A Questionnaire Survey on the Impact of Alliances on Airline Operations

Regulatory restrictions on market access, ownership and control have pushed airlines toward the formation of strategic alliance groupings. Although alliance grouping is not the optimal solution, it does harness the airlines against the instability of the sector and enable them to reap as many benefits as possible. This questionnaire survey researches how airlines judge their alliances, given such dynamics in the airline industry, the current crisis caused by the slowdown in the economy, and the 11th September events. More specifically, a study is conducted on how airlines perceive the impact of alliances on their operation in general and on passenger traffic in particular. In addition, we look to how different types of partnership agreements and different types of routes have affected the results, and if airlines of different size, operating from different region and belonging to different alliance groupings have been affected differently.

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In the age of globalisation, world's airlines are under pressure to offer both seamless global service, enter new markets and be flexible enough to adapt quickly to the economic environment and the changing customer needs. Thus, airlines have proceeded with the creation of alliances, which have radically changed the air transport industry structure, so as to enable themselves to cope with the inherent instability of the sector and to reap as many benefits as possible.

The majority of airlines are interested to extend their network beyond the markets they currently serve. However, due to regulatory restrictions on market access, ownership and control, they have been pushed towards the formation of strategic alliance groupings. Legislation aimed at protecting national interests has meant that it is virtually impossible to acquire a controlling interest in airlines in countries or trading blocks outside those in which an airline is owned and operated. Thus, airlines turned also to alliances to skirt rigid regulation.

There has clearly been a surge in formation of alliances amongst airlines in recent years. A large number of airlines have established or joined one of the four global airline alliances: " Wings" (1989)[1], Star Alliance (1997), Oneworld (1998), SkyTeam (2000) – and they now control, as allied partners, 56% of world Revenue Passenger Kilometers (Airline Business, September 2002).

Survey background

The heads of the alliance departments of all airlines – that is 28 carriers at the time of this survey – belonging to the alliance groupings of Star Alliance, "Wings", Oneworld and SkyTeam were contacted and agreed to participate in a questionnaire survey.

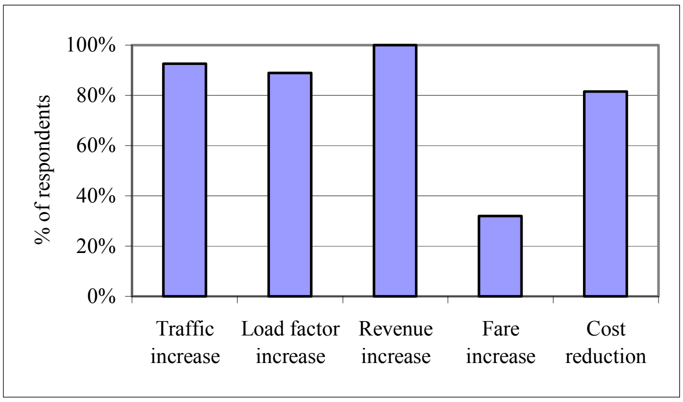
Given such dynamics in the airline industry and the current crisis due to the slow down in the economy and the 11th September events, it was of interest to assess the following:

- How do airlines perceive the impact of alliances on their operation in general and on passenger traffic in particular?
- How different types of partnership agreements and different types of routes have affected the results?
- Have airlines of different size, operating from a different region and belonging to different alliance grouping been affected differently.

The general impact of alliances on airlines operation

In general, the participation in alliances is considered successful. While one third of participants rate their alliance cooperation as "excellent", the rest believe that the course and operation of the alliances has been so far "good". A number of European regional carriers expressed some reservations and took a neutral stance.

Figure 1: Impact of airline alliances

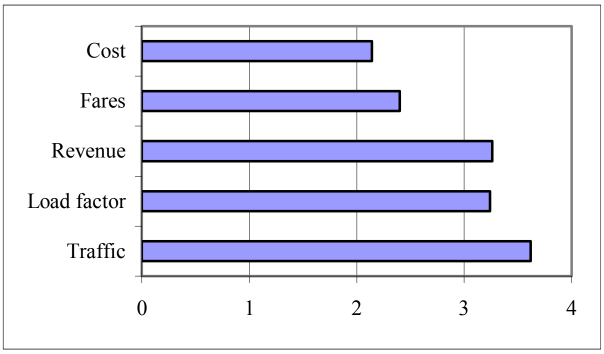


[1] Date of alliance formation

Almost all participants believe that their alliance participation has led to an increase in traffic, load factors, revenue and some reduction in costs. While two thirds of the participants expressed the opinion that fares have not been influenced, the rest declared that fares on routes operated jointly by partners have increased.

To establish the degree of the impact of alliances on airlines' operations, the respondents were asked to rate the impact from 1 to 5, with 1 referring to "no impact" and 5 to "significant impact". As it can be seen in figure 2, the most pronounced effects have been experienced in the area of passenger traffic followed by revenue and load factor. The least pronounced impacts have been observed in the areas of costs and fares, perhaps because any significant long term cost reductions/synergies require the alignment of some product specifications – such as common fleet planning, IT system harmonisation – , which not only takes some time and a high degree of integration but also needs a major commitment from the allies.

Figure 2: The degree of alliance impact on airline operations



Scale of 1 to 5, 1= no impact and 5=significant impact

Impact of airline alliances on passenger traffic

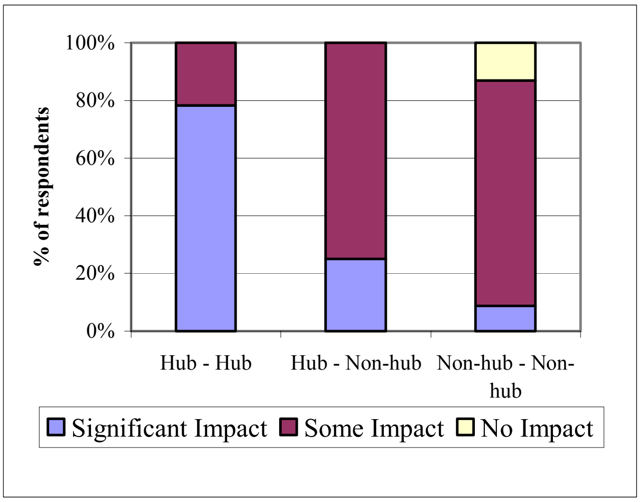
The benefits airlines have experienced from their participation in airline alliances have mostly taken the form of increase in traffic. Almost 90% of respondents claimed that they experienced an increase in traffic within one and two years from the inception of their partnerships, but they believe that this increase tends to stabilise a few years after the launch of the alliance. Although it was widely held that it is the airlines attempt to provide a seamless travel that has caused the increase in passenger traffic, the respondents attribute this upsurge to the provision of joint frequent flyer programmes (FFP).

The impact of alliance on traffic by route type

The greatest increase in passenger traffic was observed primarily on hub-hub routes, and secondarily on hub-non hub routes. The increase in passenger traffic on the hub-hub routes was assessed as "significant", with 45% of the respondents experiencing an increase of more than 16%, while the corresponding percentage increase for hub-non hub routes ranges from 6 to 15% according to 52% of the respondents; as for non hub-non hub routes, all respondents have assessed the traffic increase as moderate, with the percentages equally divided between the 0-5% and the 6-15% brackets. These results seem absolutely reasonable considering that all global carriers, especially the major ones, operate on the hub-and-spoke system and the whole alliance organisation aims at increasing the hub-hub traffic, especially on the high-yielding and efficient transatlantic routes.

International major carriers, including all the American airlines, many of the European and South American carriers claimed that alliances have had a significant impact on their hub-hub routes. The American and European carriers were the first to implement the hub-and-spoke system. However, Asian carriers claimed only a moderate increase on their hub-hub routes, probably because these carriers have not exploited their hubs operation to the same extent as their counterparts in the US and Europe. Furthermore, the US and European partners have benefited, in most cases, from antitrust immunity which allows them to harmonise their operation more effectively.

Figure 3: Alliance impact on traffic by route type

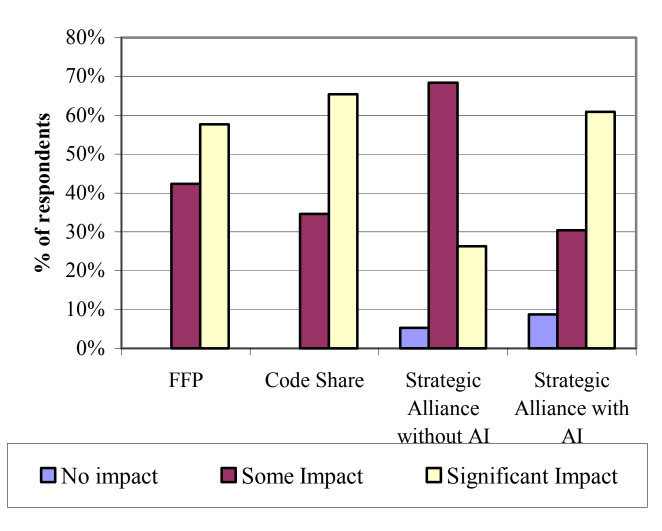


The impact of alliance on traffic by type of co-operation

Among the chosen types of cooperation, that is FFP, Code share, Strategic Alliance with antitrust immunity and Strategic Alliance without antitrust immunity, it is code share and strategic airline alliances with anti trust immunity that seem to be regarded as the most efficient form of cooperation by the airlines themselves without disregarding the significance and contribution of the other two. Several respondents also stressed that the impact of antitrust immunity is just beginning to unfold but they consider it as a very important element as it provides airlines with the ability, flexibility and possibility to coordinate their activities in scheduling and pricing. A few airlines stressed that they have experienced negative impact from "Strategic Alliance without antitrust immunity". A very small number of Asian carriers believe that strategic alliances have no impact on traffic. It results from the above that Strategic Alliances are evolving in a risky and uncertain environment in which airlines are demanded to make a commitment without being certain of the future evolution of the alliance.

The provision of joint FFP is considered very effective in boosting traffic. Most of the times FFP and Code Share co-exist and constitute a much more common form of cooperation than Strategic Alliances whether with antitrust immunity or without antitrust immunity.

Figure 4: Impact of type of airline cooperation on traffic

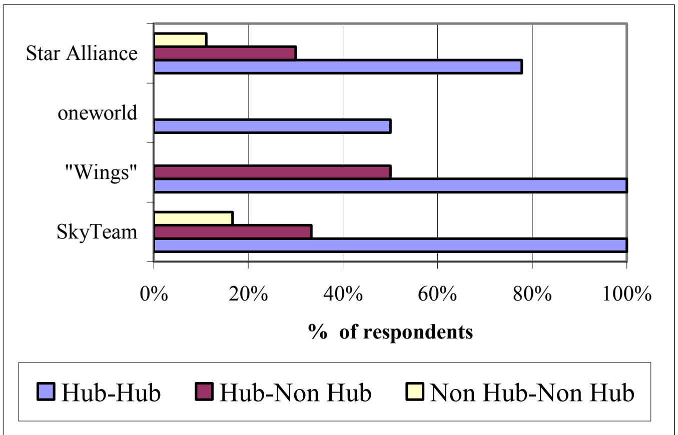


The impact of alliance on traffic by alliance groupings

SkyTeam members seem to be the most satisfied with the alliance performance followed by Star Alliance members. No member of the oneworld alliance has rated their alliance cooperation as "excellent" and this alliance has the only carrier that has taken a neutral attitude towards alliances, probably because of the lack of deeper cooperation among the members. This by alliance comparative review points out that antitrust immunity is a major parameter for the success of an alliance as far as traffic is concerned.

Almost all members of SkyTeam and "Wings" believe that the most significant increase in traffic has taken place on their hub-hub routes where as the corresponding percentage for oneworld and Star Alliance is 50% and 80% respectively. "Wings" has experienced the highest increase on hub-non hub routes. As "Wings" is made up of only two carriers, it is difficult to compare it with the other alliances whose membership ranges from 6 to 13 members.

Figure 5: The alliance impact on traffic by alliance groupings



"Wings" appears to have experienced the most positive impact in all aspects of operations. SkyTeam has registered considerable increase in traffic and revenue, which may be due to the deeper cooperation existing among the partners of this alliance.

Table 1: Impact of alliances on airlines operations by alliance groupings

	SkyTeam	Wings	oneworld	Star alliance
Traffic	3.8	5.0	3.5	3.3
Load factor	3.3	4.5	3.0	3.1
Revenue	3.8	4.5	2.7	3.0
Fare increases	2.0	3.5	1.8	2.1
Cost reductions	2.0	3.0	2.8	2.3

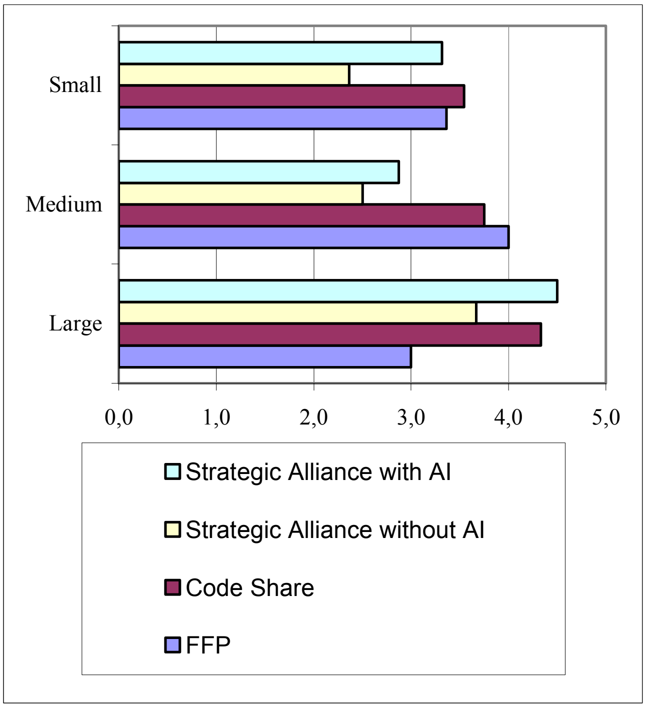
Scale of 1 to 5, 1= no impact and 5=significant impact

The impact of alliance on traffic by airline size

Large airlines, in general, seem to be satisfied with their alliance cooperation, even if with some reservations, with two thirds stating that their partnerships are "good" and only one third viewing them as "excellent". The majority experienced the increase in traffic in the first year of launching their partnership. Almost half of the large carriers have experienced an increase in traffic amounting to about 5% increase, mostly on their hub to hub routes. They believe code sharing and strategic alliance with antitrust immunity have a significant impact on traffic, scoring them as 4.3 and 4.5 respectively on a scale of 1 to 5.

While medium sized airlines are generally satisfied with their alliance cooperation, small carriers have expressed some reservations. This could be due to their rather limited influence on the decision-making mechanism within the alliance groupings. The medium and small carriers have also recorded some increase in traffic but it has taken them longer – up to two years – to experience the rise in traffic. A large proportion has experienced up to 15% increase in traffic, perhaps because their base of traffic is smaller than that of the larger carriers. It is interesting to note that medium and small carriers believe Frequent Flyer Programme cooperation and code share have had a significant impact on their traffic, which indicates that small and medium sized carriers benefit more by joining the large airline frequent flyer programmes.

Figure 6: The impact of the different alliance cooperation types on traffic by airline size

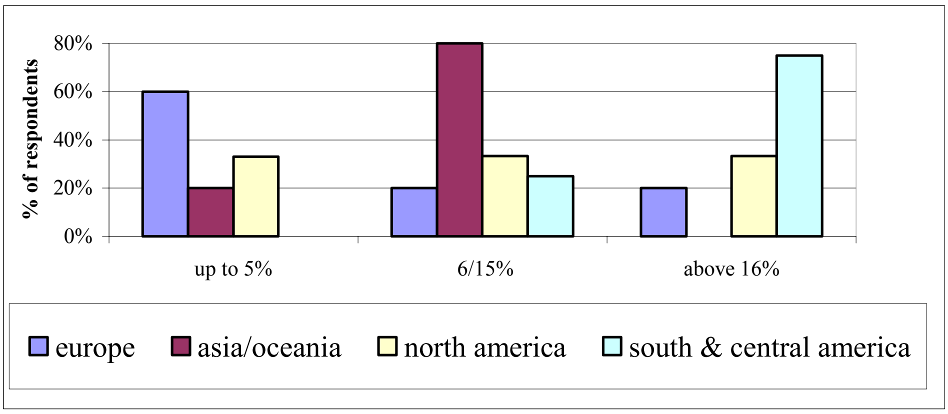


Scale of 1 to 5. 1= no impact and 5=significant impact

The impact of alliance on traffic by region

Central and South America has experienced the greatest increase in traffic, load factors and revenues as a result of alliances. Three out of the four carriers of this region entered alliances very recently and may be experiencing the initial positive alliance effects. This is the reason also why half of the carriers from this region – the highest percentage among all regions – characterize alliances as "excellent". The greatest increase in fares has been registered in Asia, whereas as far as costs are concerned, it is the European carriers that reported the most significant decrease. This can be explained from the fact that the carriers in Europe are among those that feel more pressingly the need to reduce costs. As was expected, the North American airlines followed by the European ones that have experienced the most significant positive impact from antitrust immunity since they had the majority of these exemptions.

Figure 7: Alliance impact on traffic according to geographical region



The figure beneath depicts how the carriers of the different geographical regions estimate the impact of the alliances they participate in on their traffic. It is the Central and South American carriers that seem to have experienced the greatest increase in traffic, which can be explained both by the fact that it is the area that is experiencing the greatest increase in traffic and by the fact that these carriers had a rather limited network before the establishment of the alliances. No airline of this region has recorded an increase lower than 6%. Asia and Oceania is the region that has stated the second greatest increase in traffic, with the majority of carriers stating an increase in traffic ranging from 6 to 15%. This geographic region includes many developing countries and has organized in these last years many important athletic events. European carriers have declared the lowest increase since the carriers from this region had well before the formation of the alliances an extensive network and numerous connections with all the other geographical regions of the world.

Conclusion

The overall conclusion arising from the questionnaire analysis is that alliances, despite the form of cooperation among the partners, entail numerous benefits for the airlines: alliances bring about a clear increase in the passenger traffic of the allies – and to this agree all the respondents – with a parallel increase in load factor and some reduction in costs. The impact on passenger traffic is considerable and has been experienced from one to two years since the inception of alliance cooperation. The increase in traffic has mostly been experienced on hub-hub routes. A clear improvement in revenue is observed, a fact resulting from the combination of the increase in traffic and the decrease in costs. The impact on costs, even though positive, remains comparatively limited at least on a short term basis. As regards the impact on fares, the situation remains rather hazy, since the majority of airlines have given ambiguous answers when asked to state whether there has been increase or decrease of fares.

The greatest benefits from alliances result from the more advanced and integrated forms of cooperation, just as the one that links the carriers of the "Wings" alliance, which is characterised by the existence of antitrust immunity and the establishment of a joint venture. Most alliances however, remain "strategic" only in name, at least at their present stage, basing their cooperation on Code Share and FFP coordination and have not proceeded to deeper integration.