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Management Focus

Low Cost Airlines: Business Model and Employment Relations

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The passenger air travel industry is experiencing increasing competition between low cost/no frills carriers (LCC) and the more traditional full service carriers. This paper explores the comparative business models with a view to identifying areas where these might be expected to generate different HR and employment relations practices, and checking the findings against available evidence. While some of the expectations are confirmed, unionisation is higher than anticipated in the LCC sector and a relatively high percentage of staff were on regular rather than contingent contracts. Differences in approach are observed among LCC airlines, and the evidence indicates some convergence between the two sectors as competition heightens.
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Introduction

The passenger air travel industry is characterised by the emergence of a low-cost/no frills sector alongside and partly in competition with the incumbent full service carriers. [1] These two sectors offer strong contrasts in their business and competitive strategy, effectively providing competing models of operation. Although it is now widely accepted that there is no necessary and unique connection between an organisation's business model and its HR and employment relations strategy, there is still some expectation that the latter will be influenced by, and have some interaction with, the business strategy. The aim of this short paper is to explore the comparative business models (Section 2), to identify areas where these might be expected to generate different HR and employment relations practices (Section 3), and check these expectations against the available evidence. This may in turn raise questions regarding tendencies to divergence or convergence between the two sectors, and about their respective HR responses to major market shocks.

Competing Business Models

We will refer to the two models as the full service carrier (FSC) and low cost carrier (LCC) models. The FSC model is essentially one based on a differentiation strategy, in contrast to the LCC approach based on cost leadership or cost minimisation (Alamdari and Fagan (2005)): within each model companies will seek competitive advantage through some variation in their operational vision, business routines, architecture and practice. [2] Thus we should expect to see some heterogeneity within sectors as well as between sectors. However, it is possible to present a 'typical' profile of an FSC and LCC model organisation as follows (Table 1):

It is clear from this comparison that the FSC bears much heavier overheads necessitated by the hub and spoke *modus operandi*, which is based on the premise of the need to build up capacity utilisation by links to feeder routes at the hubs; and generally higher operating costs on account of the extra services provided, for which a premium price is charged. Airline alliances in recent years can be seen as a device to share the overheads and use aircraft capacity more effectively. Even so, the level of capacity utilisation on many routes will be moderate, though off peak and other promotional fares have been introduced to increase capacity. (Scheduled

Table 1 Operational Characteristics of FSC and LCC Airline

Characteristic feature	FSC	LCC
Generic strategy	Differentiation	Cost minimisation/cost leadership, entrepreneurial in character
Scale	Typically large	Generally smaller, but some major players (e.g. Ryanair, EasyJet)
Operational model	Hub and spoke/Multiple hub and spoke, linking with feeder routes Mix of short/medium/ and long-haul routes Various aircraft type and engines Moderate capacity utilisation (c. 60%)	Point to point, no interlining, short sector length (400–600 nautical miles) Mainly short haul Uniform aircraft type High capacity utilisation, (c. 70–80%) rapid turnround between sectors, low margins
Market	Normally in competition with other FSCs, leading to differentiation by class (quality) of service, with high service image, including: Frequent scheduling & flight flexibility Extensive in-flight services Comprehensive ground services Use of principal airports	Cheap travel sector of the market, segmentation by time of booking and choice of flight Quality of service basic, e.g.: Little flexibility of flight changes (use or lose!) No catering, or meals charged for Ground services typically outsourced (but can be problematic, e.g. easyJet) Typically use secondary airports
Inventory Management	Pre arranged tickets and seats: reservation system complex, due to feeder routes: use of travel agents	Inventory management simplified: direct or online bookings, ticketless, no use of travel agents

Source: This table draws on: ITF (2002): and Alderighi *et al.* (2004).

flights, once committed to, are a sunk cost which can with benefit be spread by marginal cost pricing of spare capacity.) Travellers such as business passengers with a need for frequent scheduling, inter-flight flexibility and ground service linkages are the backbone of the FSC market, for which a premium fare is paid, with differentiation being offered through personal space and comfort on-board, inflight entertainment and free food and alcoholic drinks, frequent flier programmes, free airport lounges and use of major city airports (typically with higher landing charges). All these features raise seat costs.

By contrast, the LCC has cut costs significantly by reducing overheads, providing a no frills service and often using secondary airports with cheaper landing charges. Inventory management is simplified by the absence of feeder routes, direct or online booking and ticketless operation. By significantly reducing costs and fares, the LCCs have opened up a much wider range of point to point journeys, many not served by the FSCs,[3] and in so doing have attracted at least some price-conscious passengers from the high-fare FSCs. On routes between UK and Ireland, Aer Lingus business passengers mainly work for companies employing over 100, while Ryanair business passengers are usually self employed or work for smaller companies (Binggeli and Pompeo (2005)).

Faced with this competition, FSCs have attempted to fight back by adopting some of the LCCs' characteristics – with increasing online sales, more rapid turnround times and reduced use of travel agents or lower commission rates. Some have gone as far as to set up their own 'budget airline' within the main organisation (examples include BA and GO (later sold off): British Midland and bmibaby: KLM and Transavia). But in general they still have a long way to go and these airlines will pursue differentiated strategies (c.f. British Airways' current (2005) plans to expand the share of capacity allocated to high fare/high yield business class passengers by upgrading seating quality).[4]

Comparative HR and Employment Relations Strategies

Discussion of business strategies and their relation to HR and employment relations strategies strictly requires a detailed analysis of the meaning of business strategy, HR strategy and practice, and the interplay between them.[5] This is not feasible in the context of this short paper. Instead, we follow the general thrust adopted by Boxall (1999),[6] who found the contingency hypothesis linking business strategy and HR policy overly simplistic in terms of both strategy and HR/employment relations. Business strategy is not a given, but is seen as critically interactive with HRM. Purcell and Alhstrand (1994) note that large scale multi-divisional enterprises are able to have different strategies for different segments or levels of the business, and likewise may deploy a segmented labour force with differentiated contracts of employment to reflect the different market circumstances. This permits a pluralist view of the firm, rather than the often implied assumption that strategy will be accepted by a homogeneous workforce adopting a unitary frame of reference. It allows for

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