

American airways report examples

[Business](#), [Company](#)



Overall financial performance

US airline industry can be divided into two phase, which include the regulation phase and deregulation phase. This means that at one time the industry was being regulated and it recorded huge profits. A time came when the industry was no longer regulated, which led to increased competition from new entrants who would enter the market with a lot of ease. Year 2008 marked the worst performance in the airline's industry (Class Text book). During this year, profit margins were reported to evaporate. All the airlines, including American Airlines, recorded large losses. This was quite ironic because it had been optimistic that the industry would record profits. This followed the improved performance that prevailed during the year 2006 and 2007. Investors expected the financial stability to remain for quite some time. Similar profitability resurgence had been recorded in the 1999/2001 financial year. An end to that prosperity came on September 2001. In 2009, the global industry of airlines recorded a loss of \$8. 5 billion (Class Text book). Demand in the airline industry has deteriorated following economic downturn that has been experienced lately. U. S airline recorded smaller losses in the same year when other companies recorded losses ranging from 10-20% (Class Text book). Many airlines could be seen parked in California dessert following their surplus. Commercial jets were also seen to be in excess.

Structure of the industry

U. S airline was facing stiff competition in the industry. Following the company's history, it experienced bankruptcy. There were mixed opinions

regarding U. S airline. Some analysts argued that realism that existed, as well as financial prudence, affected the industry a great deal. Major losses and the existing competition from LCCs (Low Cost Carriers) succeeded in controlling costs. These carriers included Jet Blue, Legacy Carriers, among others. To be specific, they had formed labor unions, which gave them substantial concession as regarded working practices, pay as well as benefits. This gained them benefits in terms of efficiency that came from outsourcing, and the use of Information Technology (Class Text Book). Planes, which were fuel inefficient, became retired by the management. This further increased efficiency. Capacity of airlines was decreased significantly in order to avoid wars of fare costs, which appeared in 2008/2009. These airlines had learnt, the hard way, from experience. The industry, at that time, experienced consolidation that made it conducive to increase profitability. Economies of scale could be easily exploited; hence reducing competition pressure. America West and U. S airways had formed a merger in the year 2005. North West Airways had also formed a merger with Delta Airways in the year 2008 (Class Text Book). This convinced many airlines that mergers were the only way forward and could not be avoided no matter the circumstances.

It would also be argued that the problems experienced in the industry, came as a result of circumstances, which a brought by time. These circumstances arose as a result of international terrorism. Another contributing factor was the hiking fuel prices, not forgetting the 2007/2009 credit crunch. For several year, America Airways Industry recorded poor returns on capital both in US and other countries that the airline operated. The airlines struggled to

remain solvent but LCCs appeared unsuccessful; hence a lot of struggle.

Most companies lost money while others broke even. Pessimists attribute the losses to bankruptcy and liquidation also, whenever the industry appeared to revive, the carrying capacity would be added. New airlines also would join the market, aiming at making the expected profits.

Initial Strategies

The industry has restructured itself in an attempt to adjust to competition in order to gain competitive advantage.

Route strategy

In 1980's, most major airlines changed their routes. Each airline served a few routes. Major airports were few but became linked by services, which were frequent. They were also served by large aircrafts that connected to hubs that had small aircrafts. This allowed efficiency through reduced routes. The large aircrafts ensured that few trips would be taken in a day, but still the aircraft would carry many passengers.

Major carriers were also in a position to dominate regional markets on certain routes. There was geographical differentiation by major airlines. Hubs were also established, which made it hard for new entrants to join the market as it was hard to obtain landing slots at the hubs. The hubs were extended by forming alliances with commuter airlines. Delta and AMR established a shuttle system that coordinated marketing operations with the bigger companies, which they formed partnerships with.

Mergers

Seller concentration had reduced in the industry following deregulation of the industry. However, the leading companies desired to form both national and international networks, which encouraged formation of mergers, and in some other instances, acquisitions. Some companies formed mergers due to financial problems that affected many companies at that time. Government intervention also affected the industry

Prices and costs

Increased competition that followed deregulation affected pricing of air tickets. Price cutting resulted following either weak revenues, or the existing low cost carriers. The new entrants affected the prices following the existing competition. Companies sought expansion through low fares. The low charged fares were manageable because the airlines cut on flight meals, baggage handling, as well as entertainment. However, most of these new entrants failed to succeed initially, but new entrepreneurs replaced them by starting personal or own airlines. Major carriers were also forced to cut on their flight prices, which made the fare structures more complex. There was, therefore, the need to separate leisure loving customers from business travelers who are in most cases, price inelastic. Price cuts also depended on the route whereby major airlines allocated low prices in those areas where they faced stiff competition (Class Text Book). South West Company complained severally that the competitors were really cutting down the prices. The major airlines were unable to compete effectively by their labor agreements, commitment to certain routes, and infrastructure to various routes.

Differentiation

Under the era of regulation, airlines were unable to compete on the Basis the basis of price. This made the firms to compete under a new dimension, which was not price oriented. They, therefore, turned to customer service, flight meals and entertainment. Deregulation revealed customer loyalty whereby customers did not find any difference among the major airlines' offerings. Following differentiation, the focus was on first class travelers. To differentiate between business travelers and leisure customer, the airlines offered spacious seats, and other luxurious services.

However, this did not mean that the airlines charged expensively especially because they understood that clients did not notice major a difference in the additional services. The airlines, however, succeeded when they introduced flyer schemes that were frequent. This was launched in the year 1981. All major airlines eventually followed this trend. Free tickets would be offered depending on the flown miles. This attracted more customers and encouraged them to stick to a single airline. Additional revenue for the airlines started coming from partnerships with hotels, car companies and banks.

Cut on labor costs

The industry's costs, coming from labor, mainly come from employee remuneration and other employee benefits. On average, in the year 2007, the industry paid \$55950, which was higher by 40% as compared to costs of private airlines. Labor productivity had also become low following rigid working conditions, which had been agreed upon through trade unions. Most

of airlines' employees belong to trade unions, which have strong bargaining powers for salary increment. Such unions include Airline Pilots Association, among others. Employees use these unions as bargain tools for better pay. This further increases inflation within an economy. Airlines need to force concessions from employees. This will, in turn, reduce the average compensation per employee. This would further trigger a fall in employment in the airline industry.

Fuel efficient

The amount of fuel spent by a carrier depends mainly on the age of the aircraft and the length of flight on average. New planes are fuel efficient. Travelling for long flights also saves on fuel consumption. Fuel efficiency, however, varies depending with the design of the aircraft. Engine numbers affects fuel consumption a great deal. Fuel prices are among the highest costs in the airplane industry. Fluctuation of fuel prices has also been a major blow in the airplane industry. Air America needs to take measure, as mentioned above, to reduce on fuel cost. This would eventually lead to improved profitability.

Air Flight related costs

Cost item

Increase in cost (%) 2002-2008

Operating expenses 2006 (%)

Operating expenses 2008 (%)

Equipment price

Airlines spend a lot of capital on aircraft. An aircraft can cost as much as \$250 million. Financial strains occur when a company decides to purchase planes, which are new. The equipment should be taken care of since purchase of new equipment can exhaust all the company's profits. A company should purchase a new aircraft when necessary, and the equipment should be effective. In the year 2003, companies were recorded to purchase jets following increased competition. Some companies ended up registering losses, the following year because profits did not increase as anticipated.

Future profitability

It is expected that airlines profits will increase between the years 2010-2014. This will follow fuel price stabilization. Again, US government is committed to avoid a future economic depression, as the one that was experienced in the year 2007 and 2008. Reducing the cost base will also benefit the industry because costs affect a firm's profitability. It would be important that airline industry stops hiring excess employees, especially now that the unprofitable airlines have been closed down. The companies should also avoid purchasing unnecessary equipment as this spends a lot of capital.

Aircrafts capacity needs to be adjusted depending on demand. Large aircrafts that travel fewer flights would be very efficient as compared to jets that are quite fast, but travel for several trips in order to meet demand. Outside capital, where possible, should be used to fund losses, which are long term. The government should also make efforts to cut down fuel prices,

which have affected the industry for quite some time. Regulation of the industry would also help the industry to increase its productivity because several firms would not be allowed to join the industry due to regulation. Unhealthy competition is not advisable as it spoils the industry. However, when few firms are allowed to operate in the market, this increased productivity.

Conclusion

Year 2008 marked the worst performance in the airline's industry when profit margins evaporated significantly. US airline was facing stiff competition at that time because many other companies have joined the market. These firms came up with strategies such as flight cost reduction, which was unheard of before. Major companies found it difficult to compete effectively because they had already joined. Year 2008 marked the worst performance in the airline's industry trade unions that restricted them from doing certain things. The airlines applied strategies such as route strategy, price reduction strategy, formation of mergers and acquisitions and the differentiation strategy. However, most of these strategies did not work out well and the firm continued to register losses. 2007/ 2008 economic down turn also affected the airlines. This is because this was followed by hiking fuel prices, which greatly affected the airplane industry. There is, however, hope, the industry's profitability will improved if certain strategies are put in place. These strategies include cutting down of cost such as employment costs, reduction of fuel prices by the government, regulation of the industry, and failure to purchase unnecessary and inefficient capital equipment.

Bibliography

Class Text book. Case 3: US Airline Industry. Pp. 32-45