

# Future Scenarios for the European Airline Industry

The European airline industry is highly dynamic, competitive and has gone through significant changes in the last decade.

As Ryanair's CEO Michael O'Leary put it: 'Air transport is just a glorified bus operation'. Indeed, flying as a comfortable and fast way of travel has lost much of its glamour from the past. Whereas air travel was a high-price privilege for the upper classes during most of the last century, globalization has led to an increased need for affordable and fast world-wide passenger transport.

## Future scenarios for the European airline industry



On the one hand, this creates enormous growth potential for airlines to satisfy. On the other hand, it also creates challenges. New technologies and the vanishing of economic barriers and regulations led to decreasing prices and air transportation turning into a commodity.

The emergence of European low-cost airlines like Ryanair, easyJet and Air Berlin further spurred this development. The traditional, state-owned network carriers are facing these new competitors, which are smaller and highly flexible and can tap into almost every market within Europe.

Further challenges for the airline industry can be seen in the environmental awareness arising in the

population and its effect on consumption behavior. Besides that, the industry's strong dependency on the overall economic development on one side and oil as the basis for kerosene cost on the other, present major threats.

## **Scenarios of the Industry**

To overcome these challenges and help managers in the industry to plan for the future, we created the current study using our new and innovative approach to scenario-based strategic planning that was jointly developed by HHL and Roland Berger Strategy Consultants.

Our scenarios are based on extensive research, expert workshops and a survey that combines insights from companies which together make up for more than 40 percent of the total revenue of the airline industry in Europe. This insures a holistic picture of the relevant trends and influence factors and safeguards the quality of the scenarios.

The four scenarios, which we created, center around two key uncertainties, which we identified in our survey with industry experts and a subsequent scenario workshop. These two critical uncertainties are:

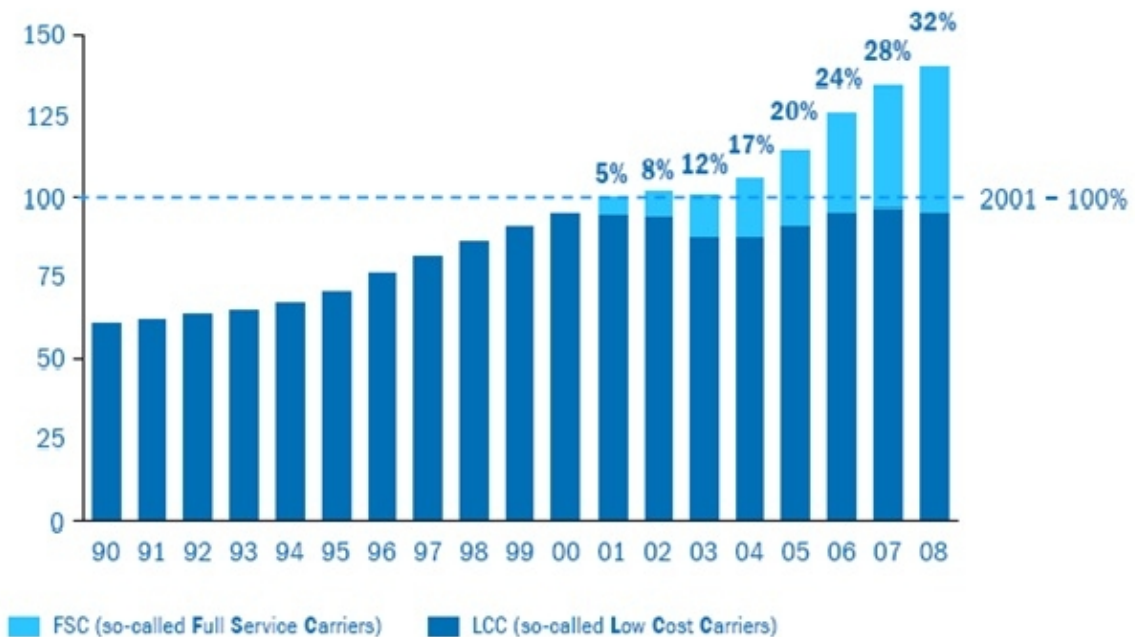
### **Regulation of the industry in Europe Price sensitivity of the customer base**

Based on these key uncertainties as well as additional trends and influence factors four plausible scenarios emerge on how the European airline industry might evolve between now and the year 2015. These four scenarios are the following:

**Network fortress** describes a future, in which the European network carriers have re-gained a strong competitive position in both the long-haul and the intra-European market. The recession of 2008 and 2009 was followed by a quick economic recovery, which increased corporate travel budgets again in 2012.

In turn, the demand for low-cost travel stagnated in favor of high quality and convenient travel, which led to growth in the more profitable business and first class segments. The growing long-haul market connecting Europe with the booming ASEAN region and China is dominated by European airlines, which can operate from a largely protected European market to which competition from Asia and the Middle East had only limited access to due to restrictive traffic rights legislation.

**Development of demand for Air Travel in Europe**  
[indexed, base year 2001]



Source: European Aviation Analysis; Roland Berger (2010)<sup>13)</sup>

**Europe under siege** describes a world in which Asian and Middle Eastern competitors dominate the future of European network carriers. Despite growing business travel based on solid economic growth in Europe, the industry faces severe competition, also in its home market.

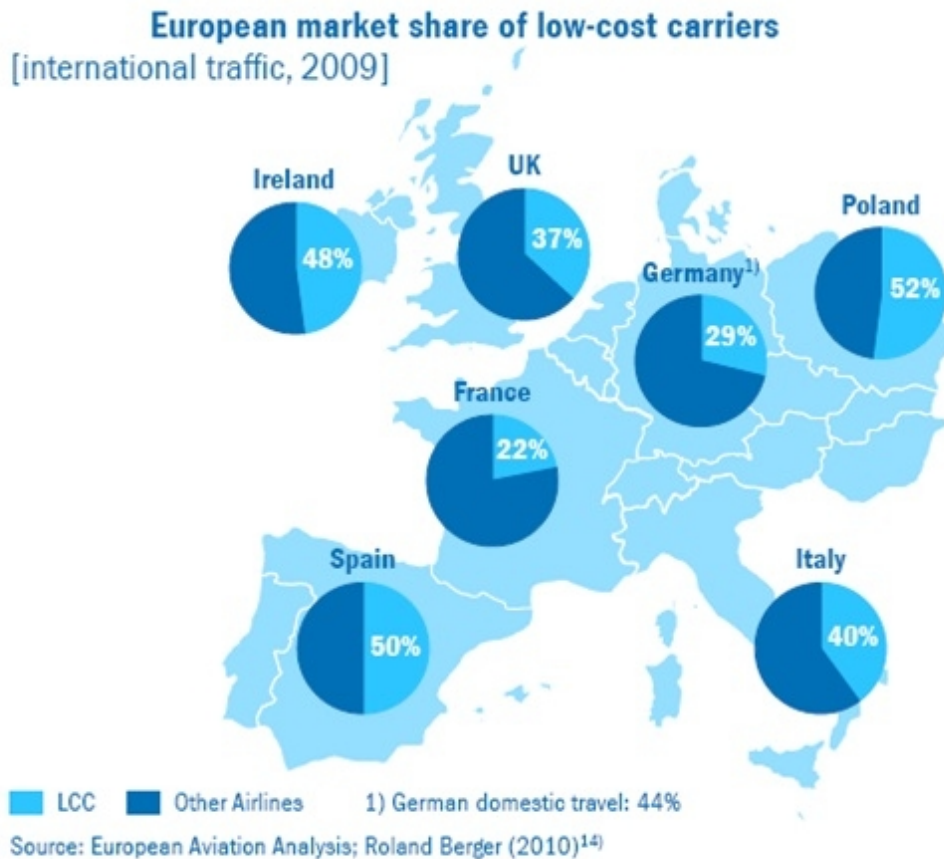
However, low-cost carrier have not been able to continue their growth seen in the first decade of the new millennium as customers became increasingly aware of the total cost of flying low-cost.

"New World", a new alliance by Middle Eastern and Asian airlines was formed in 2012 focusing on capturing the growing demand for high quality air travel around the world. The alliance also partners with a major European airline to gain easier access to the attractive European market. With their new fleet and superior service offering, the alliance has quickly gained market share and is expected to continue its growth.

**Decline of Champions** describes a world that is characterized by declining European network carriers struggling to survive the intense local and global competition. While Europe and the United States of America are again in the middle of an economic crisis, Asia is flourishing. The recession in the western world has led to a shift in the mindsets of business and private customers towards a strong price orientation.

European network carriers therefore are under heavy pressure from both European low-cost rivals and strong Asian and Middle Eastern competitors on long-haul routes. These companies have grown significantly in recent years due to favorable cost position, innovative product and high client recognition.

**New Horizons** refers to a world in which Europe is still struggling with the aftermaths of the financial crisis, which originated in 2008 and 2009. Thus, business travel has been cut to a minimum as companies face severe cost pressure. In addition, an increasing market share of this shrinking segment is captured by low-cost airlines.



While Europe is still faced with the aftermaths of an economic crisis, the ASEAN region together with China has developed into the most vibrant business area worldwide, which has increased the demand for long-haul flights to and from Asia tremendously over the last 5 years.

These traffic flows are dominated by European carriers, which benefit from political protection of the sector in Europe and a growing customer sentiment to buy 'European'.

### Strategy of Airlines

Each of these scenarios describes different possible developments of the industry in the next five years. They are not intended to predict the future. Rather, they aim at inspiring ideas that expand the field of vision of industry leaders and at helping them to prepare for the opportunities and challenges ahead.

Based on the scenario results, we recommend a core strategy for European network carriers: First, continue restructuring and efficiency improvements to curb cost disadvantages. Second, increase service and quality levels by fostering innovations both in the air and on ground in order to remain

competitive against Asian and low-cost carriers. This way, a hybrid strategy can be followed that allows investments in core customer preferences and cost saving as well as efficiency increases in back office and support processes.

In our scenarios, we have shown the enormous impact that changes in the European regulatory environment can have for European network carriers. Giving foreign airlines unreasonable access to the European market sidelines European network carriers and strongly hampers their growth prospects. Lobbying national and European bodies to constantly re-assess the advantages and disadvantages of liberalization remains top priority for European airline managements.

This core strategy has to be complemented by scenario-specific strategic options such as the increased presence on the growing Asian market or the introduction of new innovative pricing schemes.

Detailed strategy recommendations, however, can always only be derived in the light of the specific situation of the respective company. Our scenarios can serve as a foundation to develop company specific strategies and action plans that allow European players to remain competitive in this highly dynamic environment. Therefore, it is essential to review and discuss assumptions, implications and required strategic moves with the responsible management.

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