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Long-haul low-cost

– Market Opportunities and Threats –

The Hague, Crowne Plaza Hotel
September 18, 2007

Content

1. LCC market success factors in short haul markets
   - Origin/destination focus
   - Product focus
   - Yield Management / Pricing
   - Ancillary revenues
2. Opportunities from applying traditional market success factors of LCCs to long-haul markets
   - Origin/destination focus (including feeder issues)
   - Product focus
   - Yield Management / Pricing
   - Distribution
   - Ancillary revenues

Lacking capacities and competition have been key enablers for LCCs to enter into short haul markets.

Focus of market penetration

prior to 1997 → 1997 to 2005 → since 2005

Deregulation → Saturation →

Domestic services competing with low capacity/high yield offerings

Examples:
- RYANAIR within UK/Irelend
- Germanwings (1st edition) within Germany

+ Home base penetration

Examples:
- RYANAIR and easyJet within Continental Europe
- SkyEurope, Wizz … within CEE countries

European services competing with low capacity/high yield offerings

Examples:
- Mediterranean mainland destinations Italy / France / Spain
- Alpine destinations
- Scandinavian destinations

+ European high volume low yield markets (traditional charter markets)

Examples:
- Aggressive penetration of Baleares and Canaries destinations
- Greek Islands destinations
- Turkish leisure destinations
- North African leisure destinations

Simple („no frills“) product features not only reduce cost but also ease processes for customers

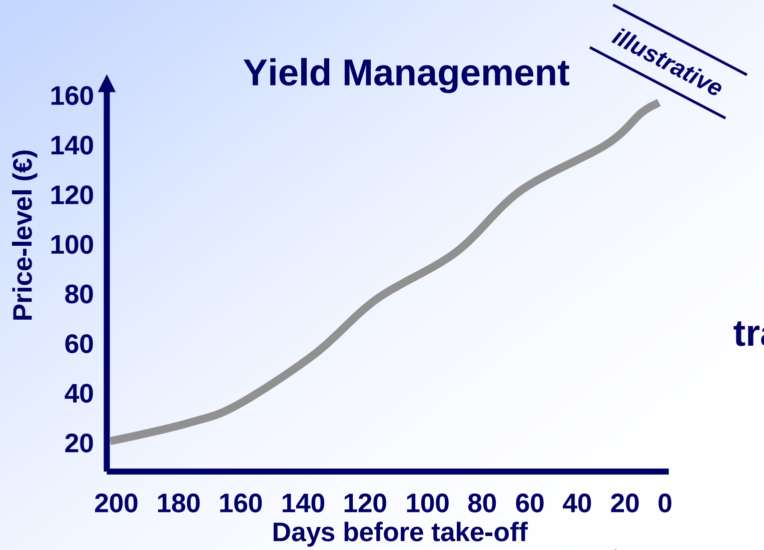
Product Focus

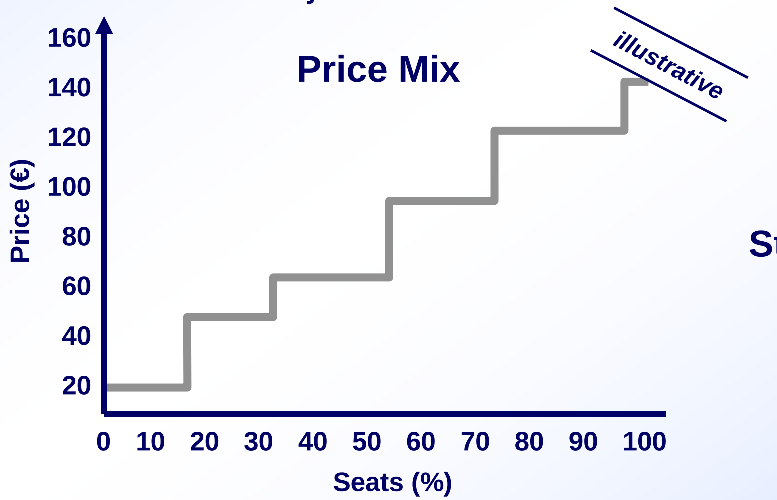
Sales and Distribution	Check-in and Boarding	On Board
• One class • One price at a time • »click and buy« • Open 7/24	• No physical ticket • Simple identification processes • Simple seating procedures • Non-stop	• Free seating • Service on demand

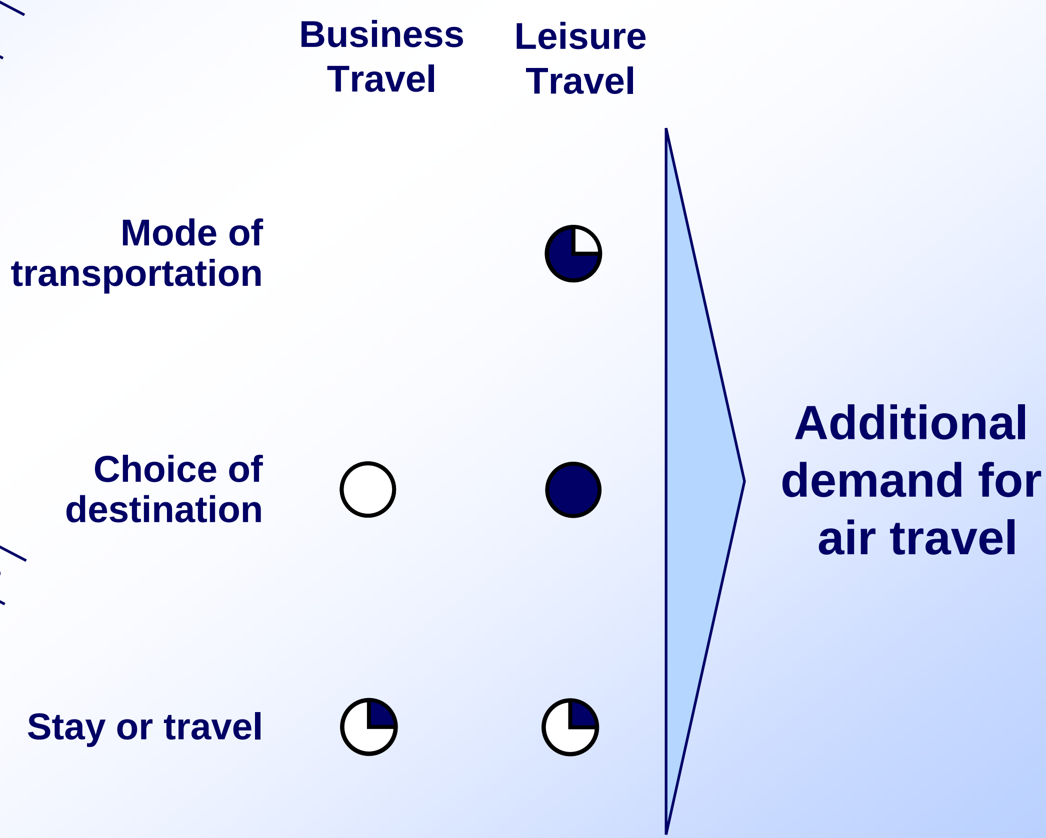
Easy to buy – easy to fly

LCCs pricing strategies create additional demand for air travel.

Yield Management and Pricing







LCCs consequently search for ancillary contributions to allow for low ticket prices.

Ancillary revenue

Examples

- Subsidies for local infrastructures
- Success fees from incoming tourism boards and airport non aviation concessionaires
- Sales commissions from car rentals, hotels, … for cross-selling via LCC web page
- Separate charges for in flight services and other additional services (i.e. seat reservation, baggage, …)

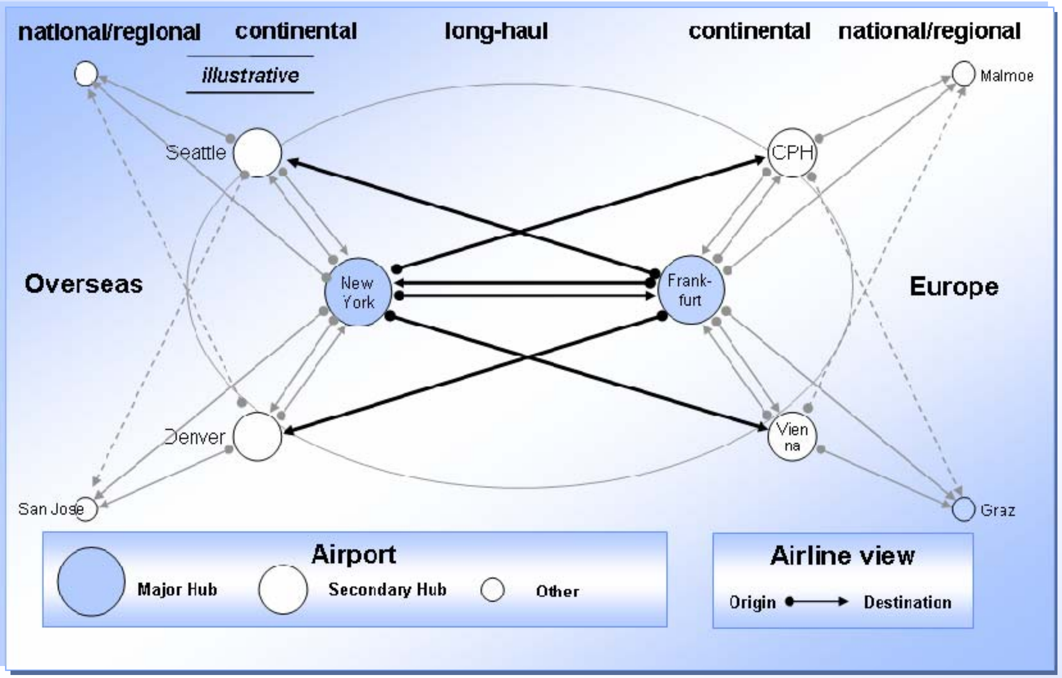
Ancillary revenue driven by transaction rather then by flight distance

Would all this bring any innovation to the long haul markets?

Not really!

Beyond hub-to-hub and hub-to-spoke routes only few O&Ds offer potential for non-stops.

Network economics of long haul markets

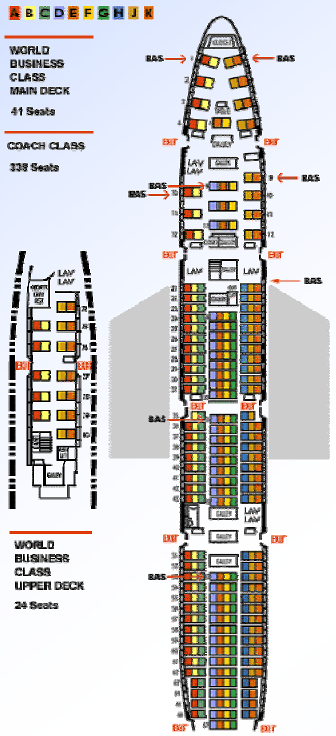


1. Long haul operations depends on feeder at the one or the other or even at both ends.
2. Network carriers don't charge but even »pay« passengers for accepting being feedered.

Network carriers' long haul aircraft offer Y-class seating capacities in excess.

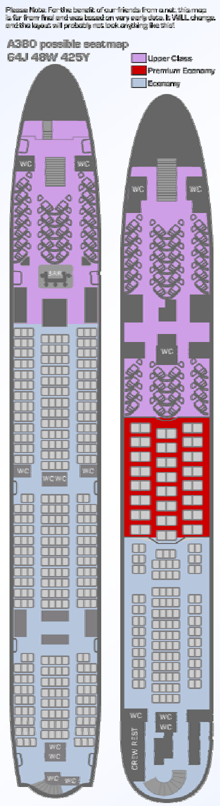
Standard seat configuration

B 747-400



65 F/B
338 Y

A 380



64 F/B
48 »Premium«-Y
425 Y

Singapore Airlines

	B 747 -400	A 380 -300	+/-	+/- %
Suites	12	12	+-0	-
Business	50	60	+10	+20 %
Economy	399	313	+86	+27 %

- **Network carriers operate huge Y-class seating capacities in order to materialize large aircrafts' unit cost advantage.**
- **A 380 will add even more surplus capacities.**

To fill capacities Economy-class tickets are dumped into markets at rates hardly covering DOC.

Examples

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⋮

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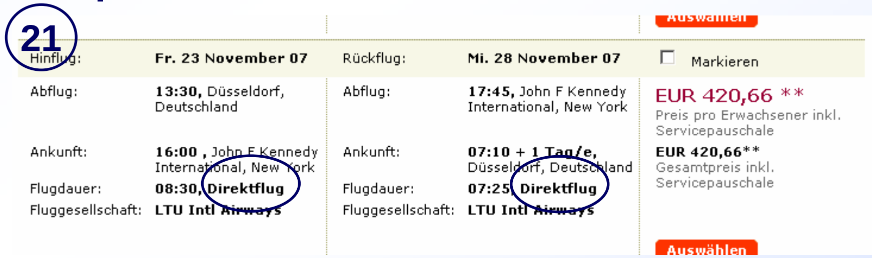

Source: http://www.OPODO.de, 15.09.2007

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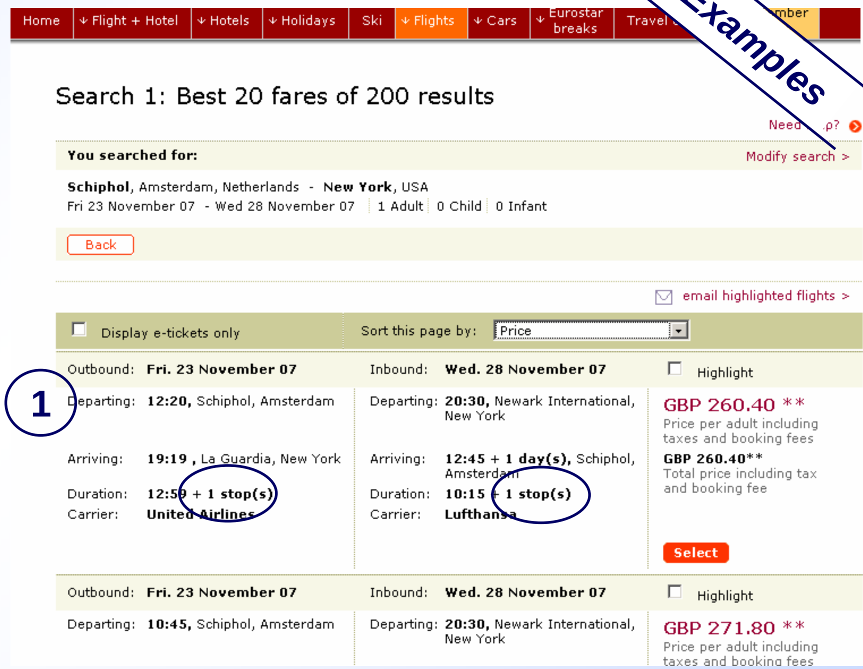

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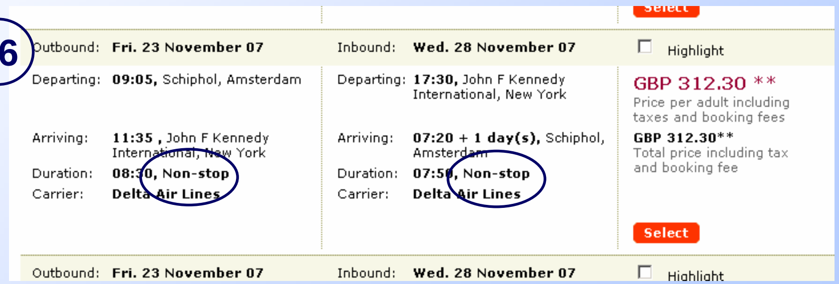
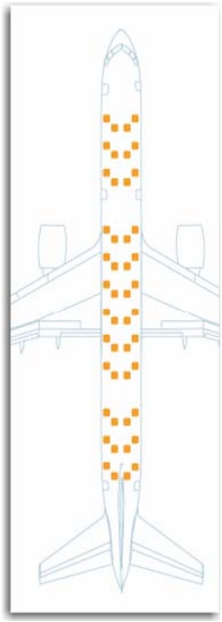


Source: http://www.OPODO.co.uk, 15.09.2007

Applying the »Product Specialist« approach to premium class services might offer a niche.

Product Specialist



Eos Airlines
JFK - STN
48 seats per B757

Focus:
High-Yield
Corporate VIPs

Key Differentiators:
Large horizontal bed with personal service

MAXjet Airways
JFK / IAD / LAS - STN
100 seats per B767

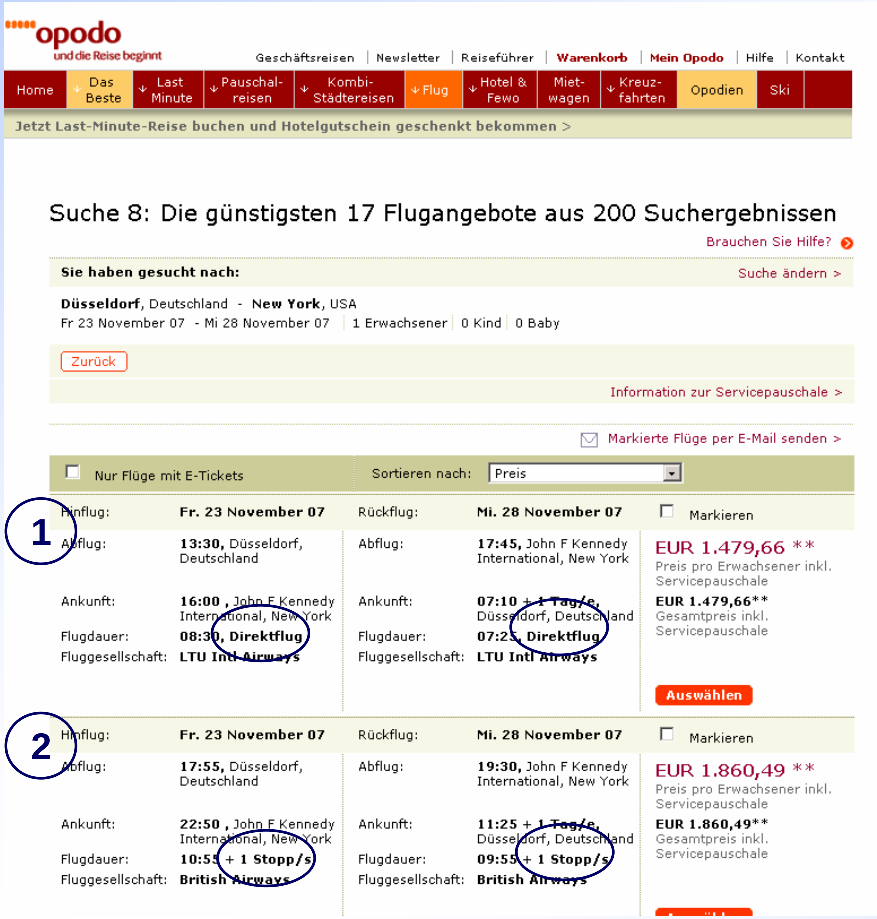
Focus:
Large and small business
Affluent leisure

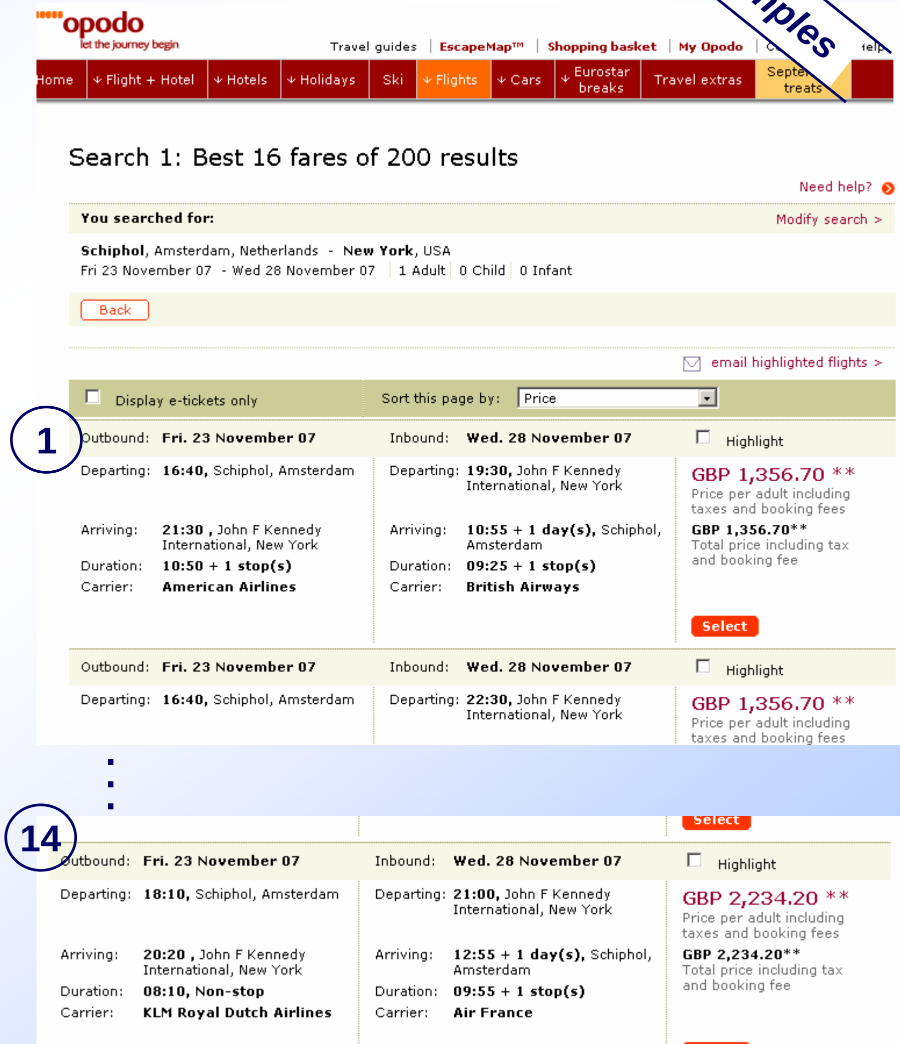
Key Differentiators:
Low, flexible fares for traditional Business Class

Source: John Wensveen: OPPORTUNITIES FOR THE LONG-HAUL LOW-COST MODEL

However, even Business-class yields are not up in seventh heaven any more.

Examples





Source: http://www.OPODO.de, 15.09.2007

Source: http://www.OPODO.co.uk, 15.09.2007

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Where »Product Specialists« enter into markets, incumbents have lowered fares to defend their stake.

Business class fares London – New York 23.11.2007 – 28.11.2007 as of 15.09.2007

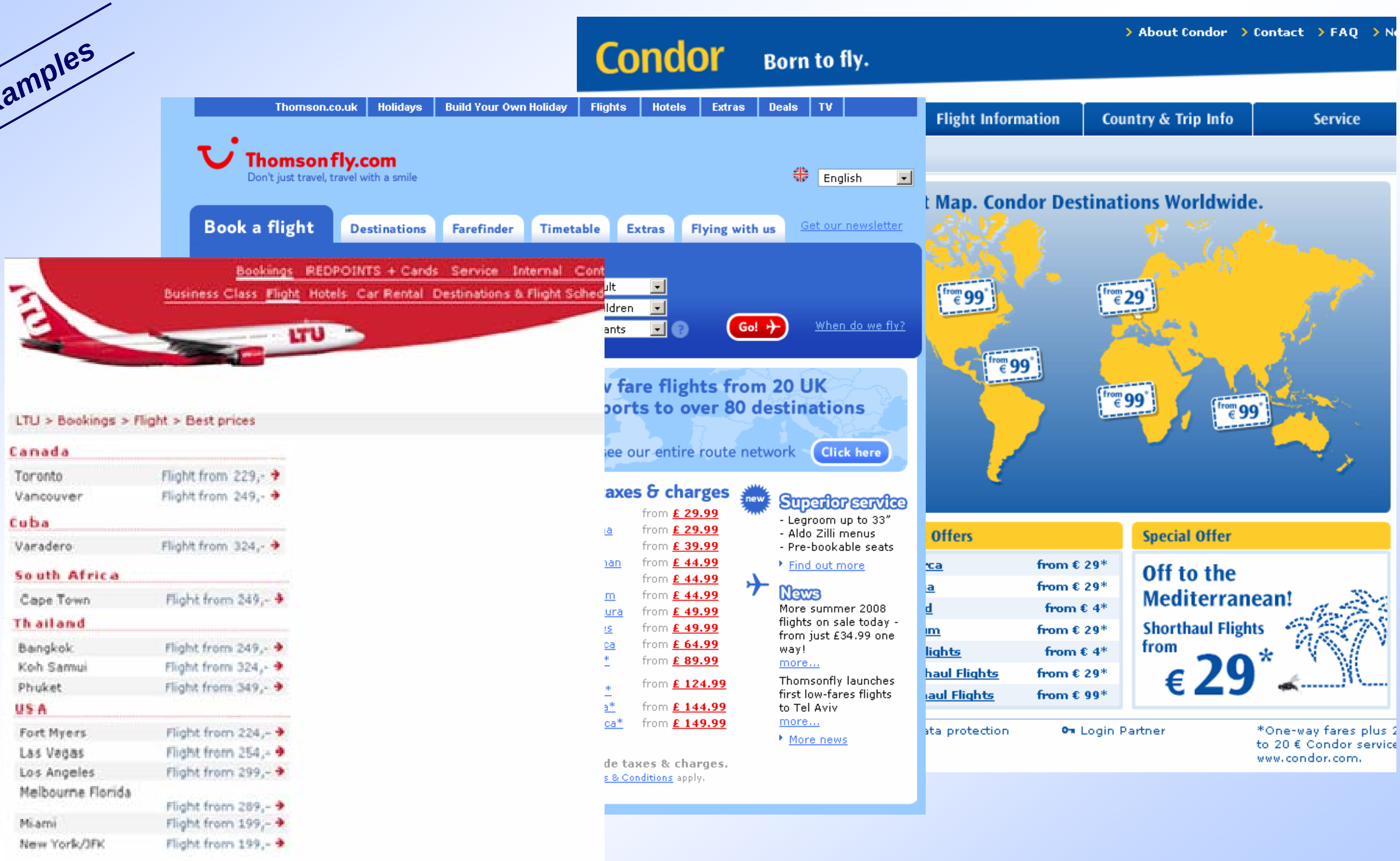
Rank	Airline	London	New York	Return fare (UK£)	Stops
1.	Maxjet	STN	JFK	835,10	nonstop
2.-5.	Silverjet	LTN	EWR	997,50	nonstop
5.	Air India	LHR	JFK	1.085,60	nonstop
6.-36.	Air France	LHR	JFK / EWR	1.358,10	1 stop
37.-41.	American Airlines	STN	JFK	1.466,68	nonstop
42.-76.	American Airlines	LHR	JFK	1.472,40	nonstop
77.-124.	KLM / Northwest	LHR / LCY	JFK / EWR	1.564,20 – 1.567,80	1 stop
125.-148.	KLM / Air France	LHR	JFK	1.604,6o – 1.608,20	1 stop
149. - 151.	EOS	STN	JFK	1.666,68	nonstop
152. - 157	Delta +	LGW	JFK	1.706,10 – 1.753,70	nonstop
158. - 159.	Continental	LGW	JFK	1.776,10	nonstop
160.-189.	Northwest/KLM	LCY	JFK/EWR	1.792,80 – 1.808,20	1 stop
190.-198.	Lufthansa	LHR	JFK/EWR	1.813,50 – 1.817,70	1stop
cheapest BA[1)]	British Airways	LHR	JFK	2.108,00	nonstop

Source: http://www.OPODO.co.uk, 15.09.2007

1) Source: http://www.britishairways.com, 15.09.2007

Last but not least, incumbent leisure carriers apply LCC pricing strategies for long haul services.

Examples



Long-haul low-cost – what makes the difference?

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In conclusion, economics of long haul markets, timing and reactions of incumbents leave little opportunity for long haul LCCs.

Summary of opportunities

Key enablers of LCCs	Reasoning	Drivers	Rating
Origin/destination focus	▪ Hub&spoke ▪ Oversized economy compartments due to addiction to »optimize« unit cost	Market economics	
Product focus	▪ Leisure travel O&Ds served by leisure carriers at LCC cost standards ▪ Higher share of hardly manageable DOC (i.e. fuel, air traffic control) ▪ Web based distribution has been adopted by incumbent players	Market economics & timing	
Yield management / pricing	▪ Strategies applied by incumbent players	Timing	
Ancillary revenues	▪ Lower impact because of higher share of DOC	Market economics	