The low cost airline air asia

[Environment](), [Air]()

The low-cost concept became a moneymaker in the United States, where it was pioneered in the 1970s by Southwest Airlines, the model for budget carriers elsewhere like Ryanair and easyJet in Europe.

Definition of low cost airlines

A low cost airline generally has many features that differentiate it from the traditional carriers. These features include ticketless travel, online ticket sales, no international offices, no frequent flyer points, no free food and beverages, no inflight magazines, no club lounges, use of secondary city airports.

Not all low cost airlines have these features, and not all airlines that have some of these features are low cost airlines. For example, Virgin Express is a low cost airline, but it still offers complimentary coffee and inflight magazine, and they are based at Brussels primary airport.

Case Study-AirAsia

Story of AirAsia

Air Asia, as the second Malaysian National Airline, provides a totally different type of service in line with the nation's aspirations to benefit all citizens and worldwide travellers. Such service takes the form of a no frills – low airfares flight offering, 40%-60% lower than what is currently offered in this part of Asia. Their vision is " Now Everyone Can Fly" and their mission is to provide ' Affordable Airfares' without any compromise to Flight Safety Standards.

The story of emergence of AirAsia is similar to Ryanair, since both carriers underwent a remarkable transformation from a money-losing regional operator to a profitable, low cost airline.

AirAsia was initially launched in 1996 as a full-service regional airline offering slightly cheaper fares than its main competitor, Malaysia Airlines. Before 2001, AirAsia fail to either sufficiently stimulate the market or attract enough passengers from Malaysia Airlines to establish its own niche market. The turnaround point of AisAsia is in 2001, while it was up to sale and bought by Tony Fernandes. Tony Fernandes then enrolled some of the lending low-cost airline experts to restructure AirAsia's business model. He invited Connor McCarthy, the former director of group operation of Ryanair, to join the executive team. In late 2001, AirAsia was re-launched in Malaysia as a trendy, no-frills operation with three B737 aircraft as a low-fare, low-cost domestic airline.

Opportunities faced by AirAsia in light of external development

Low fare of Indonesia-Malaysia trip

The fare for a Jakarta-Johor Baru trip costs Rp 100, 000 (RM 88. 88 one way). And charge Rp 150, 000 for a Bandung-Kuala Lumpur flight, and Rp 300, 000 for a Surabaya-Kuala Lumpur trip, whereas a Jakarta-Kuala Lumpur air ticket from Malaysia Airlines available at travel agents cost Rp 1. 4 million. Meanwhile, Lion Air on the same route, charged Rp 1. 05 million. The low fare provided by AirAsia helps it open the Indonesia market.

Low fare of Singapore-Bangkok service

AirAsia will increase its services between Singapore & Bangkok by introducing a 2nd daily flight to its existing schedule. This recent development came barely a month after Thai AirAsia operations started its first international flight to Singapore in early February this year. AirAsia is offering its guests promotional fares to/from Singapore- Bangkok from SGD$23. 99 (THB 499) one way from the 28th March to 30th Oct, 2004. It is much lower than the lowest fare SGD$56 offered by full-service carrier. This helps it open the Singapore market.

Political connections

AirAsia hold 49% of Thai AirAsia with 1% being held by a Thai individual. The remaining 50% is held by Shin Corp. which is owned by the family of Thailand’s prime minister, Thaksin Shinawatra. Shin Corp. has financial strength, synergy in ingormation technology and telecommunications, which support AirAsia Internet and mobile phone bookings. Shin Corp. allows subscribers of the Shin mobile phone flagship, Advanced Information Service, being able to reserve tickets through its short-messaging service (SMS). AirAsia with its politically powerful backer may well grow up to bite. This helps it open the Thailand market.

Malaysian government support

The Malaysian government supported the establishment of AirAsia in 2001 to help boost the under-used Kuala Lumpur International Airport. AirAsia’s flights from Senai are meant to develop Johor into a transport hub to rival

Singapore. AirAsia, therefore, can provide an alternative route to travel to Bangkok, by using Senai Airport in Johor Bahru, in southern Malaysia.

Opportunities faced by AirAsia in light of internal development

Issue of IPO

Kamarudin Meranun, AirAsia's Executive Director announced the appointment of Credit Suisse First Boston (CSFB) and RHB Sakura Merchant Bankers (RHB) as the bookrunners for the company's upcoming Initial Public Offering (IPO).

The IPO strengthens AirAsia balance sheet, further cuts its existing low costs at 2. 5 US cents per ASK and accelerates our growth plans throughout Asia. The IPO also allows AirAsia to expand its fleet of 18 Boeing 737-300s.

Political connections

Thai AirAsia is a join venture established by AirAsia with Shin Corp. Shin Corp. is owned by the family of Thailand's prime minister, Thaksin Shinawatra, and about 900 million baht will be invested in Thai AirAsia over a five-year period. Shin Corp. oversees the finance and administration of Thai AirAsia while AirAsia shoulders the responsibility for marketing and operations. Shin Corp. has financial strength and supports AirAsia to grow. AirAsia with its politically powerful backer may well grow up to bite.

Challenges faced by AirAsia in light of external development

Indonesian habit

Preferences of Indonesian passengers are quite different from the concept of cheap air travel without extra service for the passengers (free snacks and drinks), and also their reluctance to bring light baggage.

AirAsia prefers passengers with very light and minimum baggage. If this is the case, it may not last long.

But Indonesian domestic airline companies are able to provide value-added extras like food and beverages as part of their service to the passengers, although at a relatively higher cost.

The comparative edge of Indonesian domestic airline companies compared to AirAsia concerns habit (culture).

Furthermore, Indonesian domestic airlines were already trained with the low-cost air travel concept, known as tariff war. They have proved themselves as immune, and managed to survive.

Last but not least, the Indonesian government or domestic airline companies had never announced the availability of a low-cost airline company of the country. All these affect AirAsia growth in Indonesia.

Singapore government rejection

Initially, AirAsia wanted to start flights from the southern state of Johor, near Singapore, it hoped to attract passengers by running a convenient bus service to the city-state. However, Singapore quickly quashed that idea. The Singapore government said it would not approve a bus link for AirAsia because it was not ‘ in her national interest’, reflecting fears that Singapore’s

Changi airport would lose business to Johor’s new Senai airport. This makes AirAsia cannot abandon the use of Changi airport, and therefore suffer from a higher cost.

This is because AirAsia flying to Singapore needs to suffer from flight congestion of Changi. Changi has drawbacks of flight congestion that could prevent the quick turnarounds essential to keeping down costs. AirAsia finds it stuck between big planes and circling to wait for a slot to open up, which means extra fuel costs. Moreover, the SGD$21 departure and security tax of Changi is too high for AirAsia low-cost operation. AirAsia had asked the Singapore government to waive the fees, however, a request that was not only rejected but also criticized.

Besides Singapore – Bangkok, AirAsia now provides an alternative route to travel to Bangkok, by using Senai Airport in Johor Bahru, in southern Malaysia. Seeking to cater to the different markets, fares for Johor Bahru-Bangkok are generally 20 % lower in comparison to Singapore – Bangkok. AirAsia currently operate daily flights to Bangkok from Johor Bahru. However, the choice proved unpopular, as the route failed to attract Singaporeans because of the additional cost and inconvenience of having to travel in and out of Malaysia by road. All these affect AirAsia external growth.

Minimum air-fare rates

AirAsia faces challenges finding open takeoff and landing slots at opportune times, and Thailand’s regulation that sets minimum air-fare rates. Although Transport Minister Suriya Jungrungreangkit said the current minimum air-fare regulations will be scrapped to open up the market, he couldn't name a date when this will be done. This seems to be favoritism toward Thai Airways International's domestic operations, and affects Thai AirAsia to compete in the Thailand market.

External Changes which have impact on AirAsia

Asia's middle class growth

Low cost airlines are anticipated to have greater potential in Asia as there are many Asian cities with a population above one million people each as well as a rising middle class population. This growth of middle class in Asia provides a huge market potential for AirAsia to grow.

However, as the market is becoming larger, more airlines or new comers would like to get a piece of the action. For example, Budget airlines, it is estimated, will capture at least 25% of Asia's air travel market within next 10 years and a lot of that will be new, not diverted, traffic. Therefore, AirAsia will face more competitions at the same time.

Besides the low cost airlines, AirAsia still needs to compete with the conventional carriers. Although extra passengers of the low cost airlines will be coming from the new demand to be created by the low fares, the growth may not be entirely ' stolen' from big flag carriers.

Actions of Changi and nearby airports

The growth of low cost airlines in south-east Asia has a significant effect on which airports will dominate the regional aviation market. Low cost airlines are seen as helping funnel more passengers to airport hubs. Therefore, there is a realization among regional governments that they need smashing airports and feisty carriers or they are going to miss out big time. Therefore, these governments are more willing to support low cost airlines. For example, the Malaysian government supported the establishment of AirAsian in 2001 to help boost the under-used Kuala Lumpur International Airport, and Thai premier's Shin Corp. forms a join venture with AirAsia that would benefit Bangkok's new airport and create a new hub at Chiang Mai. Therefore, under this situation, it helps AirAsia grow in Asia.

Moreover, as there is a growth of several south-east Asian airports, this poses a challenge to the status of Singapore's Changi airport as a regional aviation hub. These airports include Johor's new Senai airport in southern Malaysia, Bangkok's new Suvarnabhumi airport which will be able to handle 45 million passengers when it opens in 2005, Bangkok Don Muang which recently overtook Changi in passenger numbers, etc. To maintain Changi's position as the air hub in the region, Singapore is proposing a budget airline terminal at Changi by 2005 and lower passenger taxes to attract low cost airlines. This helps AirAsia grow and lower the cost.

Actions of existing airlines

The existing airlines in south-east Asia have several actions to compete with AirAsia, for example, some have launched a low cost airline to fight with AirAsia.

Singapore Airlines launched a low cost airline subsidiary, Tiger Airways, in the second half of 2003, only months after the scheduled launch of ValuAir set up by one of its former executives.

Orient Thai Airlines launched a new low cost airline subsidiary, One-To-Go. One-To-Go operates with a fleet of six Boeing 757-200s and match any fares that Thai AirAsia offers.

Thai Airways have frequency and capacity to offer to their 13 domestic destinations. They also have, during the past two years, worked to improve operational efficiency, slashing unprofitable domestic routes, increasing flights on busy routes, strengthening yield management and controlling costs.

All these make AirAsia face a huge competition.

Critical success factors in the Low cost airlines in Asia

Reduction in operational cost

Low cost airlines strive to achieve the lowest possible price for their products and services. Low prices cannot sustain unless the company maximizes its operational efficiency.

The success factors of Asian low cost airlines in reducing their operational cost include:

Service savings (no frills cabin service and extensive use of outsourcing)

NO-frills include:

NO drinks, NO food, NO headphones, NO newspapers, NO movies, NO VIP lounges, NO expensive offices, NO mileage programs, NO seat allocation, NO children's fares, NO paper tickets (Electronic tickets only), NO connecting flights (All flight-legs must be booked independently)

Operational savings (point-to-point services and uniform fleet)

Overhead savings (internet sales and streamlined bureaucracy)

We can compare the operational cost in terms of costs per available seat kilometer (ASK), a measure of the running cost of the airline. For instance, Ryanair in Europe is almost half of the ASK price comparing with the full services airline. The average fare offered by Air Asia in Malaysia is 40-60 % lower than its full-service competitor.

Competitive Ticket price against traditional full-service airline

Low cost airlines begins with two initial cost advantages arising from the very nature of their operation: higher seating density and higher daily aircraft utilization. By removing business class and reconfiguring their aircraft, low cost airlines can increase the number of seats on their aircraft. Seat pitch of a low cost airline is usually 28 inches, compared to a traditional conventional economy class pitch with 32 inches. Doganis (2001) calculates that should be able to operate at seat cost that are only 40-50 % those of mainline rival. Combining the load factor benefit and beneficial distribution cost, low cost airline's cost per passenger can reduce price by one-third of conventional airline.

Flying out of secondary airports

Many low-cost airlines keep expenses down by flying out of secondary airports, avoiding major hubs where takeoff and landing fees are much higher while still getting passengers close enough to their destinations.

The travel distance is short

As the routes offered by low cost airlines are mainly short, domestic routes which may only take one to two hours, travellers might be fine with no amenities on flights

Success factors in AirAsia

Absolute Cost Advantage

Low cost per average seat kilometer

AirAsia focused on ensuring a competitive cost structure as its main business strategy. It has been able to achieve a cost per average seat kilometer (ASK) of 2. 5 cents, half that of Malaysia Airlines and Ryanair and a third that of EasyJet. AirAsia can lease the B737-300s aircraft at a very competitive market rates due to the harsh global market conditions for the second-hand aircrafts because of the September 11th event in 2001. On the other hand, the operating cost of the company is also dropped drastically.

Low distribution cost

AirAsia focus on Internet bookings and ticketless travel allowed it to lower the distribution cost.

Attractive ticket price

With the average fare being 40-60 % lower than its full-service competitor, AirAsia has been able to achieve strong market stimulation in the domestic Malaysian air market (Thomas 2003). For instance, the fare for the trip from Kuala Lumpur to Penang on AirAsia starts from 39 ringgit. Comparing to trip by bus charge 40 ringgit and 80 ringgit by car. The effect of attractive low fare is more travelers switching from bus to air, similar case as Ryanair in Europe.

Good Management Team

AirAsia value proposition is more sophisticated than Ryanair placing equal emphasis on brand reputation and customer service/people management, by a senior advisor to AisAsia's top management team. AirAsia pursue a Ryanair operational strategy, Southwest people strategy and an Easyjet branding strategy.

Weakness

Fair availability

The availability of AirAsia is not good as traditional airline as it only provide unique aircraft. However, it cannot be the cost leader if it offers customized features or comprehensive support which will result in increasing operational cost.

However, focus on a specific customer may avoid straddling.

Case of straddling

A Japanese low cost airline, Skymark, trying to be everything to everyone targeting the broader customer and offering limited special features (satellite TV, Business class and charter operations). The result is failing to both cost efficient and price competitive rendering it vulnerable to market forces and customer demand (porter1996; Lawton 1999).

Major strategic directions recommended

Open more Asian market

Low cost airlines are anticipated to have greater potential in Asia as there are many Asian cities with a population above one million people each as well as a rising middle class population. It is time for AirAsia to exploit the potentials of affordable air travel by Asia's growing middle class. Besides starting services to the Pearl River Delta in south China in 2004, AirAsia can expend its services to the coastal cities in China.

Besides the growth of Asian middle class, the liberalization of aviation sector of India is another reason for AirAsia to open more Asian market. The Indian government has liberalized the aviation sector long dominated by the national carriers. Now, only a few low cost airlines, e. g. Air Deccan, Airone Feeder Airline Pvt Ltd, Crescent Air, have launched their services there. Moreover, the national carriers, Indian Airlines or Air India, despite their domination of the Indian skies, do not seem to be much interested in operating low-cost services. Therefore, it is a good chance for AirAsia to open the Indian market.

Join venture with Virgin Group

AirAsia should put more effort to set up a pan-Asian low cost airline with Virgin Blue, which is a low cost carrier of Virgin Group serving Australia and New Zealand mainly. Virgin Blue has suggested it may extend services to south-east Asia. Therefore, setting up a join venture with Virgin Blue can help AirAsia to grow in Asia even further, and help Virgin Blue to extend services to south-east Asia.

Recommendations to maximize competitive advandages of AirAsia

1. Enforce Political advantages

AirAsia established a join venture, Thai AirAsia with Shin Corp. Shin Corp. is owned by the family of Thailand’s prime minister, Thaksin Shinawatra, and about 900 million baht will be invested in Thai AirAsia over a five-year period. Shin Corp. has financial strength, synergy in ingormation technology and telecommunications, which support AirAsia to grow in Thailand. AirAsia with its politically powerful backer can well grow up to bite, and therefore it should enforce such political advantages in order to extend the growth in Thailand.

Furthermore, AirAsia should use its Thai subsidiary, Thai AirAsia, to claim the use of Thailand’s ‘ open skies’ agreements to fly to Singapore, Brunei and Cambodia, overcoming the barrier of bilateral aviation pacts that threatened to limit its growth.

Induction of smart cards

AirAsia can issue a smart card which is compatible with the existing ticketless booking.

It can offer 2 kinds of smart cards. The first kind of smart card, aimed at ordinary travellers, will offer instant rewards when topped up, offering greater value than its purchase price. For example a Bt5, 000 card may be worth Bt5, 500. The card can also be used by other people with the same family name as the cardholder.

The second kind of smart card will offer unlimited travel for frequent flyers. Priced provisionally at Bt20, 000, cardholders will be allowed make as many trips as they want within a specified period.

Conclusion

A study by the Centre for Asia Pacific Aviation (2002) confirms that Asia continues to offer attractive conditions for the air transportation industry. With thirteen out of world’s top twenty-five major urban centres located in the Asia Pacific region and a rapidly increasing urbanization trends, the Asian air travel market is bound to continue to grow. Urbanization is highlighted as one of the key drivers for the growth in air travel. It is estimated that Asia would account for 30% of the world market by 2019, or one third of growth between now and then. While the impact of SARS is going to slow down the growth of Asian regional demand, the long-run forecast continues to be very positive. These enable low cost airlines to grow even further.