

Fear of flying

As airlines fly into a stiff economic headwind, what are they doing to encourage business travellers back on board? **Alex Blyth**



The airline industry has lost more money in the last two years than it has made in its entire history,' claims Richard Goodfellow, a British Airways spokesperson. In the past two years safety fears stemming from 9/11, the war in Iraq, and now the SARS virus, have coincided with a global economic downturn and the emergence of new technologies such as videoconferencing to produce a catastrophic collapse in passenger numbers.

In the past two years Sabena, Swissair and United Airlines have all declared bankruptcy. Despite 13,000 redundancies, BA has been making considerable losses ever since the attack on the Twin Towers. In a recent statement announcing a small profit in the first quarter of 2003, senior BA executives forecast further difficulties for the industry. A few weeks ago American Airlines reported a \$1bn (£605m) loss in the first quarter of 2003. Even Cathay Pacific appears to be in dire trouble, recently announcing that, despite suspending 45% of its services, it is running at a loss of £1.9m a day. The airline industry is facing the greatest challenge in its short history. With costs cut as much as security and service will allow, many airlines are facing a stark choice between either

stimulating demand, going cap-in-hand to government for subsidies, or going out of business.

Reluctant spenders

Retaining the corporate market has always been important for the profitability of individual airlines. Business travellers pay more for their seats and large corporate accounts have had beneficial effects on cashflow and forward planning. In return, business has always appreciated the speed and convenience of air travel. However, in the current tough economic climate, there are more than a few cracks in this once solid relationship. Corporate buyers are reluctant to admit that they are spending less on air travel, but as Keith Haynes, sales and marketing director at P&O Business Travel, the UK's eighth largest business travel agents, working for companies such as Corus, The Body Shop and Asprey & Gerrard, points out: 'The Gulf War, SARS and the economic situation generally have taken away a lot of demand in the business travel market. At the very least, those factors have caused significant troughs in travel to the Far East and the Gulf.'

Richard Goodfellow at BA puts it even more starkly: 'We thought that 2000/01 was a bad year for

sales in the corporate market, but revenue in 2001/02 fell by 20% from even that low point. The problem is that travel is a discretionary spend, and as times get tougher in the corporate world so travel budgets get cut back further and further. It's a real challenge for us to stimulate this market.'

He goes on to outline how BA is tackling the problem: 'We've put a lot of effort into becoming closer to our clients, to really understanding their businesses, and adding value to the relationship. For instance, if a company is concerned about sending its executives to a particular country we will give them all the information necessary for them to make an informed decision. Apart from offering bespoke solutions like this we have done a great deal to make air travel more pleasant for businesspeople with fully equipped departure lounges and a range of top quality services on board our aircraft. Our investment in new technologies means that passengers don't lose any opportunities to do business whilst travelling with us.'

Samantha Day, spokesperson for Easyjet, outlines the very different approach taken by that company: '40% of our passengers are business travellers. We don't capture this data specifically, but estimate it based on destinations and length of stay. In the last year we saw a 32% increase in passenger numbers. Given that the overall market is declining, these figures do suggest that we are capturing a significant share of the corporate market. We're doing this because business travellers are increasingly attracted to our low-cost, flexible and convenient offer.'

'It's well known that we can cost less than many of our competitors, but businesses are beginning to realise that, unlike other low-cost airlines, we fly to airports close to city centres, and we allow flight details to be changed for only a £15 administration fee. While we need to keep our business model simple we have recently launched a business-to-business website.'

Low-cost v full service

Robert Allison, head of transportation practice at KPMG, believes that this adding of value to a low-cost proposition is symptomatic of the shifts occurring in the airline industry: 'We're seeing considerable convergence between the low-cost and full service offers. Low-cost carriers are having to address issues of frequency and network, while the full service carriers are having to look at the value of their proposition and so reduce prices.' Goodfellow accepts that BA has had to look at its charging structure: 'In the past we operated kickback schemes with corporate clients, whereby at the end of an agreed period we'd give back to clients a certain percentage of the amount they'd spent with us. In the last few years this has changed so that we now agree a discount at the beginning of the contract

and apply it to each transaction.'

However, he does not believe that purchasing decisions in business travel are driven entirely by cost: 'Business travellers are increasingly asking themselves about the hidden costs connected with low-cost travel. They are wondering about the time implications of travelling out to somewhere like Stansted, and for longer trips they are wondering about whether it might be worth paying more to sleep on the plane so that the executive is fully refreshed and ready to do business on arrival.'

Furthermore, he points out that reducing prices has a limited impact on levels of business travel: 'If we want to persuade a leisure traveller to visit New York we can run a promotion offering cheap tickets and then sell the concept by describing Time Square, the shopping and what a fantastic place it is to visit. However, regardless of how cheaply we sell tickets, the business traveller will only go to New York if there is business to be done there.'

This comment reveals the real problem faced by the airline industry: there is in fact very little they can do to increase sales. If as an industry they were losing passengers to another form of transport then they might be able to take action, but as Gareth Hadon, spokesperson for Eurostar reveals, business travel has collapsed across the board: 'We've seen a 14% drop in numbers of business passengers in the last 12 months. We've got a strong offer to those businesspeople based in central London who want to travel to Paris, Brussels or Lille and beyond. We are successful to the extent that we now have around 60% of the market for travel to Paris, but we face the same problem as the airlines – that market is in rapid decline.'

Impact of global downturn

As Robert Allison puts it: 'Fears over terrorist activity and SARS only cause short-term dips in business travel. Airlines can't try to restore numbers through reassurance because businesspeople don't need reassuring. In the same way, I've not seen any evidence of large corporates reducing their travel budgets. It's not a case of management preventing executives

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travelling. It's a case of executives not having a good reason to travel, as global activity is down.'

BA and others with a full service offer will probably continue to attract long-haul passengers who have three-hour check-in periods and so appreciate the revamped business class lounges, internet access, and laptop connections. Easyjet and



other low-cost carriers will probably continue to attract short-haul passengers who appreciate the ease of internet booking and the low prices. While BA and Easyjet seem to be trying harder than many other airlines to stimulate demand in the corporate market, they are rapidly realising that it is by and large out of their hands.

A waiting game

Airlines are beginning to accept that corporate demand will not increase until the much-anticipated global economic revival occurs. Until then they are just waiting. Sam Birmingham, a BAA spokesperson, offers encouragement for the long term: 'Business travel is a growth area. In time we'll be able to look back on current problems as no more than temporary blips. The real problem faced by the industry is not having sufficient airport authorities to cope with the growing demand.'

Keith Haynes is more pessimistic: 'At the end of the day, it comes down to supply and demand. Airlines are desperately trying to fill seats but the demand just isn't there. They've all done as much as they can to reduce costs, but we're now getting to the point where it's necessary to look at the issue of oversupply in the industry. Having American carriers propped up by their government doesn't help the industry at all. It distorts the basic laws of supply and demand.'

For the rest of us those laws of supply and demand mean we can enjoy improving facilities and falling prices. If we can find someone overseas to do business with us, that is.



Blue Fox Airlines – fledgling airline perceives gap in the business market

Undaunted by issues of over-supply in a struggling industry, a consortium has formed and is currently raising finance to launch Blue Fox Airlines. Founder and president, Michael Lord-Castle, believes that he has discovered the key to stimulating demand in the business market: 'There is a gap in the market. We will be the first airline to offer low-cost business class. We will be able to do this by not operating the traditional three class cabin. We will fly 767-300s with only 138 business class seats.'

'By eliminating the rear cabin subsidy that burdens so many other airlines, we will provide people with the service they desire at a price they'll be willing to pay. For instance we will charge only £1,350 for business class return between Stansted and JFK, around a third charged by existing airlines.'

Lord-Castle does not believe that security fears will impact on demand: 'Whilst the initial drop in traffic after 11 September was substantial on high-density business routes, where our focus remains, business travel returned to normal levels within a three to five-week period.'

Despite this, security will be just as important a selling point as price and service for this new airline: 'Blue Fox will be a very secure airline. We will not carry cargo, as it is impossible to guarantee that it is 100% safe. Our planes will be guarded while they are on the ground to ensure that only authorised personnel attend them. All onboard consumables including food and newspapers will be screened. There will be a 100% security check on passengers, but since we are a smaller operator in a niche sector this is all feasible without adding a time burden on to customers.'

Although its investment bankers are still engaged on a funding round, trying to raise the £36m required for operations to commence, Blue Fox's first flight has been planned for spring 2004. Lord-Castle is confident that the demand will be there: 'Business people still need to travel, indeed if they are to trade out of an economic downturn they may need to travel more, not less. Moreover, we believe that our unique offer will actually create a market segment that wasn't there before.'

While the rest of the airline industry waits for salvation in the form of global economic recovery, Lord-Castle prefers more positive action: 'As with any market, business travel needs stimulating. Suppliers must offer products and services that are desirable, affordable and loyalty-building if they wish to attract custom. We are very confident that Blue Fox will be seen as a major proposition that will quickly become noticed and adopted by a wide range of cost and quality conscious employers and travellers.'