

When it comes to evaluating the saturation of a given market by low cost carriers, one of the most illuminating figures is the percentage of arrivals originating from within a region. It should come as no surprise that the European market's percentage of interregional arrivals in 2005 was 86.5%, indicating that LCCs have continued to dominate the region. Ireland alone took in 7.3 million visitors in 2005, most arriving by air, and many arriving via an LCC. European travelers have also been eschewing land and water based travel in recent years - while rail and auto trips remain the most popular, the proliferation of LCCs has propelled the share of air arrivals up by more than 5% a year since 1990: more than 176 million arrivals in 2005.

Low cost carriers have driven tourism increases in Central and Eastern Europe, and have redefined the way international tourists navigate the continent. The global proliferation of LCCs, which have enjoyed marked success in the Americas and, to an extent, in Africa, can arguably be traced back to the inroads made by LCCs in Europe, but as one of the most mature markets in the world, the European LCC model is facing some emerging challenges. The industry is running out of regional markets to open - North Africa and Eastern Europe are enjoying growth, but may soon start to see smaller per-year percentage increases as the market becomes saturated. Fixed expenses (fuel and labor) continue to grow, and EU climate change initiatives threaten to saddle margin-minded LCCs with unanticipated overhead in the form of efficiency mandates and emissions caps.

In this climate, three critical components of the LCC operational model are becoming increasingly important:

- *Cost mitigation, through group purchasing and supply-chain management*
- *Developing and maximizing ancillary revenue streams*
- *Integrating both revenue opportunities and cost savings into the operating cycle as quickly as possible*

How Did We Get Here?

LCCs overtook the lumbering operational model held over from the golden age of air travel - full service lines emulating the amenities of postindustrial ocean voyages - with cost efficient aircraft and stripped-down services.

Some lamented the loss of expected services, but customers flocked to fledgling lines like Ryanair and easyJet. Given unprecedented ability to seek and find discounts through the internet, consumers were drawn to regional flights offered for less than \$100 in some cases, gladly enduring smaller jets and meal-less flights for the chance to save money. Gone forever, it seemed, were leg room, complimentary cocktails, well-appointed airport lounges and in-flight entertainment.

Of course, the old model was untenable; air travel ceased to be a luxury undertaking when it ceased being a novelty. Once the regulatory barriers were removed, particularly in the US, the notion of maintaining a fleet safely and efficiently while bringing a realistically priced product to market, virtually necessitated the reduction of bundled services. The advent of low cost carriers, which by no coincidence coincided with the rise of internet bookings, simply gave customers exactly what they wanted: fast, safe conduct at the lowest possible price. This has, for the most part, worked extremely well, as is evidenced by LCC dominance in Europe.

But the low cost model is not without its challenges. The big expenses associated with all airlines are still realized by LCCs; the incredible infrastructural burden of having to furnish multi-million dollar aircraft, high and increasing skilled labor cost, and of course, skyrocketing fuel costs. Combined with a customer base groomed to eschew loyalty and dive for bargain-basement offerings, running even an LCC becomes a dicey proposition. Two key aspects of an airline's operational model must be addressed for any semblance of success to be achieved: effective purchasing and ancillary revenue development. Fortunately, these are within reach.



Group Buying

For a market like Europe, which has enjoyed significant growth in LCC presence in the past fifteen years, carving out a competitive advantage is imperative. Struggling against legacy carriers with international purchasing departments and economies of scale will invariably lead to unfavorable operating margins. Similarly, competing with another LCC that engages in group buying practices or contracts a group buying services firm to create purchasing alliances will likewise lead to insolvency. The solution, then, on the expense side of the ledger, is to devise a strategy that incorporates some sort of collective purchasing. Other industries, notably the lodging industry, have practiced this for years, lowering their supply costs in like markets to facilitate competitive advantage. For airlines, our company, Airsavings, is the industry leader for providing group buying services among low cost and mid-sized carriers.

Ancillary Services Development

From the unbundled package arises revenue opportunity. For a low cost carrier selling only a seat, anything else that can be offered becomes a point of sale. Those vestiges of the golden age of air travel? Still available, but for the right price. Even the internet, often cited as the engine behind low-price seeking, loyalty-less clientele, offers new and exciting ways to create ancillary sales. In fact, most ancillary sales are increasingly made during the online booking process. Developing an ancillary revenue development strategy is threefold;

- First, the slate of offerings must be expanded. A good service portfolio will include the three internet-driven pillars of hotel booking, car rental and trip insurance, along with other non-flight related services like airport lounge privileges and SMS flight change notification. It should also include further unbundled flight services, like baggage check and in-flight meals. The extent of a service portfolio is limited only by imagination and market pressures. The big three are almost imperative, as they are services the general public has come to expect from popular online booking agents like Orbitz and Travelocity. Without these incorporated into an airline booking engine, it is nearly impossible to capture a customer with the more esoteric ancillaries. That said, one-day lounge passes and gourmet meal availability are exciting high-retail items that evoke the luxury feel and have potential in the budget vacation market.
- With an extensive line of services offered, the focus shifts to selling as many as possible. Increasing the volume of ancillary sales is the second stage of an effective strategy. To maximize volume, it is imperative to integrate all of the service options into the booking process. Relying on a point-of-contact sale is predicated by the presence of a sales-motivated staff, something most airlines do not have in their cabins or at their check-in desks. In fact, with labor costs increasing worldwide, hiring and training additional salespeople is a luxury the typical LCC can ill-afford. This is particularly true if the booking process is attractive and efficient enough to generate an ancillary sale on its own, as the success of independent online bookers has proven. Cross-selling of ancillary services is also key; some services go hand-in-hand, like hotels and rental cars, and so passengers engaging in the reservation process for one should be prompted automatically to the other. Loyalty initiatives, including lucrative frequent flier programs, should be linked to ancillary services, either by promotion or by direct sale. This allows for the effective retention of ancillary-purchasing customers to the booking platform. It also serves as an outlet for miles, points or other promotionals that have fallen on disfavor due to lack of redeemability.
- The third major factor in instituting a good ancillary revenue strategy is to secure favorable margins for the proffered ancillary services. Some ancillaries are inherently profitable; like warranties in the electronics industry, trip insurance in virtually overhead-free and an exceedingly popular ancillary purchase. Likewise, hotel booking and car rental can be obtained cheaply with some negotiation with suppliers. Other services and products should be pursued with a group-buying program in order to get the absolute best prices, keeping in mind that their sale is limited to ancillary revenue, by definition an unreliable stream.

