (former biggest European regional airline) was built out to a (de)feeding airline. Crossair operated its own hub on Basle and served the European market. In 2001 Crossair carried 1,89 million passengers. Crossair used regional jets with lower cost than the Airbus operations of Swissair and was thus able to operate a European network with lower cost.

While the main hub carriers are loosing money on the (de)feeding operations, the low-fare airlines that mainly use smaller regional airports and avoiding the hubs are getting more and more business passengers out of the hub market. In order to lower the cost of the (de)feeding operations of the hub and spoke



Delta Airlines Boeing 737-200

system regional airlines are used for this operation. But due to the congestion in the European skies and the lack of slots the main hub airports do not like to serve regional jets.

Finally cities and regions are realising that the connectivity of the region can be a very important factor on the development of the economy. And thus are more and more interested in the possibilities of aviation and making linkages to other regions. Airlines are getting invitations of public authorities to start a service on their airport. Several airlines are realising their new position in this demand and exploiting this new and relatively strong bargaining position. See for example the discussion of the Ryanair Charleroi deal. Only one point-to-point link to the regional airport is not necessary interesting for the regional airport and its region, but a link to a main hub with good connection times to other destinations can be very valuable.

If the developments are taken together the expectation is that regional airlines will be used for (de)feeding hubs with thinner routes in the future. While the more congested routes still will be served by the hub carriers. This means that the hub carriers will lose the strong position they originally had. The developments of regional aviation and the demand of cities for links to the world will be so strong that the operators of point-to-point services will become the strong party in negotiations and will be able to make more money in the near future.

In the aviation industry where only the suppliers of the 'picks and shovels' are making money this development can mean an important shift.

Sources
Airline business, May 2003

This article is read by some people with strong interests in the aviation industry. Here after is asked for their comments and vision about this issue.

[Prof dr Hugo B Roos; Erasmus University Rotterdam – Economic Faculty:](#)

The aircraft manufacturers can be seen as the shovels' parallel. However, given the airline industries' dependence upon the movements of the business cycle it is important to note that even the aircraft manufacturers have great difficulties to survive. Only with help of governments and after a process of mergers the manufacturers are now able to survive. Regional airlines are niche players, emerging from remote places where traditional airlines were not interested in. In recent years, especially after September 11, 2001 the regional airlines offer an unexpected advantage over traditional hub airlines: more transparent and safer security procedures and smaller aircraft promising a better sense of security than larger aircraft used by traditional airlines.

[Drs. Jan-Willem Perdon; Manager Operations Department & VP; Rotterdam Airport BV](#)

It cannot be denied that - as stated in the article - there are several developments within the aviation industry. Apart from the entry of the low fare airlines, which definitely has a major impact on the traditional airlines, the way of travelling by air within regions is in a transformation process. As said, the introduction of the regional jets is a fact. In the old days people who wanted to fly from A to B in Europe in most cases always needed to travel to a hub or mainport first to make this possible. For airlines this was the easiest way, because they could concentrate their means at the mainport, while it was the passengers' "problem" how to get to the airport and how to get into the region from the airport at the destination, no matter how much time and inconvenience it took. This traditional "supplier driven" market is now changing to a "demand driven" market, the so-called system of "hub bypassing". People who need to travel within a region are more and more asking for convenient and time saving solutions. It is proven that people living or working within about half an hour from a regional airport are saving many hours when compared to travelling by way of a mainport (in

most cases at least 50% or even more of the total travelling time from door to door). People more and more see the advantages of using a regional airport. Airlines should have a response to this development and jump into this market by increasing their operations from regional airports. Of course the mainports will keep a major role as a hub for intercontinental connections including the necessary hub-feeders. The development of the hub bypassing trend will definitely stimulate economic growth in the city and region where the regional airport is located, simply because the importance of the regional airport as a port of entry will increase. This will lead to more consumption in the region. In another way more passengers will lead to more aviation business and generate (in) direct employment in the region.

[Simon Breedveld; Managing Director, Air Agencies Benelux](#)

The tendency of the article is that the regional airport (specifically Rotterdam Airport) will profit from the new developments in the aviation. The new generation regional jets will make it possible to operate from the regional airports with thinner lines (markets) and to offer tailor made products and solutions for the business man.

This development is the aim of the local Rotterdam policy as the management of Rotterdam Airport. This means that this article is almost written about the strategy of Rotterdam Airport. If you place this parallel to the strategy of Rotterdam Airport to avert aggressively driven low-cost airlines as Ryanair we can conclude that the chosen strategy is the right one.

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