Low-cost aiming for long-haul?

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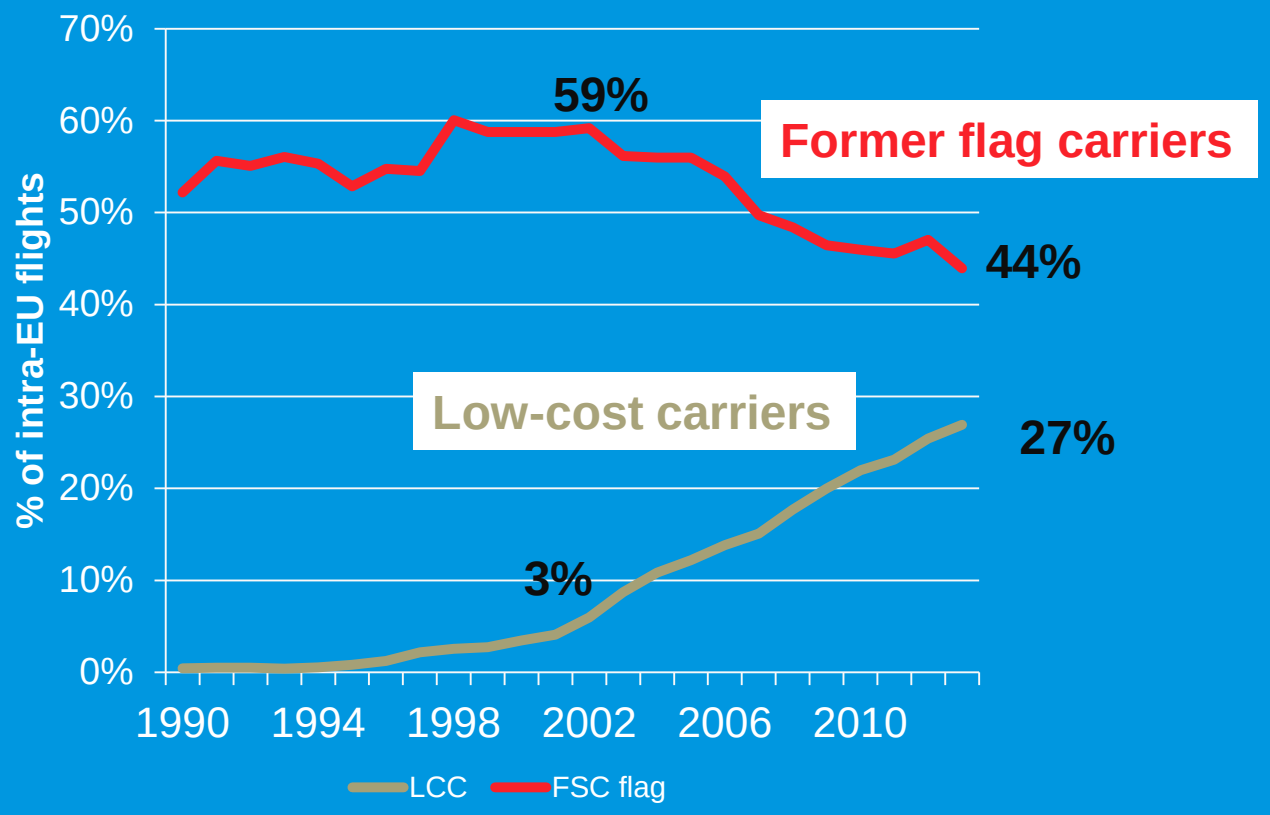
Keep fares low, costs lower. Southwest Airlines believes in low fares by philosophy. The only way to keep our fares low is to keep our costs even lower. It's our primary goal. And you can take that to the bank!

According to Mike Levine, the challenge in the airline industry is:

"To generate sufficient passenger route density, at fares that will pay the total cost of running the route"

Low-cost on the rise in Europe



Source: Burghouwt & De Wit (2015)

Traditional low-cost markets saturating?

- According to research by De Wit & Zuidberg (2012; 2015):
  - Low-cost carriers increasingly serve low frequency routes
  - Low-cost carriers increasingly serve longer routes
  - Low-cost carriers increasingly use primary airports
  - Transfer traffic to supplement route density

  - Long-haul low-cost

Airneth 2007 conclusions

In September 2007 Airneth organized a seminar on Long-haul Low Cost. We concluded that the scope for Long-haul Low-cost operations is limited because:

1. The scope for cost reductions is limited:
   - Large share of costs is fixed (fuel)
   - Some services must be retained (seat pitch, in-flight entertainment)
   - More efficient crew scheduling is difficult
   - Fleet utilization in long-haul is already high
   - Long-haul operations are more complex (catering, transfers, accommodation for crew, cargo)
2. Legacy carriers already offer relatively low fares on long-haul flights :
   - Business class passengers ‘subsidise’ economy class passengers

Airneth 2007 conclusions

Example: Potential cost differentials for a sector of 4,000 miles (e.g. London-Chicago):

All figures in £	Virgin Atlantic	Adjusted for high density all economy (90% loadfactor)	Low-cost airline with other adjustments
Crew	27.65	19.75	12.00
Fuel	47.09	33.64	33.64
Aircraft	73.71	52.64	52.64
Charges	38.39	27.42	17.57
Passenger services	25.19	17.99	0.50
Sales & advertising	24.76	17.69	4.14
Cargo specific	8.10	5.79	0.00
Other	13.19	9.42	5.02
Total cost per passenger (one-way)	258.08	184.34	125.51
Total cost per passenger (return)	**516.16**	**368.68**	**251.02**
			+10% margin
Cheapest return fare	**330.00**		**276.12**
			-16%

Source: Adjusted from Francis et al., 2007

- "For most passengers this is unlikely to be a sufficient discount to offset the disadvantages of a higher seat density and no in-flight services", features especially valued on long-haul

Airneth 2007 conclusions

3. Barriers to entry:

- Few dense long-haul routes can be operated based on only the local demand → Feeder traffic is required to operate thinner routes
- Potential for use of secondary airports is limited since many airports lack sufficient runway capacity.
- Airport costs are only a small portion of total costs on long-haul flights

4. Demand stimulation more difficult:

- Time constraints for long-haul leisure travel
- No diversion from surface modes

Airneth 2007 conclusions

However, we also identifed opportunities for Long-haul Low-Cost operations:

1. Market opportunities exist for pure leisure markets (VFR) operated at low frequencies or in dense markets. Leisure passengers are more sensitive to price, but less to frequency and service level
2. New aircraft technology may increase the scope for long-haul operations
3. Labour is an area where costs can be reduced by locating in a low-cost or low-tax economy (flags of convenience)

Recent developments

Since 2007, 19 airlines have launched scheduled long-haul services. Twelve of those are low-cost carriers

Full-service	Low-cost
Arik Air	AirAsia X
Hainan Airlines	Azul
Mega Maldives (quasi charter)	Cebu Pacific
Oman Air	Eurowings
Sichuan Airlines	Indonesia AirAsia X
Xiamen Airlines	Jetstar
Virgin Australia	Jin Air
	NokScoot
	Norwegian
	Air Canada rouge
	Scoot
	Thai AirAsia X

Source: Airline Leader, Issue 28

- Technology: B737 Max, 787, A350
- Labour: flags of convenience; atypical employment
- Liberalization (EU-US, EU-Canada)
- Traditional Point-to-Point markets saturating?

Although the Long-haul Low-cost model is still a niche in Europe, this may change due to developments in aircraft technology and labour costs, as well as changing market circumstances and business model development