

Investigation of british airways plc strategy

Environment, Air



Flying an extensive route network of more than 300 different destinations in more than 70 countries, with nearly 250 aircrafts in service, British Airways is today the largest airline in the UK and the leader in terms of transatlantic flights globally. They are a group mainly based in Heathrow Airport, London Gatwick and Manchester, where they operate international & domestic scheduled air services for carriage of passengers, freight & mail.

In addition, British Airways is part of the oneworld alliance that together comprises 700 destinations. Founded in 1999, American Airlines, Cathay Pacific, Finnair, Iberia, Japan Airlines, Lan Airlines, Malév, Qantas and Royal Jordanian are also members of this association. The establishment of this kind of business partnership benefits customers expanding their access to a much wider network of destinations.

In terms of shareholding, for instance, the group has participation of 13.5% in the Spanish airline Iberia and 15% in Flybe. According to Key Note (2009), 'other British Airways ventures include a 10% stake in Eurostar (UK) Ltd as part of the InterCapital and Regional Rail alliance. BA also operates a number of subsidiaries and franchises organisations, for example, British Airways World Cargo, BA Cityflyer and OpenSkies.'

BA's financial overview defined by Key Note (2009) says that in the year ending in 31st March 2008, 'British Airways PLC increased its turnover to £8.76bn from £8.49bn in 2007. Pre-tax profit increased to £922m in 2008 from £611m in 2007. In the year ending 31st March 2009, turnover was up to £8.99bn and there was pre-tax loss of £401m.' The company's annual report of 2009 describes in more details that 87.1% of this revenue is from passenger

traffic, 7.5 % from cargo and 5.4 remains from other activities. The great financial results in the year that anticipated the credit crisis, a record of profitability in BA's history, left the company in a good position to a much harder period that should arrive in 2008/09.

The airline industry

Key Note (2009) considers Aviation an important sector of the economy, enabling people to visit countries it contributes to the development of other sectors and to warm the economy in general. It is a competitive field which has been recently affected by the low-cost companies, specially the scheduled flights market, where price pressure has being on emphasis influenced by short-term issues as, for instance, the economic recession, oil price fluctuation, government taxation and international environmental and health concerns.

In accordance to Key Note, the number of companies on the air travel market significantly increased since 2004, the main reason to explain the expansion was the increasing operation of non-scheduled flights, which represented 48.7% of the overall total on that year and 63.9% in 2008. Even though the rising demand stopped in 2008, this period was a continuous growth for airline enterprises, companies were still able to operate revenues of £18.25bn that year, which means an increase of 6% on 2007 figures.

In summary, all the positive results are certainly a consequence of globalisation, the airline industry has an important role in this process as it

stimulates tourism, global trade, foreign investments and therefore despite the recent economic recession it remains a large and growing industry.

Environmental Influences

Political and Legal

There have been some major political issues since the start of the millennium, which have affected the airline industry and British Airways in particular. One specific event was the September 11th 2001 terrorist attack to the world trade centre in New York and the London attack on July 7th 2005, which have resulted in introducing new regulation and security procedures in European countries and the United States. The new regulations have come into effect in 2006 to try to combat the threat of terrorism and illegal immigration which have indirectly affected the buyers' travelling confidence (BA's Annual Report).

In addition, the 2003 war in Iraq and, the political situation in the same nation have contributed to drive oil prices high and therefore, higher cost of fuel for airline companies were experienced.

In recent years, substantial deregulations like " open skies agreement 2008", has given more opportunity to airlines and also had a great impact on the long-term business strategies in British Airways. In addition, there are some legal factors affecting BA which are as the results of trade unions' power in the UK. British Airways has suffered significantly from the strikes over the last decades which are believed to be taken place under the implication of trade unions. The strikes are mainly concerned with the employee rights, environmental and ecological issues (Clarke, 2007).

According to Key Note, from November 2009 the new Air Passenger Duty (APD) will be implemented increasing charges applied for every passenger flying from an UK airport. This measure is going to be based on distance and will make long flights significantly more expensive, which consequently might reduce overseas travellers demand. Moreover, increasing government taxation might affect competitiveness against other transports in the domestic market, as can be observed in the economic effects below.

Economic

With the economic downturn in 2008 the demand for air travel declined, this is due to the lower demand by business travellers as a cost reduction strategy of their organizations. Key Note defines the effects of the current recession as one of the worst experiences passed by the air travel trading market, specially occurred because of the incremental rising of oil price in the recent past years. Companies were vulnerable to surges in oil price, what could easily affect their trading and profitability. Even though it has fallen since the peak of nearly \$150 a barrel during 2008, many companies were locked with fuel bills acquired through hedging into higher prices. Lastly, the financial impact caused by the global recession might persist until 2010/11.

Apart from the economic downturn, according to features presented by the Consumer Price Index (CPI), in comparison to other forms of transport, the air travel industry had its prices increased by more than a third (34.3%) in 2008, against for instance, annual increases of 4.3% and 6.8% of road rail and sea, respectively (Key Note, 2009).

Social

As BA is a global organization operating in different countries it needs to consider different social and cultural factors. These factors are important as they can affect customer needs and the size of potential market. Nowadays, for example, the changes in demographics has changed the customers' needs with new life styles, tastes and fashions, customers seek opportunities to go for long-haul destinations interested in new holidays places.

Since 2001, after the terrorists' attacks in the US, Great Britain did not suffer such decline in the percentage of adults travelling by air. In the year ending in March 2008 this percentage fell to a 3-year low of 47. 3%, making it the first annual fall in 8 years (Key Note, 2009). Despite the fact that the domestic demand suffered a considerable decline, air travel is very popular among UK costumers and often the only way of transport to international destinations. International scheduled flights are mentioned by Key Note as the growth sector of the airline industry. In 2008, more than 83 million passengers represented 5. 1% increase in demand for international travels, a considerable part of that can be attributed to the large volume of tourists visiting the UK even in a time of economic crisis.

Following the same idea, although the industry expected a decline on the number of passengers uplifted until the end of 2009, this situation will be surely recovered from 2010. The UK is a leading tourist and business destination and a boost is forecast on 2012 when the London Olympics should provide a significant increasing on air travel, therefore the number of

passengers uplifted is expected to jump from 123.5 million in 2009 to 134 million in 2013, according to Key Note.

Finally, an issue that was recently observed in a global perspective was the spread of diseases such as the Swine Flu; such phenomenon might reduce travel and tourism, consequently affecting the airline performance.

Technological

BA is not different from any company of the 21st century. The aviation sector has grown together with the fast advances in high technology systems, and nowadays it is considerably dependent on its IT structure. At the same time IT is a defining agent in BA's strategic position contributing to various facilities that comprise customers' high expectations and satisfaction; on the other hand BA is exposed to a great risk whether this system comes to a failure. Hence, it is extremely necessary that the organization prepares itself through prevention and recovery plans in order to minimize reputation impacts among customers in case of disruption.

For example, different strategies (operational, commercial and social) mentioned in this report could not be possibly implemented if the technology was not available; actually this tool is essential for the company to follow the rise in customer needs as well as their competitors' innovations.

In the aviation industry, technology plays a significant role. Premium airlines want to serve the passenger a convenience journey, starting from the booking to the entertainment onboard, what can only be possible through incremental advances in IT solutions. In addition, efficient engines can

consume less fuel and gives more mileage. It can reduce the cost and fulfil quality. BA is trying to minimize the average noise per flight it operates by 15% by 2015 with the use of new technology. Lastly, all the investments in technology helps air travel to remain as one of the safest modes of transport.

Environmental

Regarding environmental concerns, Key Note (2009) states that the EU is planning to include aviation as part of its emissions trading scheme, this can be considered a reaction to respond critics received for the reluctance of airlines in taking climate-change initiative. Cooperation between BA and Virgin proposes a carbon trading agreement; they are among other companies who volunteer to initiate a process to develop the emissions trading system to the airline industry.

Because of the global warming, protection of environment has become a substantial issue for the organizations to consider. Today many of the airlines are trying to reduce CO₂ emission and BA is one of them. BA's long term goal is to reduce the Carbon Dioxide by 50% by the year 2050. BA also aims at zero waste to the landfill by the end of 2010 in the UK and reuse or recycling of all the waste.

To the airline industry, severe changes in weather conditions represent lost of revenue, things such as heavy snow might disrupt air schedule and lead to operations' disruption.

Industry Structure and Attractiveness

Porter's five forces model facilitates an analysis on the competitive environment as well as identifying the forces that affect the level of competition in the airline industry.

Existing Competitive Rivalry in the Industry

Air travel industry is a large industry with high speed of growth which results in creating more opportunity for competition. According to the annual report, BA faces fierce competition in most of its markets whereby different routes have different levels of competition. The high Competition in short-haul market comes from the free market for internal flights, where European airlines are allowed to choose any route within Europe and set its own fares. Additionally, the emergence of "no frills" companies like EasyJet and Ryan Air contributes further to the intense rivalry in the short-haul market. The longhaul market is significantly influenced by deregulation. Due to the EU-US Open Skies liberalisations, which allow any EU or US airline to operate flights to US from Heathrow, the competitive environment on transatlantic routes increased dramatically. However, there are few international routes with competition restricted to national airlines.

Threat of Entry

Most new comers to the airline industry would find it difficult to enter the market as it needs high investments to establish a competitive structure, for example, an aircraft fleet covering the airline's route network. Over the last decade, however, there were a number of newcomers within the low-cost

niche; EasyJet and Ryan Air in the European market have dominated the segment.

Established airlines, while dominating the market, would not allow new companies to easily compete with them. They would always defend themselves strategically through price reductions, special offers and most of the times a better service. Lastly, these days, it is even more costly to adopt new requirements regarding legal concerning over health and safety regulations that are in evidence in this industry worldwide.

The power of Buyer

Due to the high competition and an increase in the number of airlines in today's market the buyer has got a large number of airlines to choose from and therefore, has got high power.

Therefore, the quality of service the customers receive has become even more important these days. The switching cost for the leisure travellers is very low and so they can easily switch from one airline to the other. As a result, airlines like British Airways would focus on keeping loyalty of business travellers who tend to travel more frequently by introducing incentives such as air miles, hotel reservations or car hire.

Power of Supplier

Bargaining supplier power will be high with the dominance of Boeing and Airbus as the suppliers of aircraft and there is not much of competition amongst suppliers, therefore, there is a low possibility of vertical integration.

Threat of Substitutes

As the product and services in the airline industry are similar in nature, therefore, the threat of substitute is considerably high. This can be presumably higher for the local airlines for example for UK or French local airlines. Euro star as train service operating between London and Paris can be considered a threat. However, for the international airlines operating in long distances, trains and sea craft cannot be considered as substitution.

Travelling with airplane is no longer a luxury; therefore, some people prefer to travel with cheaper airlines which are sometimes even cheaper than travelling by car or train. These cheap airlines have made the threat of substitutes lower than before. However, there is still higher expectation from airlines, therefore, better service and higher frequency of flights would help lowering the threat of substitute.

Capabilities and Core Competences

Strengths

British Airways PLC is the largest UK airline with £8. 75bn sales in the year ending 31st March 2008, it is nearly four times the second-largest carrier, easyJet with £2. 35bn. This difference can become even greater as according to Key Note, British Airways is allowed by the Government to merge with Iberia and maybe become a Spanish company.

What makes BA successful is the company's capability to effectively deploy its resources through its activities and processes. Although financially the company goes through very difficult times, operationally however, BA is achieving levels of excellence never experienced before. BA has made

remarkable operational progress during the last year. In accordance to its annual report last year, improvement of 20% in punctuality is achieved and, nearly 82.5% of the flights at Heathrow, Terminal 5 have delay less than 15 minutes of their scheduled time. In addition, 72% less mislaid or misdirected bags during the year compared with the previous one (British Airways Annual report 2009).

Furthermore, according to the company's investor relations website, British Airways launched a 32-seat flight from London City airport to New York that for the first time ever will provide internet services on a transatlantic flight, an exclusive service to attend the business demand. This can be certainly an example that any strategic change that will be taken by BA is going to happen gradually, without leaving behind the nature and history that makes the company a synonym of high quality services.

In addition, a unique resource that underpins BA's competitive advantage and represents their major strength is the company's long-established brand, which is synonym of high quality services and represents BA as a high-performing, customer orientated, and global premium airline. During 2008 the satisfaction level across BA's network has risen to 72 per cent.

Furthermore, the opening of Terminal 5 at Heathrow and the way BA organises its operations and services at the new Terminal delivered a steady rise in customers' satisfaction reaching 76 per cent at the end of 2008.

During its first year of operation Terminal 5 has served 21 million passengers (British Airways Annual report 2009).

Moreover, BA's participation in oneworld alliance builds unique relationships with other airlines and allows the company to offer its customers much wider network of destinations. This business relationship, along with the ability to manage effectively its resources represents a core competence, which helps BA to build its competitive advantage over other airlines. BA's strong fleet base allows the company to serve its robust rout network. At the end of 2008 the company possess 245 aircrafts. Although BA experiences difficult financial times, the company continuously invests in new aircraft, its lounges, a new in-flight entertainment system, cabin upgrades across their longhaul fleet and premium service training in order to further increase the customer's satisfaction and sustain competitive advantage (British Airways Annual report 2009).

Weaknesses

Brand erosion

The merge with Iberia and the joint ATI application could cause brand erosion, which will adversely impact relationship with customers and will result in decrease of revenues (British Air ways Annual report 2009)..

Breakdown in the bargaining process (unionised workforce)

BA planes to cut costs wherever it is possible in order to survive the difficult financial times. In this respect, the airline plans to cut 1, 700 jobs and to freeze pay for current staff, in accordance to BBC News. This will increase the risk of workers' strike actions, which will interrupt operations and adversely affect business performance (British Air ways Annual report 2009).

Failure of a key supplier

BA's sole source of in-flight meals at Heathrow was Gate Gourmet. In 2005 Gate Gourmet failed to supply BA with the necessary in-flight meals due to internal argument with its staff over working conditions, which led to a strike supported by BA's own workers. This caused major operational disruption in BA, which resulted in huge additional costs of 40 million £ (Waters, 2007). This is one example for how a failure of a key supplier may cause disruption to the operations of the airline and adversely affect business performance. Another such example is BA's dependence on fuel supply. Any problem as contamination or breakdown in the infrastructure that provides jet fuel to Heathrow will cause a huge operational impact.

Failure to prevent or respond to a major safety or security incident

A major security failure could consequently damage the reputation of BA as a high secure airline (British Airways Annual report 2009).

Failure to adopt an integrated environmental strategy

BA markets itself as being a responsible airline. BA has set industry-leading targets for reducing its carbon emissions from 110 to 83 grammes per passenger kilometre between 2005 and 2025 and to halve its net CO₂ emissions till 2005. Failure to implement this strategy could damage the reputation of BA as a responsible company (British Airways Annual report 2009).

Substantial debt burden

BA's net debt in 2009 is £2, 382 million, which represents an increase of £1, 072 million in comparison to the previous year. Accordingly, the company's net debt to total capital ratio is 27. 6% higher than the previous year. The substantial increase in debt obligations means that considerable part of BA's operational cash flow will be spent on interest, principal and lease payments. This not only lowers the ability of the company to finance working capital and other general corporate requirements, but also limits its flexibility in planning and reacting to environmental changes (British Airways Annual report 2009).

Overdependence on the European market

According to Datamonitor 62. 5% of BA's profit is made from serving the European Market. Taking into consideration the current unfavourable economic situation in European, the overdependence on this weak market will prevent the company from increasing its future profits.

Organizational Structure and Processes

There are major factors that influence an organization's strategic position, for instance, it might be its overall strategic purpose and corporate governance policy, expectations of stakeholders, social responsibility and ethics are also part of this list.

The recent annual report 2008-2009 shows that BA places high importance on corporate governance. The Board is responsible for the leadership of the organization to the shareholders. Accordingly, " The Board directs the Company's risk assessment, resource management, strategic planning and

financial and operational management to ensure that obligations to shareholders and other stakeholders are understood and met” (Annual report 2008-2009, p. 56). The principal-agent conflict might arise owing to the leadership of the business by managers, whereas they might put their interests first instead of meeting shareholders interests ladder (Johnson et al., 2009). The New Companies Act from 2006 aims to overcome this problem though.

Authority and control responsibilities are determined by the clear organizational structure of BA. The company’s personnel is highly qualified which is assured through the thorough recruitment process, the internal performance appraisal system and the appropriate training requirements. The performance of employees is evaluated according to action plans and targets established by the performance appraisal system to ensure that employees have all the skills necessary to complete their responsibilities. Clear and specific objectives are established for the staff in order to make their contribution to the overall performance of the company more transparent. This increases the motivation and the responsibilities awareness of the staff. Also the staff is trained to behave in a way that will create a warm and friendly atmosphere in the work place and that they are happy to work for BA.

In order to measure its performance and to make its managers accountable for delivery of the set targets BA uses a comprehensive management accounting system. This system provides financial and operational performance measurement indicators which allow the company to regulate

its expenses more accurately and make financial decisions more precisely. 'Customer recommendation' carried out by an independent research company assessed the number of satisfied customers and is supposed to be a one of the most significant indicators due to the potential to affect the profitability in the future. Company's operations are evaluated via a broad scope of methods across a variety of levels; however, the most important is departure functionality. It consequently shows that the other processes are performed in a high standard and ultimately effects customer satisfaction. (British Airways Annual Report 2009).

British Airways Current and Future Strategy Perspective

Based on Porter's generic strategies, British Airways strategic analysis is built under the importance of employing a plan through one of the three strategies, Differentiation, Overall Cost Leadership and Focus. Those three strategies are relevant factors on the process of outperforming competitors in the industry. Even though it is possible to pursue more than one strategy, this is rarely seen because of their own different characteristics as will be evident on this topic.

After the initial analysis of British Airways current situation in the air travel industry, it is clear that during all its modern history as a passenger carrier, the company stayed committed to its principles and invested on what could enforce its plans to continue being very successful. As a leading airline company its brand was always associated with the best service and treat available to customers in the market. In this point of view, the company

service differentiation strategies and development of new services appear to be the considerable competitive advantage to outperform its competitors.

There are some authors that argue in favour that differentiation and overall cost leadership are not always mutually exclusive although it is very complicated to match both strategies in most industries. However, the market is showing a rising positive trend to companies with an overall cost leadership strategy and they are growing their market share considerably. It becomes obvious that BA could not ignore low-cost rivals if the company wants to sustain its market position. Therefore, BA established a low-cost company called Go, created in response to falling profits after 1998 due to the emerging no-frills companies. Go was later sold to easyJet in 2002 - it was a proof that an opposite price-based strategy is difficult to be applied even creating a new company under the same governance. The cost leadership strategic failure pushed the company to focus on differentiating its services even more. Nevertheless, in some price sensitive segments the differentiation strategy might not be sufficient to compete successfully. Therefore, BA concentrates on long-haul flights where there are not "no frills" companies. Furthermore, the company operates slots on popular and convenient airports such as Heathrow, what further attracts some short-haul customers (Kumar, 2006).

Additionally, BA has successfully segmented its markets by offering different ticket classes which allows them to attract price sensitive customers from no frills airlines as well as manage to cover costs and increase revenues. The airline also succeeded to reduce costs through the successful

implementation and management of an online booking system. BA tries to increase the economies of scale by raising the frequency of flights to popular holiday destinations like Caribbean islands or seasonal increase in the frequency of flights to religious destinations like Mecca and Vatican (Kumar, 2006). All these strategies made BA very successful during the last few years (in 2007 BA achieved the highest profit in its history) and created competitive advantages over company's traditional and low cost competitors.

Reducing cost activities are taking place since 2008 over the company's renewal strategies in order to fight against the short-term crisis effects. Job-cutting would increase profitability within the company in short term, but this could lead to decrease in the quality of customer service. Furthermore, job-cuttings would lead also to confrontations with unions and employee strikes, which will disrupt the company's operations. Hence, this change in the organisational structure could damage BA's image reputation as a premium service airline in the long run. Other problems are the company's £2. 7bn pension deficit and its high debt burden.

On the other hand, in an innovation sense, after huge investments and improvements on operating activities, a proof of the continually effort to maintain its first quality standard is the new terminal in Heathrow airport, which brings lots of new facilities to customers and improvement of conditions at the working place to all its employees. Despite the impact of the recent recession, in comparison to easyJet, British Airways is focused on pursuing to offer its customers the best possible service that makes its brand

a synonym of first class, the innovation appears into new customer needs, environmental forces and trends to reinforce its differentiation for which people are willing to pay more.

To cope with future environment trends BA has started tuning its current strategy and differentiating itself from competitors according to new patterns of responsible attitude, especially within big companies. To adapt its structure to a 'green' efficient standard is not an easy process and requires huge investments. The environmental concern is a topic highly discussed worldwide and has become a popular issue; BA is certainly paying attention to that and has the objective of becoming reference as the most responsible airline. Sustaining and developing its current strategy BA believes that is the right decision in order to achieve always the best possible satisfaction of its stakeholders.

To illustrate British Airways' future actions, for instance, Terminal 5 is a set of procedures already working that underpins BA's long-term goal of creating a world-leading global premium airline with a reputation for being the very best at meeting its customers' needs, according to its website, for instance:

â[™] At T5, most of the rainwater will be collected and re-used for non-potable uses.

â[™] 85% of T5's heat will be supplied by excess heat produced from the Heathrow heat and power station.

â[™] 30, 000 native woodland plants and 4, 000 trees and shrubs are being planted around T5.

â ^™ Smarter runway and airport design means aircraft engines idle less, reducing emissions. Aircraft will do less taxiing too.

â ^™ T5 offers 96 Check-in Kiosks designed to eliminate queuing.

â ^™ The rapid transit system connection between the two buildings making up T5 means you'll move swiftly and smoothly to where you need to be.

â ^™ The baggage system has been designed to move your baggage efficiently to the aircraft ready for departure and to minimise waiting time when you land.

In addition to that, a new internal program developed in parallel with the 2012 Olympic Games' spirit has definitely enforced the importance of BA's culture, which has the customer as its core. Compete 2012 aims to inspire the spirit of team work and competition in all corners of the company, and as a result establish a level of excellence that competitors aspire to. The strategy of being one of the UK sponsors and the official airline for the event matches BA's future vision and reinforce its credibility among its target customers.

Above, they are examples of the evolution in British Airways culture that, when added to the company's capabilities and competences and the strengths earlier described, its value chain can be clearly understood. The evolution of BA's strategy easily refers to Porter's conclusion that 'competitive advantage frequently comes from perceiving new ways to configure and manage the entire value system'.

In terms of suitability, BA's current strategy successfully exploits its core competences and unique resources and allows the company to respond appropriately to key environmental trends such as economic downturn, political and legal changes and changes in social perceptions. Also their strategy is aligned with their culture. However, the current differentiation strategy could prevent some of BA's weaknesses such as brand erosion. In terms of feasibility of the strategy, BA has the financial resources and competences to invest and differentiate furt