AN ANALYSIS OF THE FORCES THAT DETERMINE THE COMPETITIVE INTENSITY IN THE AIRLINE INDUSTRY AND THE IMPLICATIONS FOR STRATEGY

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Abstract

The research analyzes the dynamic forces of competition and demonstrates that competition embodies the fact that it can appropriate value, and that management of the competitive tensions is central to strategy. The paper also demonstrates that the level of intensity in the industry is determined by basic competitive forces and through the organization's choice of strategy it can alter the impact of these forces to its advantage. Central to the paper is a series of realist appraisal of what is right and wrong with current industry thinking and practices. The research investigates, through a questionnaire, the why and how of decision making in the airline industry given the competitive environment of this industry. Data was coded into themes, ideas, topics and key words leading to an analysis which attempts to show that the two sides of competition create an interesting tension, the intensity and balance of which has major, often surprising implications for strategy. Despite the intensity of the airline industry rivalry, this research proves that an airline has latitude to influence rivalry through its choice of strategy. The results show that the airline business is dynamic and complex. Therefore effective strategy is separable from execution and is based on a match between capabilities and activities. The ability to anticipate and be innovative is a critical core competence. The net result of this rivalry and intense competition in the airline industry reflects in an overall slow market growth, margins driven down to unattractive levels and competitors chasing the same flighty customers.

Key words; competitive intensity, business environment, competitive strategy, competitive advantage, value addition.

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Background

Air travel has changed the way people live and experience the world today. The airline industry is a strategic sector that plays a fundamental role in the globalization of other industries as it promotes tourism, world trade, and foreign investment and, therefore leads to economic growth. However all airlines within the industry operate in a highly dynamic environment where various legal, social, technological and economic forces interact with each other, thus influencing their decisions and actions. The question is “what are the most feasible and attractive ways to enhance market access for airlines worldwide?” The ingredients come from the worlds of competition policy and international trade policy. Competition is a condition that every business must continuously recognize as it is a major factor in determining success or failure of the business. The strength of competition a business faces is called competitive intensity. The industry competitive intensity is determined by the number of competing firms, their competitive strategies and the industry competitive forces. In three decades of strategy research, a few in the literature dispute the premise that competition is central to a company’s performance. Much of the discourse in strategy is organized around barriers to competition.

Competition creates an interesting tension, the intensity and balance of which have major, often surprising, implications for strategy. The environment in which airlines compete does influence what the airlines can and cannot do.

Research Questions

This research explores the competitive environment facing the airline industry. The research is guided by research questions rather than research hypothesis. The questions include the following;

1. What have been the notable developments in the airline industry and how is the industry changing?
2. Is it appropriate for Airline management to routinely blame issues of; overcapacity, high fuel costs, government, deregulation, employees and

customers, for their failures?

3. Is the level of competitive intensity determined by basic competitive forces?
4. Is management of competitive tensions central to strategy?
5. What bedevils airlines: should they talk strategy or tactics and are customers likely to see one sound airline strategy?
6. Does competition embody the fact that it can appropriate value and does it ensure that passengers do not pay excessive fares?
7. What is really happening to the airline industry and what are the predictions as to what the next few years may hold for the airlines.

Significance of the research

The airline industry is a major economic force, by both its own operations and impact on related industries, such as aircraft manufacturers and tourism to name a few. Few other industries generate the amount and intensity of attention given to airlines, not among its participants but from government policy makers, the media and almost anyone who has an anecdote about a particular air travel experience. This research provides a foundation for understanding the economic aspects of competitive wars, including their antecedents, triggers, and consequences.

Who should be interested in the significance of this research?

1. Industry suppliers, consultants, and analysts who want to appreciate the inevitable business.
2. Educators, government officials, and business executives who are confused by the industry rhetoric and want an independent view of what is really happening in airline travel.
3. Independent agents who want to understand the challenges facing the airline

industry today and the opportunities these create.

4. Corporate travel managers who want to understand the fundamental financial, and customer service changes airline industry events will cause.
5. Anyone interested in a short and long term strategic outlook on airline travel.
6. Provides senior airline managers with novel approaches to key strategic issues, as the fundamental changes in the industry are throwing up some crucial strategic decisions on network configurations, sales distribution and relationships with other carriers.
7. Policy makers and managers in airlines, government departments, regulatory authorities and international agencies concerned with civil aviation. The policy makers issues will involve trade offs between pro and anti competitive effects, weighing of positive/efficiency enhancing effects against adverse effects flowing from increases in market power.
8. Students who might be interested or find this thesis useful are likely to be following courses in business, economics, management and tourism.

Source of the problem

Airline industry structure and overview

Today the global airline industry consists of over 2000 airlines operating more than 23,000 aircraft and providing services to over 3700 airports. The growth of world air travel has averaged approximately 5 % per year over the past 30 years. During much of its development, the global airline industry dealt with major technological innovations such as the introduction of jet airplanes for commercial use followed by the development of wide –body “jumbo jets”. At the same time, airlines were heavily regulated throughout the world, creating an environment in which technological advances and government policy took precedence over profitability and competition, an issue that will be addressed in this paper.

A well known authority in the field of air transport, Stephen Wheat croft in "Air Transport Policy Wheat croft 1964" , explained at the beginning of this book that the problem he encountered was keeping up with a constant flow of new material. Hardly a day goes by without the announcement of some new development in the airline industry. In the sixties the main concerns were with the reasons why governments needed to control entry to routes, the issue of capacity supplied by airlines, and the fares and rates charged. Today the focus of attention has shifted to deregulation, privatization, emergency of global carriers and problems posed by an increase in industrial concentration. The transition taking place in the airline industry has attracted some attention in the microeconomics and strategic management literature, which often contains a number of vignettes on the experience of airlines in the process of profound and continuous change. In many ways the airline industry provides a kind of test bed for theories on deregulation, contestable markets, alliances formation and many other issues.

It is true that there is always significant attention that the airline industry receives from the media, its customers and government policy makers. Despite this attention there have been relatively few comprehensive studies of airline management and competition related issues since the industry was deregulated in the US, in 1978.The few comprehensive studies that have been completed were mainly from government agencies and independent research institutions rather than universities.

What is already known about this problem?

Michael Porter, an authority on competitive strategy, contends that a company is most concerned with the intensity of competition within its industry. The level of this intensity is determined by basic competitive forces. The first step in structural analysis is an assessment of the competitive environment in which the company operates the basic competitive forces and the strength of each in shaping industry structure. The second is an assessment of the company's own strategy of how well it has positioned itself to prosper in this environment. To assess a firm's strategic position, its managers must collect and interpret data regarding the firm itself, its competitors, its stakeholders, and the industry. Having implemented a strategy based on that information, the managers further must measure the effects of that strategy. These are the issues which this research will be addressing.

Many of the published studies of airline competition and management are in the form of journal articles with examples like Levine's "Airline Competition in Deregulated Markets: Theory, Firm Strategy and Public Policy", Yale Journal on Regulation (1987) and Borenstein "The Evolution of U.S.Airline Competition". These studies of the changes in the airline industry that have occurred since deregulation have focused primarily on the economic impacts on market competition, consumer welfare, airline profitability. Therefore they tend to be aggregate studies of measurable outcomes and trends in airline markets and for the industry as a whole. This research will attempt to be more specific on how airline management practices have changed in the face of increased competition.

Other methods that have been tried to solve the problem.

1. Price and Non-Price Competition in the Airline Industry

In a study done by Philip G.Gayle of Kansas State University in June 21,2004, his results suggest that, on average, prices may not be as important as we think in explaining passengers' choice behavior among alternative products. Non price characteristics may include convenience of flight schedules, frequent flyer programs, the quality of in flight service, and travel agent commission such as override programs. In the paper no.93 "Competitive Advantage Through Innovative Pricing Strategies: The case of the Airline Industry", Andreas Knorr and Silvia Zigova, argue that complex pricing strategies alone are no guarantee for long term success in a very competitive business environment like the airline industry.

Normative models typically suggest that prices rise in periods of high demand and cost. However in the airline industry market, prices fall when demand or costs rise. This inconsistency occurs because the normative models assume that competitive intensity does not change with demand and cost conditions over time. Green and Porter (1984) assume that aggregate demand and competitor actions are unobserved, so when a firm faces low demands, it cannot distinguish whether this is due to price cutting by a competitor or due to low aggregate demand. Researchers typically assume that competitive intensity is invariant when the demand and cost conditions change. This scenario will be addressed with specifics to the competitive environment in the airline industry.

Yields of many airlines continue to be driven down by excess capacity, aggressive competition from the frills carriers, and a customer base demanding less restrictive/ simplified fare structures, making traditional network carriers bank more on their route market value.Todays air travel industry is highly competitive, volatile and dynamic, and needs understanding and quantifying customers purchase behavior. Despite the numerous non-price aspects of competition among airlines, the focus of policy makers is often on the potential price effects that various business decisions of airlines may have. Examples of airline business decisions that often concern policy makers include mergers and code share alliances among airlines.

Most literature typically assumes that competitive intensity is invariant when demand and cost conditions change. With this assumption, an increase in demand or cost will cause prices to increase. [Gatignon, Anderson and Helsen, 1989] content that whereas all elements of the marketing mix (product, price, promotions, and placement) can serve as competitive weapons in a war, price cuts have received most attention, particularly for their destructive consequences for firm performance.

2. Low Cost Carriers

On both sides of the Atlantic deregulation gave birth to a new type of airline the so called low cost carrier (LCC).The role model-US-based Southwest Airlines, grew from a fleet of just 3 Boeing 737 aircraft, 195 employees and 108,554 revenue passengers in 1971.Southwest Airlines is unique in the airline industry in posting an operating profit for

31 years straight, including the crisis year 2001 and 2002, when it did not lay off a single employee. By 2007 LCCs had control of a market share of around 14 percent in Europe.

While the business models of LCCs differ to a certain degree, they all share some basic features which contrast markedly with the traditional flag carriers network approach. LCCs offer non-stop point to point services to and from uncongested airports instead of connecting flight via a hub.LCC's specialize in short to medium range flights, deploying a highly standardized fleet with a maximum of two different aircraft types. With LCC's the fare only includes basic transportation in a single class cabin.

Passengers who wish to consume food or beverages have to purchase them on board at an extra charge. Productivity at LCC's is substantially higher due to systematic outsourcing.LCC's do not have costly frills like frequent traveler lounges or interline agreements. Distribution costs are minimized by bypassing computer reservations systems (CRS) and Travel Agents through direct selling via the internet and call-centers and by issuing no paper tickets. Low cost carriers can pose a serious threat to traditional "full service "airlines. A case study on passengers' perception of low cost airlines and full service carriers by John F.O'Connell and George Williams showed that direct competition between full service airlines and no frills carriers has intensified across the world. Information was obtained through passenger surveys which attempt to provide answers to questions on the key drivers of each airline's business model, the difference in passenger perceptions between low cost carriers and full service in cumbents, the particular reasons why a passenger chooses a particular airline model and how carriers can encourage passengers to return.

Numerous studies have confirmed that the low cost carriers (LCCs) have the ability to considerably reduce airfares in the markets where they operate and beyond. Most studies have used cross sectional snapshots of the industry to investigate the difference in fares between routes with and without LCCs at different points in time. Work by Windle and Dresner (1999), Morrison (2001), Ito and Lee (2004) presents compelling evidence that on average travelers on routes served by LCCs benefit from airfares that are considerably lower than those charged in routes where LCCs do not operate.

3. <u>Competitive Strategies</u>

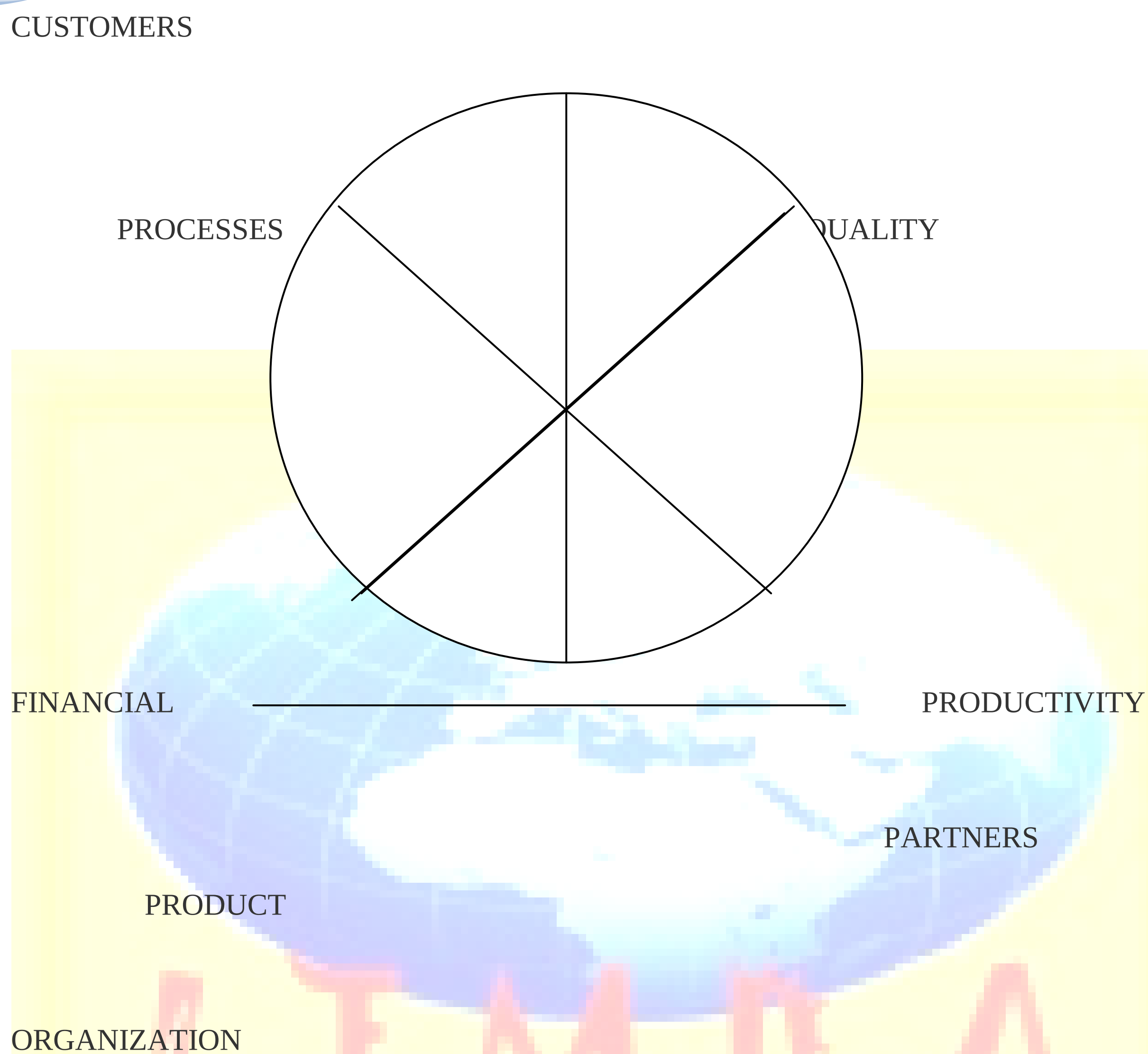


Figure 1 strategy wheel

3.1 Strategy definition

The industrial organization economics (Scherer & Ross, 1990) research defines competitive wars as a form of extreme, cut throat competition that results primarily from the structural characteristics of industries. With airlines, the industry conditions, such as low growth, excess capacity, and large number of competitors with similar relative power, standardized products, and high fixed costs are identified to be among the primary antecedents of warlike competitive behavior. The International Trade Centre, International Trade Forum Issue 3/200, contents that, I quote," The seeds of innovation need fertile terrain in order to grow. Innovation strategy is most likely to succeed when it compliments service excellence, quality assurance, customization and bench-marking strategies," end of quote. Competitive focus is more value for money in the airline environment. Once the airlines control their current service delivery process (quality assurance), they are able to meet appropriate customer expectations, and know what the competition are doing, and will be in a position to consider innovation. Service innovation is driven by focusing on solving customer problems while maintaining a loyal customer base.

A strategy is a plan for interacting with the competitive environment to achieve organizational goals. Strategies can include any number of techniques to achieve the goal. The essence of formulating strategies is choosing whether the organization will perform different activities than its competitors or execute similar activities more efficiently than its competitors do. Strategy necessarily changes over time to fit environmental conditions, but to remain competitive, companies develop strategies that focus on core competencies, develop synergy, and create value for customers. Core competence represents a competitive advantage because the company acquires expertise that competitors do not have.

3.2 Complex Pricing Strategies

Complex pricing strategies alone are no guarantee for success in a very competitive airline environment. When the airline industry was deregulated, most airlines introduced highly sophisticated yield management techniques to maximize profits. While revolutionary at that time, complex pricing strategies spectacularly failed the test of time. One of the crucial success factors is an innovative, and extremely simple, pricing strategy, embedded, however in a much more coherent overall corporate strategy.

3.3 Competition embodies two competing rivalries

Competition either appropriates value on one hand or creates it on the other. Management of this tension is central to strategy. Discourse in strategy is organized around barriers to competition in the airline industry. These include firm positioning (Porter, 1979) and transactions cost economics (Williamson, 1971.) The two sides of competition create an interesting tension-the intensity and balance of which have major, often surprising, implications for strategy. What makes competition interesting in the airline industry is this essential tension. The full effect of competition is to determine for each market participant, a range of appropriate outcomes.

3.4 In structural analysis and competitive strategy

Once the forces affecting competition in an industry and their underlying causes have been diagnosed, a company is in a position to identify its strengths and weaknesses relative to the industry. The crucial strengths and weaknesses from a strategic standpoint are the company's posture vis-à-vis the underlying causes of each competitive force. Where does the company stand against substitutes, entry of barriers, and copying with rivalry from established competitors?

3.5 Strategy and spirit

To assess an airline's strategic position, its managers must collect and interpret data regarding the company itself, its competitors, its stakeholders, and the industry. Having implemented a strategy based on that information, the airline must further measure that strategy's effect. Equipped with requisite information managers develop market and non-market strategies by matching internal resources with external opportunities. The complete set of strategies pursued by a firm is the result of analyses, decisions, actions, and results.

Airlines need to balance strategy and spirit as expressed by Tony Manning in his book "Making Sense of Strategy. See fig 1 below. For those airlines who are weak and have no strategy, we categorize them as the "NO-HOPERS". It is not worthy creating a strategy that is precise and detailed, but you have no spirit to drive it. The kind of airlines that have no drive are termed the "NERDS". The airlines that fall into the category of "PARTYGOERS "are those that are always busy but lack strategy and go no where. We finally have what Tony Manning calls the "PITBULLS" who are clear and ferocious about where they are headed. They fix a target and go for it.

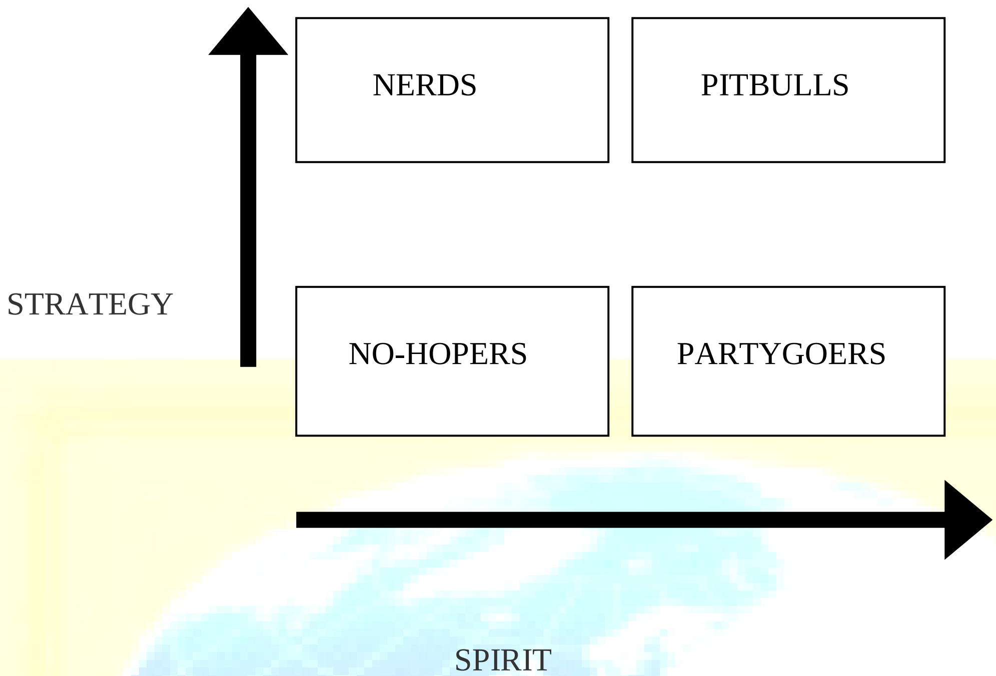


Fig 2 Source (TONY MANNING –MAKING SENSE OF STRATEGY)

3.5 Porter's Five Forces of Competition

3.5.1 Competitive Forces

The model originated from Michael E Porter's 1980 book" Competitive Strategy: Techniques for Analyzing Industries and Competitors." Since then, it has become a frequently used tool for analyzing a company's industry structure and its corporate strategy. In his book Porter identified five competitive forces that shape every single industry and market. These forces help us to analyze everything from the intensity of competition to the profitability and attractiveness of an industry. Quote "Moreover, in the fight for market share, competition is manifested only in the other players. Rather, competition in an industry is rooted in its underlying economics, and competitive forces exist that go well beyond the established combatants in a particular industry. Customers, suppliers, potential entrants, and substitute products are all competitors that may be more or less prominent or active depending on industry" Michael Porter.

The Airline is one of the major industries in the world today that is majorly affected by_Michael Porter's "Five Forces' model. The state of competition in an industry depends on five basic competitive forces. The collective strength of these forces determines the ultimate profit potential in the industry, where profit potential is measured in terms of return on invested capital. Competition extends well beyond the established players. Customers, suppliers, substitutes and potential entrants are all competitors and maybe more or less prominent depending on the particular circumstances. All five competitive forces jointly determine the intensity of industry competition and profitability, but the strongest force become crucial from the point of view of strategy formulation.

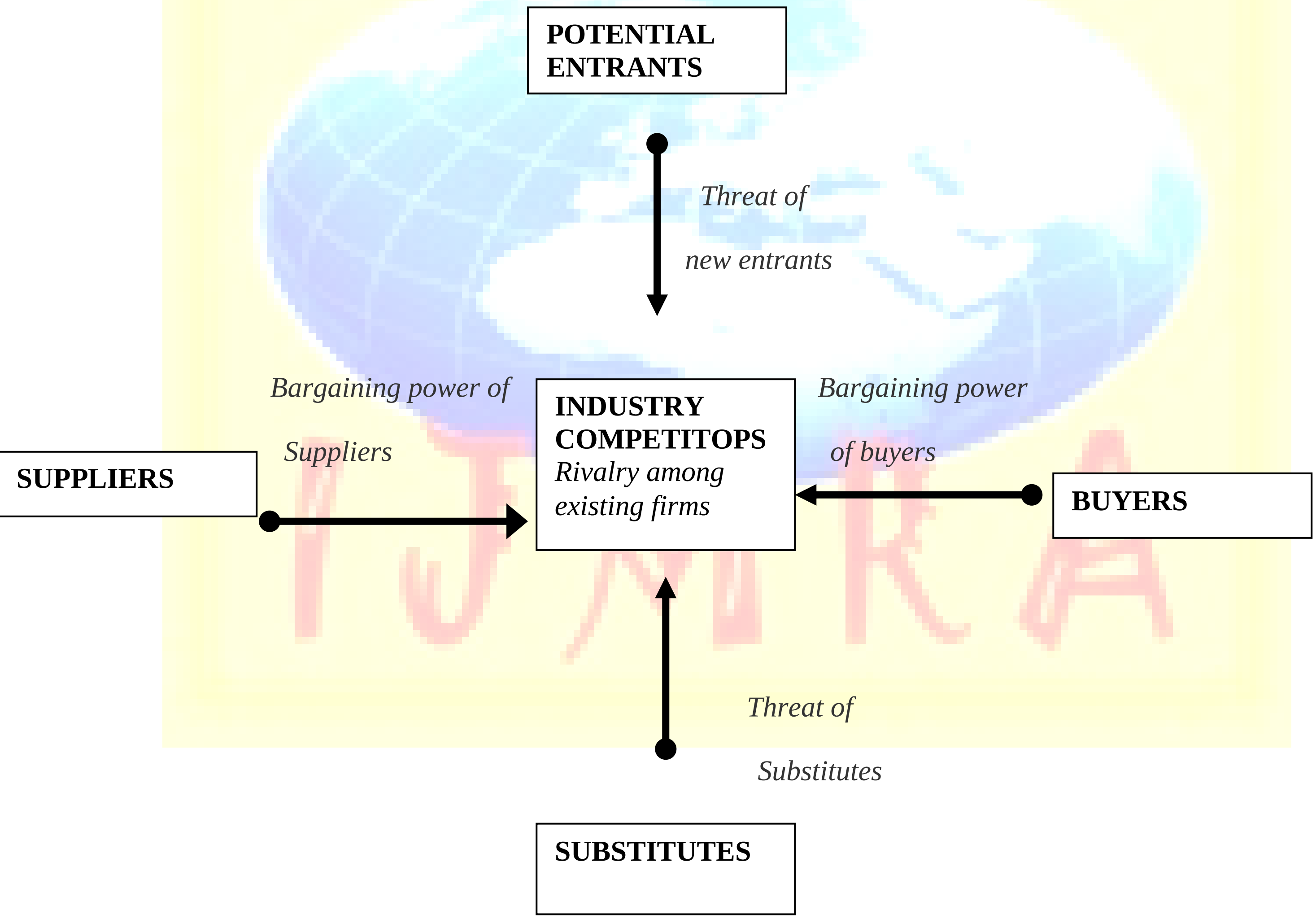


Figure 3 Porter's five competitive forces

3.5.2 New entrants to an industry

These bring new capacity, the desire to gain market share and other substantial resources. They can bid down prices or inflate costs. The cost of entry into an industry will depend in part on the probable reaction from existing competitors If a potential entrant expects the incumbents to respond forcefully to make its stay in the industry a costly and unpleasant one, it may well decide not to enter. The need to invest large a financial resource in order to compete creates a barrier to entry in the airline industry.

Entry can be deterred by entrant's need to secure distribution channels for its services. Existing airlines may have ties with channels based on long term relations, high quality service and even exclusive contracts. In the world today, the airline industry is so saturated that there is hardly space for newcomer to enter the market. The biggest for this is the cost of entry. The airline industry is one of the most expensive industries, due to the cost of buying and leasing aircrafts, safety and security measures, customer service and manpower

3.5.3 Bargaining Power of Buyers

This clearly demonstrates that buyers represent a competitive force because they can bid down prices, demand higher quality or more services, and play competitors off against each other, all at the expense of airlines' profitability. The power of each important buyer group depends on a number of characteristic of its market situation and on the relative importance of its purchases from the industry compared with the industry's overall business. Business class passengers are an airlines choice of the buyer group which they sell to as a crucial strategic decision. There is an amount of pressure customers can place on airlines, thus affecting its prices, volume and profit potential. Virgin Blue for example attracts travellers that are price sensitive by offering them low fares and those that are convenience oriented by providing them with frequent flights. The bargaining power of buyers is another force that can affect the competitive position of a company (Porter, 1998, p.45).

3.5.4 Bargaining Power of Suppliers

This depends on supplier concentration, substitute supplies, switching costs, threat of forward integration and buyer information (http://www.unisanet.unisa.edu.au, 14 April 2008).Suppliers within the airline is dominated by Boeing and Airbus as the main suppliers. Suppliers can exert a competitive force in an airline industry by raising prices or reducing the quality of the goods they sell. However there are other suppliers who work with the airline industry like the Jet A1 fuel suppliers, caterers and spare parts suppliers who have contributed to the erosion of profitability, and intense competition facing the airline industry. It is important to recognize labour as a supplier in the airline industry, and one that exerts great power. There is substantial empirical evidence that scarce, highly skilled employees (e.g. engineers and pilots) and or tightly unionized labour can bargain away a significant fraction of potential profits in the airline industry. Where labour is strongly organized and supply of scarce employees constrained from expansion they can be a factor in competition. Government which has been discussed primarily in terms of its possible impact on entry barriers must also be recognized as a potentially powerful buyer and supplier especially with national carriers. Many times government's role as a supplier or buyer is determined more by political factors rather than by economic circumstances, and this probably is a fact of life.

3.5.5 The availability and threat of substitutes

Is this another factor that can affect competition within the airline industry? It refers to the likelihood that customers may switch to another product or service that performs similar functions (Stahl, M, Grigsby D 1997, pg 145).Substitutes for air travel include travelling by train, bus or car to the desired destination. The degree of this threat depends on various factors such as money, convenience, time and personal preference of travellers. The competition from substitutes is affected by the ease of with which buyers can change over to a substitute. A key consideration is usually the buyers switching costs. Virgin Blue has actually joined forces with its substitutes, such as car rentals and hotel and tour packages as they believe that these compliment the Airline Industry by helping its growth and popularity.

3.5.6 Rivalry between existing competitors

In the airline industry, this takes the familiar form of jockeying for position using tactics like price competition, advertising battles, product introductions and increased customer service. A sequence of actions and reactions may or may not leave the industry as a whole better off. Some forms of competition, notably price competition are highly unstable and are likely to leave the whole industry in a worse situation from a profitability standpoint. Rivalry in airline industry is characterized by such phrases as

"warlike," bitter" or 'cutthroat'. When the competitors in the airline industry are as numerous as they are, the likelihood of mavericks that will touch off rivalry is great.

Airline industry rivalry becomes even more volatile if a number of airlines are high in achieving success. Such may be willing to sacrifice profitability for the sake of expansion.

Since the carriers are involved in a constant struggle to take away the market share from each other, industry growth is average and it is easy for buyers to switch between the airlines companies, depending on price, and the rivalry is increased. Rivalry is also high in the airline industry due to high fixed costs. As much of the cost of a flight is fixed; there is a great opportunity for airlines to sell unsold seats cheaply, which results in pricing wars between the airlines (Hubbard, 2004, pg 38). Airline Industry rivalry can be volatile when an industry faces high exit barriers, factors that keep companies competing even though they may be earning low or even negative returns on investment. Excess capacity does not leave the airline industry, and airlines that lose the competitive battle do not give up. Rather, they hang on grimly and, because of their weakness, sometimes resort to extreme tactics that can destroy the profitability of the entire industry.

Branding of Airlines.

"Like any other product, branding is a key component in the airline industry also. This is because all flying experiences are similar, boring and stressful. The plane is becoming a commodity and flying has lost all its magic" Reena Amos Deves, Emirates Business 24/7".To top it all; the competition in the aviation industry is increasing with the launch of new budget airlines. According to research, while 35 per cent of passengers choose an airline on the basis of punctuality, pricing comes second at around 30 per cent. However, this also means that 35 per cent of the decision making is influenced by other factors. This is where branding comes in. Hermann Behrens, CEO, Brand Union, and Middle East, told *Emirates Business*: "Branding is a key component for the development of airlines. Especially in today's competitive world where budget airlines are being continuously launched, branded, and aggressively marketed".

When combined with the pressures of increasing costs of running an airline like the soaring fuel costs and increasingly lower consumer price expectations, the market is ultra competitive. In the light of these developments, airlines are increasingly realising the need to build their brands to maintain and shape their market position, creating loyalty beyond price, where they can count on consumers returning, and offering services that will help the consumer, and run the business more profitably. Olivier Auroy, managing director of Landor Associates, said: "Branding helps airlines to differentiate themselves from others. It also helps them showcase their strengths beyond the expected basic requirement of taking a person from point A to point B',end of quote.

Differentiation has become important since low-cost airlines entered the market. Low-cost airlines provide basic services for low prices. That is why traditional carriers had to respond and improve the experience, because if the passenger only made his decision based on price, low-cost airlines would always be chosen. Though the basics of branding even for an airline remain the same, there are subtle differences. While from an operation point of view, the airline business consists of moving millions of people in metallic flying objects all around the world, from a customer point of view, ideally speaking, the airline experience should be the perfect combination of a limousine, a hotel, a restaurant, a lounge, a movie theatre, a comfortable bathroom, and a luxury shop.Auroy said: "The specificity of airline branding is that you carefully look at the brand experience and the customer journey". The customer journey is easy to identify.

The passenger becomes aware of the offer, explores the possible options, books his ticket, checks in, clears the formalities, waits to board, flies, disembarks, leaves the airport, hears again about the airline through promotions and advertising, and hopefully becomes a loyalist. Airline branding is to make sure that, at each stage, the passenger will have the best possible experience and that he will attribute that great experience to the airline he is flying with. The good thing about airline branding is that you can really connect and interact with the customer. When flying, he has no choice, he must stay on board – you can communicate and build relationship in all possible ways. But for the same reason he has to stay on board, he or she cannot move, the passenger can be easily frustrated and his or her expectations will be high. You have many opportunities to build brand loyalty. It is becoming closer to the hospitality business than ever before.

Unlike other products, most of the airline brand experience is delivered predominantly through service as all offer the basics of flying you to a destination, in very similar planes, and through the same airports and security measures. Airlines have an extensive array of service touch points where they can differentiate, from the moment a person picks up the phone to book a ticket until they reach their final destination, travel to the airport, priority check-in counter at the airport, lounges, baggage handling, cabin crew service, and uniform style and recently, with Virgin America, the advent of cosmetic changes to seats, cabin, and literature to change the flying experience. Airline branding helps passengers fly again and again. If the consumer buys the product once, it is great. If the consumer buys the product again and again, it is better. This is where the frequent flyer programme matters, because according to research, 35 per cent of passengers choose an airline on punctuality and 30 per cent on pricing. Football Association (FIFA) and football Emirates signed a \$195 million (Dh716 million) eight-year deal with Fédération Internationale de clubs Paris Saint-Germain (PSG), Hamburg, and Arsenal. The airline also bought the naming rights of Arsenal's £357 million (Dh2.6 billion) stadium. The 60,000-seat stadium will be known as Emirates Stadium for 15 years. While Emirates has also got its fingers in the Formula 1 pie with its tie-up with the McLaren team, its closest rival Etihad has partnered up with racing team Spyker, with the Chelsea Football Club and with the English rugby union team, Harlequins. However, not all airlines take that route. Some of them find their inherent strength and build on that.

Emirates, a global national flag carrier, project itself as a progressive, cosmopolitan airline that represents a dynamic and progressive country such as the UAE. It has realised that the world is changing and now seeks more from life [and airlines]. Virgin Atlantic renewed the whole in-flight experience with duvet, pyjama, popcorn, and bar and 'steal me' sticker on the salt cellar. They chose the in-flight message to symbolise this new way of flying. Another good example of this is Singapore Airlines (SIA), which runs one of the most comprehensive and rigorous training programmes for cabin and flight crew in the industry to make sure the SIA brand experience is fully and consistently delivered. Singapore Airlines built its reputation around hostesses. This has become their united selling proposition. Airlines can be divided into four different segments.

However, no amount of branding will be of any use if the airlines do not bring its staff into the experience. Airline expert at Landor, Al St. Germain, said: "How can any organisation expect its people to continue to improve in service without taking the time to properly instruct and evaluate them? Great airline customer service is made of consistency, empathy, support (frontline staff, a lot of work behind the scene), and style."

An Overview of Strategic Alliances

In a study done by Abhimanyu Bissessur and Fariba Alamdari, 04 September 1998, for the Air Transport Group, college of Aeronautics, they argued that with increased liberalization in major air transport markets, the intensity of competition increased among air carriers. Airlines responded to the competitive pressure in many ways, one of them which have been the formation of alliances. Alliance goes beyond the common interlining agreement to encompass certain marketing and cost reducing features. However the question is how the success of these alliances can be ensured. The analysis of recent major alliances covering 52 inter-hub routes, done by Cranfield University, suggested that the main factors ensuring the alliances operational success are: the partner’s network size and their compatibility, the frequency of service between the hubs of the partners, the flight connection time at the hub and the level of competition on their network. Collaboration has always been an integral part of airline business ever since the inception of the airline industry.

Arguments have, in most cases, involved technical cooperation, the exchange of aircraft and parts and joint aircraft maintenance. The practice of interlining is a good example of a type of cooperation which is characteristic of the airline industry. However with competition intensifying in a deregulated market, airlines are in search of size by first ensuring a dominant position within their own home market, second by gaining a foothold in other major regional markets and third by establishing a global presence (Doganis 1994).What differentiates these types of agreement with the contemporary alliances is that the latter are becoming increasingly strategic. In other words, the degree of commitment in and the importance attached to alliances as a competitive tool has increased. The notion of companies collaborating for their mutual benefit through the formation of strategic alliances has gained credibility in recent years and international airlines have been very active in utilising this form of strategic development. Strategic alliances can be effective ways to diffuse new technologies rapidly, to enter a new market, to bypass governmental restrictions expeditiously, and to learn quickly from the leading firms in a given field. However, strategic alliances are not simple or easy to create, develop, and support. Strategic alliances projects often fail because of tactical errors made by management. By using a well managed strategic alliances agreement, companies can gain in markets that would otherwise be uneconomical. Considerable time and energy must be put forth by all involved in order to create a successful alliance. It is essential that corporations enter into strategic alliances arrangements with a comprehensive plan outlining detailed expectations, requirements, and expected benefits.

Alliances among airlines are not a passing phenomenon but rather a permanent fixture of the industry because they not only create values to customers, but also enhance profit opportunities for the partners. Therefore, strategic alliances among major carriers are likely to be strengthened in the future. In addition, the cost of ending a strategic alliance relationship increases as the partners work closely by investing time, energy and resources to enhance mutual benefits. Also, the opportunity cost of finding another partner will increase rapidly as many airlines find durable alliance partners. These factors will provide an increased stability in alliance structures. Airlines have learned to fine-tune alliance relationships to make the gain-sharing more equitable. Governments began to scrutinize alliances with one-sided gain-sharing. Alliances involving unidirectional equity investment tend to be structured in such a way that the investing carrier gets a major share of gains from the alliance. Because of this and the inherent risks involved in investment, equity alliances tend to be unstable. Therefore, in the future there will be fewer alliances with equity investment. Already, there has been a decline in the growth rate of equity alliances.

Technology

In the face of ever growing competition and new industry requirements, including environmental benchmarks, fuel efficiency and passenger preferences, airlines are engaged in fleet renewal programs and have made orders for or indicated interest to order the latest equipment in the market. Passengers are becoming more demanding regarding comfort even on short haul flights.

To remain in contention airlines need to overcome the lure to step down their quest to acquire newer airplanes on the reason that oil prices have ebbed. Besides fuel related cost reduction, newer airplanes offer more customer satisfaction and environment efficient services. They could also save airlines the extra hassle of retrofit for emerging new technologies. This is also in line with global target to achieve a 25 % improvement in fuel efficiency by 2020 compared to 2005.Iata also says that further efforts are needed in user preferred air routes and implementing performance based navigation procedures for all phases of flight. It is also expected that oil prices could rebound when the economic meltdown ebbs because improved economy would spur oil based activities that would drive up demand for oil.

RESEARCH METHODOLOGY

Research Design

The design centers on issues of competitive intensity and other environmental factors in the airline industry. The program was based on qualitative research, which was basically a field of enquiry. The research method was to investigate the why and how of decision making in the airline industry given the competitive environment that exists in this business and the implications these decisions had on strategy formulation.. Therefore a smaller but focused sample comprising of fifty airlines (50) was chosen. I used the questionnaire approach which had the advantage of allowing for more diversity in responses as well as the capacity for me to adapt to new developments or issues during the research process itself.

In terms of other sources for data collection, I ensured that the program allowed me to emphasize on direct and frequent interaction with the airlines, through direct observation and on site visits with industry stakeholders, as well as meetings with distinguished industry leaders, and visiting of certain places and finally evaluating answers. I selected the airlines for a case study as they typify certain outstanding characteristics of competition. I adopted a systematic and transparent approach to analysis through coding of data, discerning and documentation of themes. This entailed a comparative analysis where data from different airlines, at the same point in time or same environment settings over a period of time were analyzed in order to identify similarities and differences. Graphs were used in the analysis and interpretation of data, justification being that they clearly demonstrate the competitive aspects and their correlation to strategy formulation.

My main purpose was to test emerging ideas which might take this research in new and fruitful directions.

Data Collection

I used different approaches in collecting data. I typically relied on the following methods for gathering information namely interviews structured through questionnaire, acting as a participant/ observer, data from journals, information from websites and analysis of documents and materials supplied by the airlines.

The questionnaire helped me obtain data through an airline survey which attempted to provide answers to questions on the key drivers of each airline's business model, the issues of strategy, pricing, the difference in passenger perceptions between low cost carriers and full service incumbents, and the particular reasons why a passenger chooses a particular airline model and how carriers can encourage passengers to return. A questionnaire was administered to a sample of a fifty (50) airlines comprising of leading airlines, small carriers and the low cost carriers. Data collected involved participation by management in the various airlines, shading light on their activities, the competition and and their strategy. A stratified sample was used with the population being divided into three categorical subgroups i.e European carriers (60 percent of the sample) ,African carriers (30 percent of the sample and Low Cost carriers (10 percent of the sample).The selection process from the above three groups in terms of submitting questionnaires was done randomly. Only 35 airlines responded constituting an overall response rate of 70 percent.

I also obtained data through direct interviews, documents (reports and emails from airlines), library sources, and websites of airlines, newspapers reports and my direct observations, albeit with reference to original documents. To further augment data collection, the research relied upon widely recognized and pioneering research that was provided by senior managers in the airline industry with their novel approaches to key strategic issues. This research dwells much on data reported through theoretical work that is not original, in which case it will include sufficient material to allow understanding of the arguments used and their physical bases.

Data Analysis

Data collected through questionnaire responses from airlines was meant to attempt to address the issue of competitive intensity from the perspective of all the aspects addressed in literature review. The analysis comprises of my impression through examining data, interpreting it via forming an impression as reported in the graphs shown below. The analysis also entails the range of processes and procedures where I moved from the qualitative data collected into an explanation, understanding and interpretation of airlines and situations which were investigated. The analysis attempts to identify any of but not limited to the following;

- Management interpretation of the airline competitive world
- Why they gave that point of view
- How thy came to that view
- What they have been doing
- How they conveyed their view of that situation of competition
- How they identify or classify their airlines through what they say.

Data was scanned and segmented. It was coded into themes, topics; ideas terms and key words. Codes were identified through previous research as tabulated in literature view, questionnaire, presuppositions and my previous knowledge of the subject area that I was researching. I did ascertain patterns which represent major issues, leading to coded areas i.e the competitive behaviour of airlines in a given environment, strategies and tactics, relationships of airlines, general concepts and constant comparison of the data from different airlines, at the same point in time or same environment settings over a period of time.

RESULTS AND DISCUSSION

Results

1. Percentage ranking of factors attributed to Poor Performance of Airlines

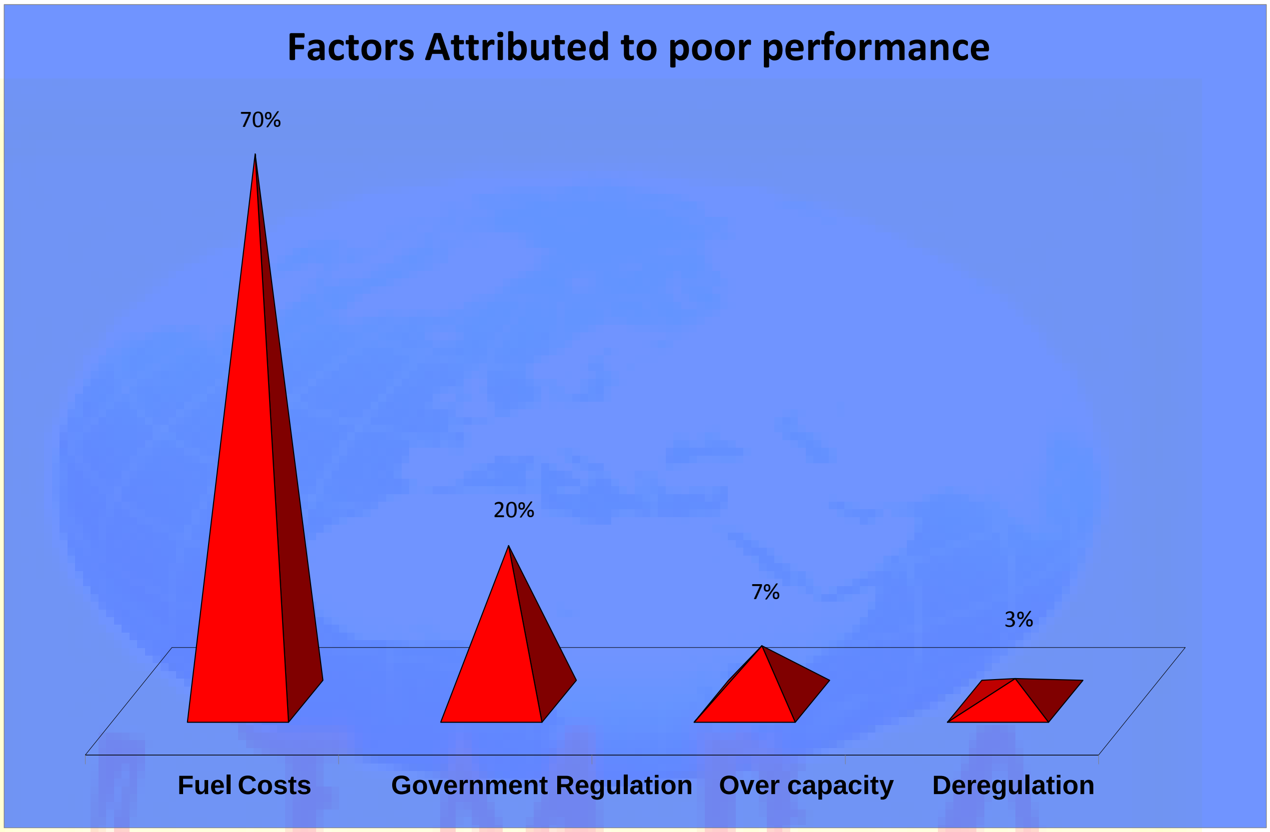


Fig 4

70 percent of the respondents ranked fuel costs as the highest contributor to poor airline performance followed by government regulation, overcapacity and also deregulation to a very small extend. Managers indicated during interviews that their fleet renewal programmes were meant to enhance fuel efficiency in their operations.

I also gathered that this was in line with the industry global target to achieve a 25 % improvement in fuel efficiency (verified through IATA).

However the 20 % reflected as contribution to poor performance due to government regulation was mainly echoed by respondents from the group of African airlines, a reflection of the fact that the majority of these African airlines are parastatals wholly owned by their governments. This group of airlines confirmed that government regulation had adverse consequences and no incentives to reduce costs.

2. Percentage Ranking of Factors considered in strategy formulation

Strategy Formulation

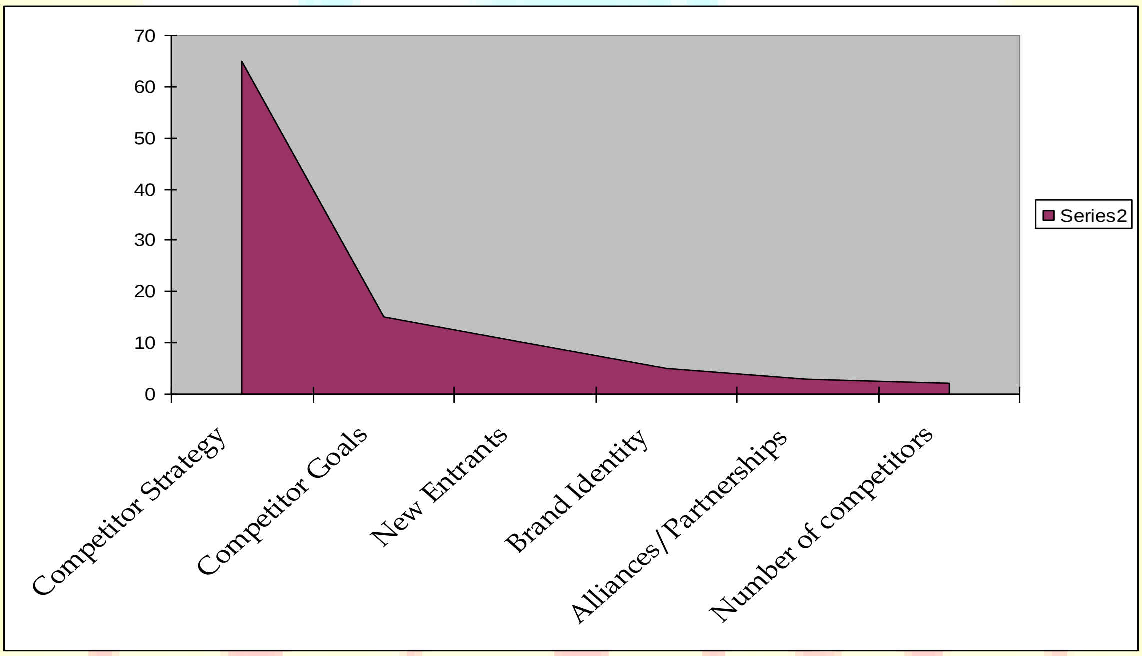


Fig 5

The issue of intensity in competition is clearly reflected and rated as a highly critical component in strategy formulation. All the respondents rated competitor strategy, goals and new entrants at 60, 12 and 10 percent respectively. Brand identity and alliances were reflected not as a major issue in strategy formulation. This confirms the managers sentiments that the issue of formulating strategies is choosing whether the organisation will perform different activities than its competitors or at least execute similar activities but more efficiently. The new entrants were rated low at 10 percent because the respondents confirmed that these are affected by the high costs of entering the airline industry.

3. Factors Contributing to Competitive Intensity

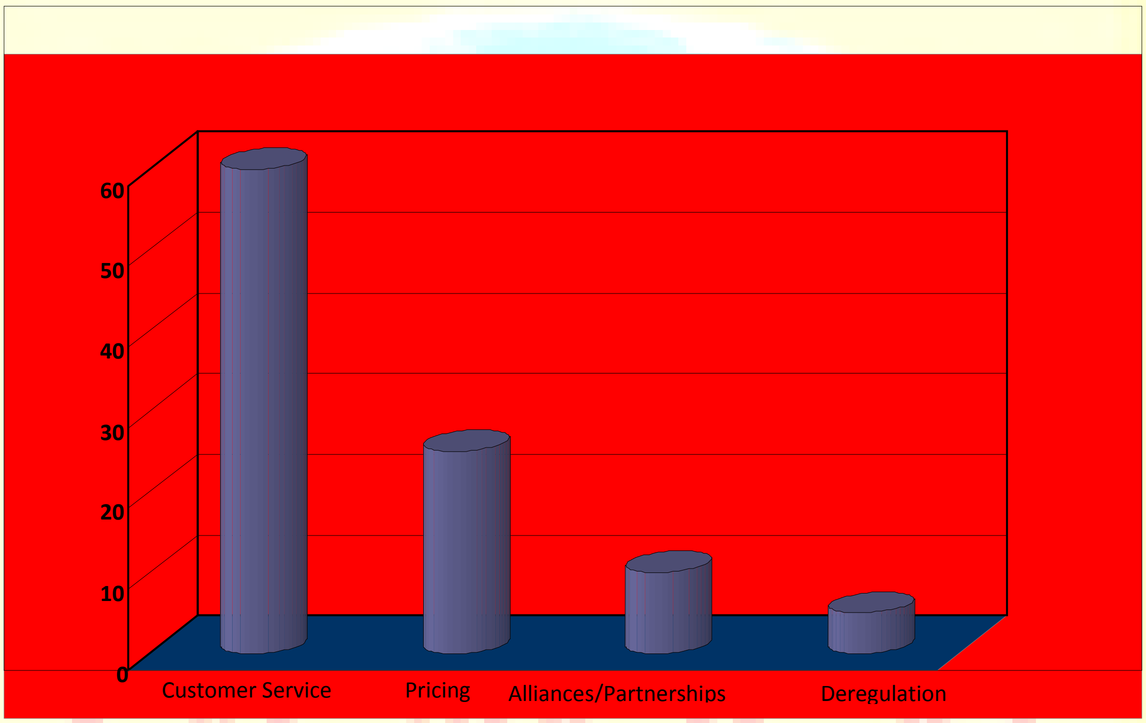


Fig 6

The highest contributor to competitive intensity as indicated by 80 percent of the respondents was the issue of customer service, followed by pricing. Of less significance was the impact of alliances or partnerships and deregulation which were mentioned by only 8 and 2 percent of the respondents respectively. Airline managers believe alliances are not simple to create, develop and support , hence some alliance projects often fail.

4. Percentage ranking of factors adding value to Customers.

VALUE ADDITION

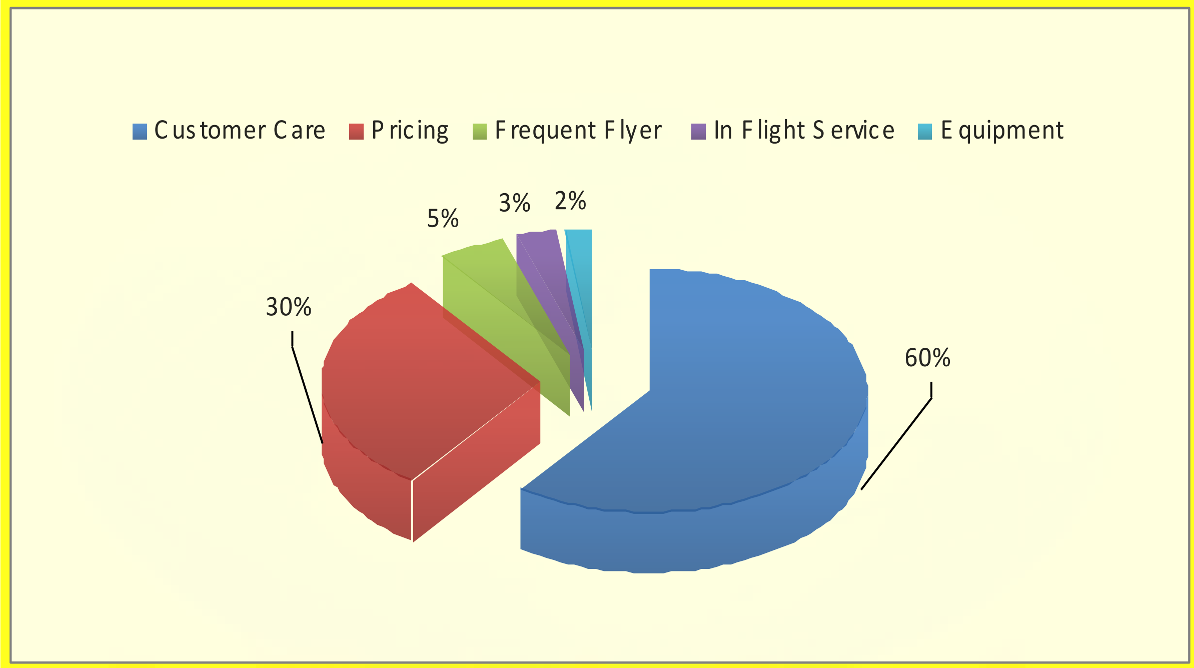


Fig 7

The respondents clearly indicated that customer care, ranked at 60 percent, has a critical role in adding value to the customer followed by pricing at 30 percent, with frequent flyer program and in-flight service at 5 and 3 percent respectively. These same value addition components add up to create the competitive intensity in the airline operating environment. Great airline customer service is made up of consistency, empathy, support of frontline staff and style. The focus of policy makers is often on the potential price effects that various business decisions of airlines may have.

5. Surviving Competitive Intensity

COMPETITIVE INTENSITY

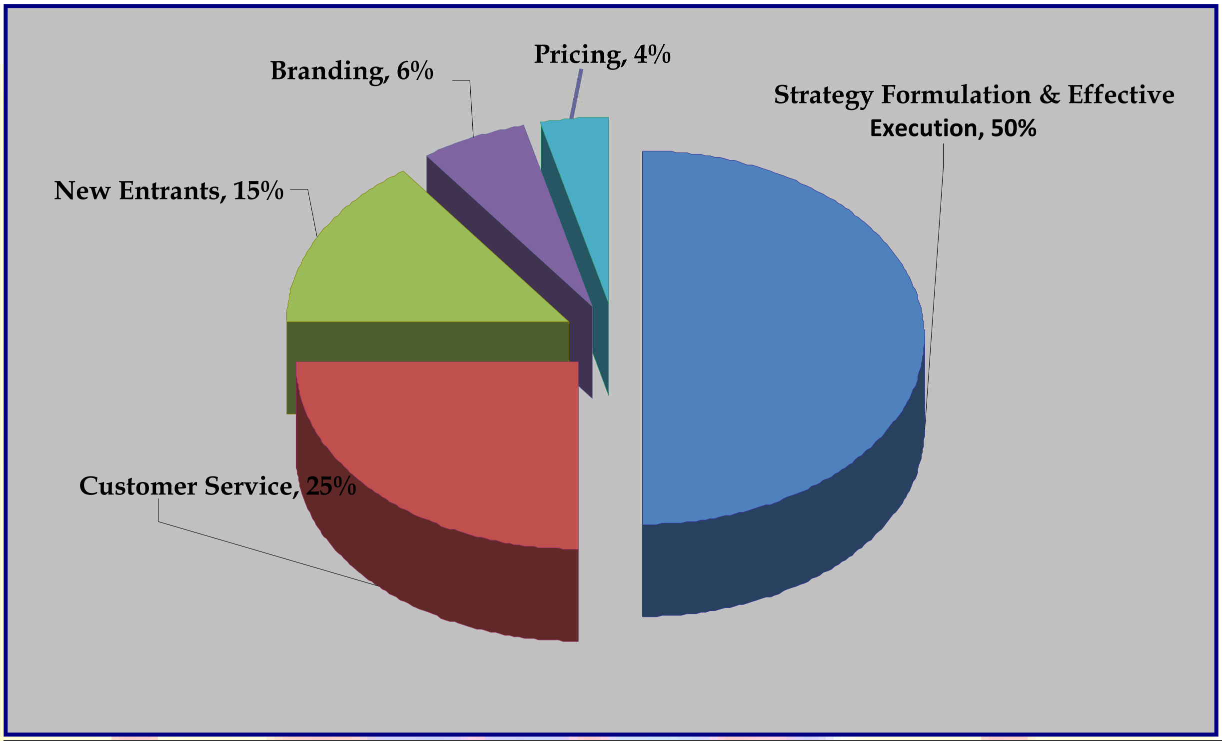
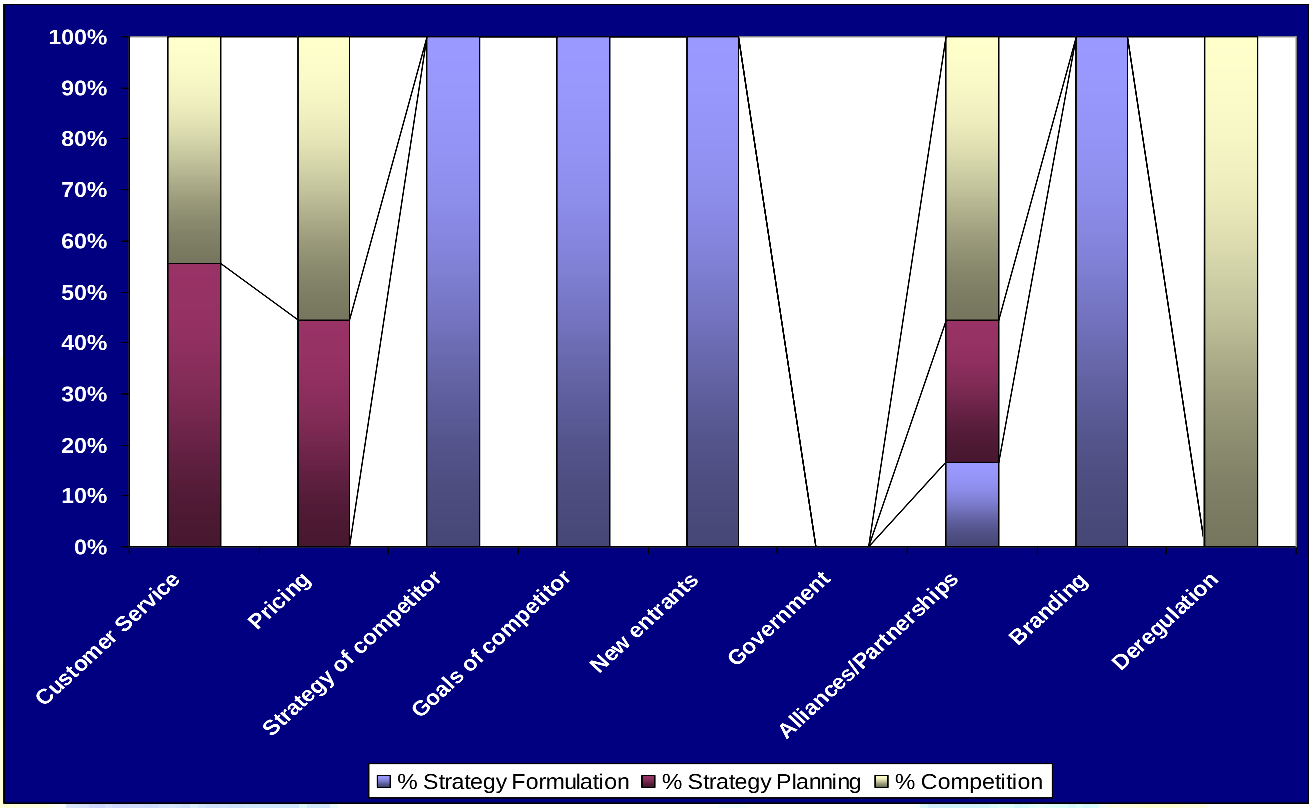


Fig 8

When you aggregate all the factors related to the analysis of the forces that determine competitive intensity and other environment in the airline industry, the above graph indicates areas the airlines should focus on in order to survive competition. According to the respondents, strategy formulation and implementation tops at 50 percent, customer service 25 percent, new entrants 15 percent, with branding and pricing at 6 and 4 percent respectively.

CORRELATION OF COMPETITION AND STRATEGY



Airlines are most concerned with the intensity of competition as shown in the graph. But the level of intensity is determined by basic competitive forces. The elements that constitute aspects of competitive intensity of airlines i.e customer service, pricing and alliances/partnerships, are highly considered in terms of strategic planning. In the same vain, the goals and strategy of the competitor, new entrants into the market, and brand identity form an integral part in the strategy formulation process. This analysis shows that the determinants of competition do have a direct bearing and implications on the choice of strategy adopted by airlines.

DISCUSSIONS

The air transport industry has experienced the broader consequences of the economic recession that became more acute towards the end of 2008.Beyond the projection of USD 5 billion losses IATA made for global airlines for 2008, the airlines lost about USD 8 billion going by IATA figures. The trend appears not to have bottomed out yet, in which case the industry must continue to embrace cost readjustments and revenue enhancements. The contributions of the aviation industry to economic recovery and growth have become clearer to governments who should be encouraged to increase support to the air transport industry. Liberalization is good and protectionism is bad. It is too late to go back to the days of heavy protectionism. Protectionism creates high fare levels, leading to low loads and ultimately poor performance of an airline compared to its competitors.

The general trend noticed in the results is that airlines think the aspect of pricing in the airline industry plays a significant role in creating competition and adding value to the customers. While the pros and cons of alternative product, place and promotion strategies have been discussed at length in innumerable academic and trade journals, and clearly prevailed in the practice of marketing management, most airlines have so far ignored the crucial importance of innovative pricing strategies as a tool to create a sustainable competitive advantage over rivals. As a result traditional approaches to pricing such as cost plus pricing or simply following the prices of the competition prevail.Relative importance of price and non-price product characteristics in influencing potential passengers' choice of products offered by airlines clearly shows that on average prices may not be as important as we think in explaining passengers' choice behaviors among alternative products. I argue that changes in demand and cost conditions may influence the competitive intensity, thereby causing an indirect effect on prices. It is however astounding that pricing is the only tool in the marketing mix which generates revenues directly, whereas, all others cause costs to rise. While cost reduction potentials have been largely exploited by most airlines and an increase in volumes is hard to realize on saturated markets, the optimization of pricing processes remains at least a promising strategy. However complex pricing strategies are no guarantee for success in a very competitive airline environment.

While collaboration has always been an integral part of airline business, the issue of alliances and partnerships has minimal effect on competitive intensity and strategy formulation as observed in the results. The conventional wisdom of the airlines was and is still to some extend, that globalization demands concentration into a small number of global operators, a conventional wisdom which did not really reflect in this research and which perhaps could be false. The important changes in airline industry structure have come not from mergers but from the ability of new entrants to grab market share in more competitive markets. Of course national protectionism prevented full consolidation and global alliances of business carriers were established with the main groupings being the Star Alliance and One World Strategic alliance projects often fail because of tactical errors made by management.

The airlines are continually competing against each other in terms of prices, technology, in-flight entertainment, customer service and many more areas. In the past monopolization of major routes, emergence of limited brand loyalty and tacit price agreements helped reduce the intensity of competition. Slumping demand beginning early 1990s plunged the industry into a severe price war. Overall competition, in summary of the five forces model, suggests that the intensity of competition in the airline industry will continue to be severe. The net result of this competition between the airlines is an overall slow market growth rate. We can understand from the results that the airline industry is very competitive and Michael Porters five –force model demonstrate why the potential for returns is so low in the airline industry.

Branding is to make sure that, at each stage, the passenger has the best possible experience and he will attribute that great experience to the airline he is flying with. Brand identity according to results of this research, has very little or minimal influence in terms of strategy formulation and competitive intensity. This shows that airlines are failing to grasp the concept that a brand is a bundle of perceptions and feelings that customers hold for a product or service or the airline company. It becomes harder to stay apart or ahead, and this explains why some airlines find branding not a big deal.

New entrants are supposed to bring in new and extra capacity. They fight for market share and bid down prices. This ultimately inflates the costs of doing business. Entry is mainly deterred by the cost of entry into the airline industry and is largely determined by the existing competitors.

The essence of formulating strategies is choosing whether the airline will perform different activities than the competitor or pursue similar activities but in a more effective way. Once the airlines control their service delivery process, they are able to meet appropriate customer expectations and are able to survive competition.

CONCLUSION

Major findings

- Industry competitive intensity is determined by the number of competing firms, their competitive strategies, and the industry competitive forces. The competitive intensity of the industry determines how difficult it is for the business to earn a sufficient profit. Competition in the airline industry drives down the profits that can be achieved by the airlines.

- Ultra complex pricing strategies have spectacularly failed the test of time. Airlines are advised that price wars tend to increase total industry demand and consumer surplus, but simultaneously they tend to be detrimental to the airlines' profitability. Therefore airline organisation economics should emphasize that avoiding price wars is an important strategic concern for the airlines.

- One would like to conclude that airline business is a big gamble which involves a lot of guesswork, with a few certainties and many possibilities. The best the airlines can do is making some assumptions based on what is already going on. Executives in poorly performing airlines are quick to blame external factors for their plight. It is everyone's fault but their own .They are victims to forces or events around them so they say. I believe this is absolute nonsense and the fact still remains that they have a huge amount of influence over their own fortunes.

- The other major pattern in my observation of the results is that, while an airline must live with many of the factors determining the intensity of the airline industry rivalry that are built into industry economics as reflected in this research, it has latitude to influence rivalry through its choice of strategy.

- Prices and margins in the airline industry are being driven down to unattractive levels because too many competitors are chasing the same flighty customers. This can be overcome by getting the basics right, creating an appropriate value proposition and executing effectively. However if ones value proposition is just like everyone else's, there is no reason for customers to buy from you. In this cluttered, fast moving airline world, change and innovation are on everyone's lips. Airlines go to great length to promote their services and products, but unfortunately majority cannot deliver what they promise and so they destroy their credibility. The customers' views may be precise and intense when they shop around. However those views are made up of people, machines, ideas, technologies, systems and philosophies.My advice to airlines is to find a bright idea that is new, exciting to the consumer, and moves the market. They should build their own brand identity to make sure the brand is at the centre of everything they do, and every service they provide. It is however difficult for the airlines to build brand loyalty due to travel being a commodity type product with limited potential for differentiation. Mismanagement and time has also killed brands in airlines.When it comes to experience, airlines already know where the improvements should or could be made.

- Strategic alliances are also an effective way to diffuse the intensity of competition in the airline industry. Alliances have in most cases proven to be a positive sum arrangement and one foresees that it will be a matter of time before the emergence of competing global alliance networks.

- The problem as I see it does not necessary lie with strategy, but with execution of strategy. Effective strategy is not separable from execution and is not based on visions and dreams, but on match between capabilities and activities. While all the five competitive forces do jointly determine the intensity of airline industry competition and profitability, ultimately the strongest force, which is very crucial, lies in the formulation and implementation of strategies. Some airlines have been damaged by unrealistic ambitions: the remarkable feature of the Swissair debacle was the quality of the business that was destroyed and the degree to which the strategy was inappropriate for the distinctive capabilities of the organization.

Implications of findings

- Everybody agrees we are in a recession and the rest of the world is joining in. Nobody knows how deep we will sink or how long it will last. Airlines are affected differently. There could be more airline failures, bankruptcies or threat of bankruptcy in 2012 and 2013.Oil prices may resume climb or demand weakens leading to airlines shrinking. There are a lot of issues that will determine whether the world air carriers will thrive or struggle to survive. If crude oils remain low, the airlines could have a banner year despite the current recession taking place. If there was an unfortunate scenario where oil prices were to climb back to then levels of mid 2008, then there would be a lot of bankruptcy. The late collapse part of 2009, in energy prices, has mitigated the damage to airlines' bottom line this year. What drives airline planners to distraction is the unpredictability of fuel prices as each price brings different answers. This points out to the strong possibility of more airline failures and consolidation in the next twelve months. If oil prices resume their climb or demand weakens significantly, airlines may need to shrink even more. This would have a ripple effect for the employees, airports, airplanes lessors and the flying public. There will be fewer flights, routes cancelled and fares going up as the industry's capacity gets smaller. Airlines would have to adjust to falling demand.
- John Lennon put it perfectly when he said," Life is what happens when you're busy making other plans." Unfortunately life does not wait for the market analysis done by the airlines, nor does it wait for advice from consultants or the 600 page plan. The airline business is a dynamic, complex, surprising, exhilarating, wonderful and sometimes shocking process that can sweep a company along or sweep it away. Most airlines fail not because their executives are dimwits, but because they interpret environmental signals to suit their own mental models or they throw their heads in the clouds and ignore what is going on in the global industry.

- Two of the hottest business themes in recent years have been core competencies and chaos theory. The ability to anticipate, imagine, and innovative is the most critical competence of all. The world is inherently unpredictable hence you do not have to know everything. Surprises can only energize one and serendipity becomes a spark for change. Strategy demands discipline. It is stupid to do change for the sake of change in the airline environment. By the same token it is insane for airlines to do more of the same while expecting different results. Generally I would recommend airlines to aim for both improvement and radical change. It makes it hard for competitors to match.
- Airline consolidation has never resulted in lower customer prices and there is no reason to believe it should.
- Overcapacity is not the problem; appropriately priced capacity is the issue.
- Even if all airlines looked like major low cost carriers, the industry would not be better off.
- I can postulate that airlines will continue to employ predatory tactics only to strengthen or preserve their monopoly position in the markets. My concern is therefore that airlines might engage in predation with the aim of dissuading entry and increasing market power through their networks. Distinguishing predatory behavior and competition of the kind that benefits consumers is difficult in the airline industry because of frequent fare wars.
- Despite the record passenger numbers, the airline industry is in such a mess and cannot rationalize its operations or finances.
- Therefore in strategy research, very few people will dispute the premise that competition is central to a company's performance. The competition inherently creates tension and intensity and simultaneously this has strong implications on the choice of strategy adopted by the company.

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Abbreviations

IATA	International Air Transport Association
ASA	Air Services Agreements
LCC	Low Cost Carriers
CRS	Computer Reservations System
GAO	US General Accounting Office
SIA	Singapore Airlines
FIFA	Football Association
UAE	United Arab Emirates