

Incompatibilities of the low-cost and network carrier business models within the same airline grouping

Luca Graf

Institute for Public Services and Tourism (IDT-HSG), University of St. Gallen, Dufourstrasse 40a, 9000 St. Gallen, Switzerland

Abstract

This paper examines the strategy of setting up a low-cost unit adopted by some incumbent airlines to the threat and opportunity of the low cost incursion. Based on the analysis of five case studies in the European airline industry, the chances and risks of establishing a low-cost carrier within the same grouping of a network carrier business model are explored. The paper examines the hypothesis that incompatibilities of the two business models are the causal reason for failure of earlier attempts. By following this idea, a set of propositions is developed that contribute to the debate of how to control these incompatibilities and when it is favorable to follow other strategic response options.

© 2005 Elsevier Ltd. All rights reserved.

Keywords: Airline business models; Internal low-cost carrier; Incompatibilities

1. Introduction

Many attempts to set up a no-frills low-cost carrier as an internal unit or subsidiary of a full-service network carrier have failed, in particular in the US airline industry. One of the most prominent examples was the effort of Continental Airlines in establishing its low-cost spin-off Continental Lite. In 1994, Continental Airlines suffered a monthly loss of nearly \$55 million, of which up to 70% could be attributed to Continental Lite (Bethune and Huler, 1998). Moreover, the idea of running two different and actually conflicting airline business models simultaneously resulted in poor quality, dissatisfied customers, and discouraged employees (Porter, 1996). The move nearly drove the parent company into bankruptcy, which had been prevented only by the US law Chapter 11 protection clause. The endeavor was soon closed, and the activities of Continental Lite were reintegrated into Continental Airlines.

In the mid- and late 1990s, other airlines in North America and in Europe followed the example, but most

attempts to set up an internal low-cost carrier failed again. Despite these experiences, the airline incumbents in Europe and Asia are in recent time's increasingly adopting low-cost strategies in addition to their premium services, while setting up a parallel no-frills business model. Interestingly, some of the major US American network carriers, which already have made their experiences with this strategy before, are re-implementing the same idea. Table 1 gives an overview of closed down, active, and planned low-cost units of incumbent airlines which also operate the business model of a full-service network carrier.

The large number of attempts underlines the spread of this strategy in the airline industry as one of the options for the incumbents to participate in the growth market for budget air travel, and to react to the spread of the low-cost carriers.¹ It seems that the management of

¹The competitive response of operating various business models within the same grouping or holding company simultaneously, based on a low-cost/full-service combination, and delivering the same basic output, has also been applied in other industries, such as in the retailing, car rental, railroad, banking, insurance, news, power supplying, tour operator, consulting and airport business. In some of these industries, this strategy could be implemented successfully.

E-mail address: grafluca@gmx.net.

Table 1
Closed down, active and planned low-cost units of incumbent airlines

Closed down		Active		Planned	
Low-cost unit	Airline grouping	Low-cost unit	Airline grouping	Low-cost unit	Airline grouping
Buzz	KLM	Song	Delta Air Lines	SAS Braathens	SAS
Go	British Airways	Zip, "Tango"	Air Canada	Smart Wings	CSA
Lufthansa express	Lufthansa	Ted	United Airlines	Nice Jet	Air France
Shuttle by united	United Airlines	Germanwings	Lufthansa/Eurowings	Iberia Express	Iberia
Delta express	Delta Air Lines	Snowflake	SAS	Air India Express	Air India
MetroJet	US Airways	Bmibaby	British Midland	Virgin Express	SN Brussels Airl.
Continental lite	Continental Airl.	Transavia (Basiq Air)	KLM	Indian Airlines	Alliance Air
People express	Frontier Airlines	flynordic	Finnair/Nordic Airlin		
"Austrian Bratislava"	Austrian Airlines	Centralwings	LOT		
		"Swiss in Europe"	Swiss Intl. Air Lines		
		"Fare 4U"	Air Malta		
		"red ticket"	Austrian Airlines		
		Hapag-Lloyd-Express	TUI/Hapag-Lloyd		
		"SAS Economy"	SAS		
		Thomson Fly	TUI/Britannia		
		Freedom Air	Air New Zealand		
		"Express Class"	Air New Zealand		
		Australian Airlines	Qantas Airways		
		Jetstar	Qantas Airways		
		Jetstar Asia	Qantas Airways		
		JAL Express	Japan Airlines		
		Nok Air	Thai Airways		
		Tiger Airways	Singapore Airlines		

Note: Standings March 2005; the low-cost units in quotation marks are not separate legal entities nor independent organizations but within-low-cost carrier business models.

these airlines is not completely aware of the negative impacts and the reasons behind these, and hypothesizes that incompatibilities of the business models are the causal reason for failure. Apparently, the existence of the incompatibilities and the resulting negative impacts makes it difficult to successfully implement such a strategy.

To understand the rationale of the incumbent airlines, this paper first highlights the motives for setting up a parallel low-cost carrier: it seems useful to understand the economic logic for a company to condone the operation of several business models with the same basic output inside the organization boundary that appears to run counter to the traditional logic of efficiency.

Secondly, the goal is to consider the incompatibilities in operating the business model of the no-frills low-cost carrier and full-service network carrier simultaneously. When talking about incompatibilities of the business models, reference is made to any inconsistencies or the missing fit of strategic positions from which conflicts or negative impacts arise, and where it becomes necessary to make trade-offs.

Finally, a set of propositions is developed following contingency theory, in which the incompatibilities can be controlled in such a way that the overall benefits are higher than the costs. It is believed that incompatible positions and the resulting negative impacts arise

automatically, when a company operates two business models simultaneously, which are turning out the same basic output. It is, however, assumed that the number and extent of the negative impacts can be reduced, depending presumably on organizational and market-driven conditions, thus on controllable and non-controllable contingencies.

2. Conceptual background

On the one side, the conceptual background of this study is constituted by evolutionary theory and the theory of economies of scope and scale, discussing the rationale for companies to set up and operate various business models with the same basic output within the same grouping. On the other side, the theory of generic strategies and the concept of business modeling offer insights into the incompatibilities and why such endeavors are doomed to fail, if certain rules are not observed.

2.1. Evolutionary theory

Evolutionary theory considers evolutionary processes within organizations. The ongoing process of adjustment and change inside organizations that is driven both

متن کامل مقاله

دریافت فوری ←

ISIArticles

مرجع مقالات تخصصی ایران

- ✓ امکان دانلود نسخه تمام متن مقالات انگلیسی
- ✓ امکان دانلود نسخه ترجمه شده مقالات
- ✓ پذیرش سفارش ترجمه تخصصی
- ✓ امکان جستجو در آرشیو جامعی از صدها موضوع و هزاران مقاله
- ✓ امکان دانلود رایگان ۲ صفحه اول هر مقاله
- ✓ امکان پرداخت اینترنتی با کلیه کارت های عضو شتاب
- ✓ دانلود فوری مقاله پس از پرداخت آنلاین
- ✓ پشتیبانی کامل خرید با بهره مندی از سیستم هوشمند رهگیری سفارشات