How did the deregulation of air transportation in Europe foster entrepreneurial behavior and innovation in the European airline industry over the last twenty years?

Case studies: SAS Airline & Ryanair

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Supervisor: Håkan Bohman
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Authors: Gilles Helterlin and Nuno Ramalho
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Gilles HELTERLIN
Nuno BERBERAN
Abstract

The dynamics of business contexts influence the way firms act in their industry. These changes can have effects in several areas within a company. Entrepreneurship and Innovation are two areas that are affected when a change in firm’s environment occurs, like Schumpeter, Shane and Drucker point. Changes in the deregulatory framework are a specific type of change that can occur. According to Entrepreneurship theories, the removal of regulatory barriers creates opportunities to different reallocation of resources that can lead to changes in market equilibrium. This study addresses this relation between deregulation and entrepreneurship-innovation in the European airline industry. With the removal of regulatory barriers, companies like SAS and Ryanair, saw opportunities to do something new and at the same time had to adapt to these “doing something new” behavior of other companies. Entrepreneurship and innovation were the answer to theses changes and the weapon to fight answers to others with this change. Considering this, our statement problem is the following:

How did the deregulation of air transportation in Europe foster entrepreneurial behavior and innovation in the European airline industry over the last twenty years? The case of SAS and Ryanair.

Our goal is to describe the process of deregulation and how firms reacted to it and to give explanations behind the relation deregulation-entrepreneurship, identifying the direct and indirect influence of deregulation in the studied companies. Furthermore, based on this investigation, we will trace possible ways on how future deregulation in Europe can foster further entrepreneurial behavior and innovation.

This thesis was conducted with a positivism scientific ideal and a deductive approach. We used a qualitative method to collect empirical data that could match with the theories we had chosen beforehand. We conducted three interviews with people inside the industry – from airlines (SAS Braathens and SAS) and from airports (LFV). The first two were used as main sources to SAS case study and the third to have a perspective of airline industry. Since we could not get any interview with Ryanair, Ryanair story book was used as main source for this case study.

Our theoretical framework consists of four different broad areas that are interrelated to each other. These areas and the respective theories integrated in them are: institutions and regulation, changes in context and strategic position.

Our study shows that EU deregulation altered the five competitive forces in European airline industry and in turn this fostered entrepreneurship and innovation, as a reaction of firms to adapt to the change in their context. The reaction of Ryanair and SAS through entrepreneurial and innovative behaviour was different due to the differences in their business model. We argue that the removal of barriers to new entrants and the increased rivalry between firms were the main forces that fostered entrepreneurship and innovation. We predict that if further EU deregulation comes (as it is the trend) this will generate more opportunities to entrepreneurship and innovation like it generated in the past.
# TABLE OF CONTENTS

1 INTRODUCTION .......................................................................................................................... 1

1.1 BACKGROUND OF THE STUDY ............................................................................................... 1
1.2 RESEARCH PROBLEM .............................................................................................................. 3
1.3 RESEARCH OBJECTIVES ......................................................................................................... 4
1.4 DEMARCATIONS AND LIMITATIONS OF THE STUDY ......................................................... 5
1.5 DEFINITIONS AND ABBREVIATIONS .................................................................................... 6
1.6 DISPOSITION OF THE THESIS ............................................................................................. 8

2 RESEARCH CONSIDERATIONS .................................................................................................. 10

2.1 CHOICE OF TOPIC .................................................................................................................. 10
2.2 PRECONCEPTIONS .................................................................................................................. 10
2.3 SCIENTIFIC IDEAL (EPSTEMOLOGICAL CONSIDERATIONS) ................................................ 12
2.4 SCIENTIFIC APPROACH ......................................................................................................... 12
2.5 RESEARCH METHOD .............................................................................................................. 13
2.6 RESEARCH DESIGN ............................................................................................................... 14
2.7 PERSPECTIVE OF THE STUDY ............................................................................................ 17

3 PRACTICAL METHOD ................................................................................................................. 18

3.1 SELECTION OF SOURCES ...................................................................................................... 18
3.1.1 Selection of Literature and Scientific Articles .................................................................. 18
3.1.2 Selection of Primary Sources ........................................................................................... 19
3.1.3 Selection of Other Sources ............................................................................................... 19
3.2 CRITICISM OF SOURCES ....................................................................................................... 20
3.2.1 Criticism of Primary Sources .......................................................................................... 20
3.2.2 Criticism of Other Sources ............................................................................................. 20
3.3 THE INTERVIEWS .................................................................................................................. 21
3.3.1 Creating the Interview Guides ......................................................................................... 21
3.3.2 Performing the Interviews ............................................................................................... 22
3.3.3 Processing and Analyzing the Interviews ...................................................................... 24

4 THE AIRLINE INDUSTRY AND THEORETICAL FRAMEWORK ............................................. 25

4.1 PREVIOUS RESEARCH .......................................................................................................... 26
4.2 INSTITUTIONS AND REGULATION ....................................................................................... 29
4.2.1 Institutions ....................................................................................................................... 29
4.2.2 Economic Theory of Regulation .................................................................................... 31
4.2.3 Public Interest Theory ..................................................................................................... 33
4.3 CONTEXT AND INDUSTRY ANALYSIS ............................................................................. 35
4.3.1 The Pestel Framework ................................................................................................... 35
4.3.2 Changes in the Environment and Entrepreneurial Opportunities .................................. 36
4.3.3 Structural analysis of an Industry .................................................................................. 37
4.4 ENTREPRENEURSHIP AND INNOVATION ..................................................................... 38
4.4.1 Entrepreneurship ............................................................................................................ 39
4.4.2 – Innovation .................................................................................................................... 42
4.4.4 Institutional Entrepreneurship ....................................................................................... 45
4.4.4 Corporate Entrepreneurship .......................................................................................... 46

5 STRATEGIC POSITION ............................................................................................................. 47

4.5.1 - The SWOT analysis ....................................................................................................... 47
4.5.2. Competitive Strategies .................................................................................................. 48

5 EMPERICAL DATA PRESENTATION ......................................................................................... 52

5.1. THE EUROPEAN AIRLINE INDUSTRY ............................................................................ 52
5.1.1 Evolution of air transport regulation in Europe ............................................................ 52
5.1.2 Consequences of deregulation for the airline industry................................................... 52
5.1.3 Types of airlines in Europe ............................................................................................... 57
5.1.4 The largest European Airlines ......................................................................................... 59
5.1.5 Strategic trends after deregulation .................................................................................... 63
5.1.6 The three main Alliances ................................................................................................ 64
5.1.7 Future and Challenges of European Airline Industry .................................................... 68
6 EMPIRICAL DATA ANALYSIS
6.1 SAS ANALYSIS .................................................. 88
   6.1.1 Context and Industry Analysis .................................................. 88
   6.1.2 Entrepreneurship and Innovation ............................................... 92
   6.1.3 Competitive Strategies ....................................................... 97
   6.1.4 Future Deregulation and Opportunities for Entrepreneurship and Innovation ............................................... 98
6.2 RYANAIR ANALYSIS .................................................. 99
   6.2.1 Context and Industry Analysis .................................................. 99
   6.2.2 Entrepreneurship and Innovation ............................................... 100
   6.2.3 Strategic Position ........................................................... 105
   6.2.4 Future Deregulation and Opportunities for Entrepreneurship and Innovation ............................................... 108
6.3 COMPARATIVE ANALYSIS .................................................. 109
   6.3.1 Context and Industry Analysis .................................................. 109
   6.3.2 Entrepreneurship and Innovation ............................................... 113
   6.3.3 Strategic Position ........................................................... 117
   6.3.4 Future Deregulation and Opportunities for Entrepreneurship and Innovation ............................................... 121
7 CONCLUSIONS .................................................. 123
   7.1 CONCLUSIONS .................................................. 123
   7.2 MANAGERIAL IMPLICATIONS .................................................. 125
8 FURTHER RESEARCH .................................................. 126
9 CRITERIA FOR EVALUATION .................................................. 127
   9.1 TRUSTWORTHINESS .................................................. 127
      9.1.1 Credibility ............................................................... 127
      9.1.2 Transferability ............................................................... 127
      9.1.3 Dependability and confirmability .................................................. 128
   9.2 AUTHENTICITY .................................................. 129
      9.2.1 Fairness ............................................................... 129
      9.2.2 Ontological authenticity, educative authenticity, catalytic authenticity and tactical authenticity .................................................. 130
10 BIBLIOGRAPHY .................................................. 131
   10.1 BOOKS AND ARTICLES .................................................. 131
   10.2 WEBSITES .................................................. 135
   10.3 REPORTS .................................................. 136
   10.4 INTERVIEWS .................................................. 136
11 APPENDIXES .................................................. 137
LIST OF FIGURES

FIGURE 1 - SELF CHECK -IN ........................................................................................................ 8
FIGURE 2 - REPLICATION APPROACH TO MULTIPLE CASE STUDIES ................................ 16
FIGURE 3 - FORMULATING QUESTIONS FOR AN INTERVIEW ........................................... 22
FIGURE 4 - LAYERS OF THE BUSINESS ENVIRONMENT ...................................................... 25
FIGURE 5 - THEORETICAL FRAMEWORK, AUTHORS’ CREATION ........................................ 26
FIGURE 6 - THE PESTEL FRAMEWORK ................................................................................. 36
FIGURE 7 - THE FIVE COMPETITIVE FORCES THAT DETERMINE INDUSTRY PROFITABILITY 38
FIGURE 8 - INNOVATION CYCLES AS A RESPONSE TO ECONOMIC CYCLES ...................... 44
FIGURE 9 - THREE AREAS OF POTENTIAL INNOVATION .................................................. 44
FIGURE 10 - THE INTERDEPENDENCY OF INTERNAL AND EXTERNAL FACTORS OF THE SWOT ANALYSIS 47
FIGURE 11 - THREE GENERIC STRATEGIES ....................................................................... 49
FIGURE 12 - THE STRATEGY CLOCK: COMPETITIVE STRATEGY OPTIONS ..................... 51
FIGURE 13 - FOCUS ON THE SAS GROUP 2007 REPORT AND SUMMARY .......................... 71
FIGURE 14 - COMPOSITION OF SAS’ SHARES .................................................................... 71
FIGURE 15 - THE SAS GROUP’S AIRLINES ......................................................................... 72
FIGURE 16 - THE SAS GROUP STRUCTURE AND ITS BUSINESS AREAS ............................... 72
FIGURE 17 - THE MARKET SHARE OF THE SAS GROUP ..................................................... 74
FIGURE 18 - E-TICKET, SELF-SERVICE AND INTERNET CHECK-IN IN PERCENTAGE .......... 79
FIGURE 19 - SAS’ MODEL TO UNDERSTAND HOW TO FULFILL ITS CUSTOMERS’ BASIC NEEDS 89
FIGURE 20 - FIVE FORCES FRAMEWORKS (PORTER) BEFORE DEREGULATION, AUTHORS’ CREATION 110
FIGURE 21 - FIVE FORCES FRAMEWORKS (PORTER) AFTER DEREGULATION, AUTHORS’ CREATION 110
FIGURE 22 - INNOVATION CYCLES AS A RESPONSE TO ECONOMIC CYCLES .................... 120
FIGURE 23 - THREE AREAS OF POTENTIAL INNOVATION ................................................ 121
FIGURE 24 - INTERPRETATION OF OUR RESEARCH PROCESS, AUTHORS’ CREATION ........... 123
FIGURE 25 - KEY ACTORS IN THE NORTHERN EUROPEAN AIRLINE MARKET .................... 137

LIST OF TABLES

TABLE 1 - THE BENEFITS SOUGHT AND ACTUAL RESULT OF THE NATIONAL POLICY IN IRELAND ............................................................................................................................ 34
TABLE 2 – APPLICATION OF SCHUMPETER COMBINATION OF NEW MEANS OF PRODUCTION TO THE AIRLINE INDUSTRY, AUTHORS’ CREATION ......................................................................................................................... 40
TABLE 3 – APPLICATION OF SCHUMPETERIAN OPPORTUNITIES TO THE AIRLINE INDUSTRY, AUTHORS’ CREATION .......................................................... 42
TABLE 4 – APPLICATION OF SOURCES OF INNOVATION TO THE AIRLINE INDUSTRY, AUTHORS’ CREATION .......................................................... 43
TABLE 5 - THE EU AIR TRANSPORTATION PACKAGES ............................................................ 56
TABLE 6 - CHANGES IN COMPETITION ON SELECTED EU SCHEDULED ROUTES .................. 57
TABLE 7 - CAPACITY OF AIR SYSTEM (NUMBER OF SEATS AVAILABLE IN ’000) ON SCHEDULED RETURN FLIGHTS WITHIN THE EU ........................................................................................................ 58
TABLE 8 - AIRLINES SERVING THE EU MARKET ....................................................................... 58
TABLE 9 - ELFFAA VS. AEA, AUTHORS’ CREATION WITH AVAILABLE DATA COLLECTED .......... 61
TABLE 10 - DIFFERENCES BETWEEN LCC AND FSC, AUTHORS’ CREATION WITH AVAILABLE DATA COLLECTED .............................................................. 62
TABLE 11 - TOTAL SCHEDULED PASSENGERS CARRIED IN 2006, AUTHORS’ CREATION WITH AVAILABLE DATA COLLECTED ............................................................................................................................ 63
TABLE 12 - MEMBERS OF STAR ALLIANCE .............................................................................. 66
TABLE 13 - KEY FIGURES OF SAS AIRLINE .............................................................................. 76
TABLE 14 - SCHUMPETERIAN OPPORTUNITIES AND SAS AIRLINE, AUTHORS’ CREATION .......................................................... 92
TABLE 15 - SAS AND SOURCES OF INNOVATION, AUTHORS’ CREATION .................................. 93
TABLE 16 - EXAMPLES OF SAS’ NEW COMBINATION RESOURCES (ACCORDING TO SCHUMPETER THEORY) INDUSTRY, AUTHORS’ CREATION .......................................................... 94
TABLE 17 - SCHUMPETERIAN OPPORTUNITIES AND RYANAIR, AUTHORS’ CREATION ................. 101
TABLE 18 - EXAMPLES OF RYANAIR’S NEW COMBINATION OF RESOURCES (ACCORDING TO SCHUMPETER THEORY), AUTHORS’ CREATION .......................................................... 102
TABLE 19 - RYANAIR AND SOURCES OF INNOVATION, AUTHORS’ CREATION .................................. 103
TABLE 20 - SCHUMPETERIAN OPPORTUNITIES AND RYANAIR, AUTHORS’ CREATION .......................................................... 112
TABLE 21 - SCHUMPETERIAN OPPORTUNITIES AND SAS AIRLINE, AUTHORS’ CREATION .......................................................... 113
TABLE 22 - EXAMPLES OF SAS’ NEW COMBINATION RESOURCES (ACCORDING TO SCHUMPETER THEORY) INDUSTRY, AUTHORS’ CREATION .......................................................... 113
APPENDIXES

APPENDIX 1 - KEY ACTORS IN THE NORTHERN EUROPEAN AIRLINE MARKET ......................................................... 137
APPENDIX 2 - INTERVIEW WITH DAN LUNDVALL, LFV’S MARKETING DIRECTOR ................................................... 138
APPENDIX 3 - INTERVIEW WITH MATS VALINGER, VICE PRESIDENT CORPORATE DEVELOPMENT OF THE SAS GROUP .. 151
APPENDIX 4 - INTERVIEW WITH KJELL WILSBERG, DIRECTOR GOVERNMENT RELATIONS OF SAS BRAATHENS............. 153
1 Introduction

In chapter one, we will present the background of the study. We start by introducing the airline industry, and then we continue by giving our research problem and objectives. Afterwards, we will clarify the demarcations of our thesis and explain some terminologies. Finally you will find the disposition of the whole thesis.

1.1 Background of the Study

In most industries, economic agents need to obey the rules of the game introduced by institutions, that is, their strategies are limited by regulation imposed by the regulatory bodies of the industry where they operate in. Governments regulate public utilities following the public interest theory, with the main aim to control the market power and to correct market failures in the economy. Those state owned monopolies get more capital in their firm than it is needed, which is not fair for the other firms who are not provided with subsidies. This centralization of power hinders entrepreneurial activity, due to the fact that most of the decisions are made by the central actor, reduces the internal locus of control of economic agents and eliminates the rewards of entrepreneurial exploitation of market. The distortions that occurred in these markets are originated from regulation that instead of serving the public interest brings advantages only to one small group of the society with specific interests – that is, the organizations capture the regulation. Facing this situation, deregulation is the only solution to provide a better competitive environment.

This deregulation can come when economic agents identify problems and failures in this regulatory framework, put these norms under pressure and shake the rules of the game by previous legitimized institutionalized logics change. Deregulation may lead to a monopolistic competition which means that there are many competitors and consumers on the market, competitors try to differentiate their products with heterogeneous services, there are few barriers to entry and exist. There might be a non-price competition, based more on the differentiation of the product. The companies which take advantage of that situation, mainly the former state-owned companies, keep their customers thanks to brand loyalty even though their prices are generally higher than the average. This decentralization of powers and deregulation, according to Shane, provides opportunities for entrepreneurial exploitation and thus further changes in market structure (more competition and innovations). This was what happened in utility industries such as telecommunications, electricity or air transportation, where a natural monopolist dominates the market.

The telecommunication industry was also bind to deregulate. For instance, German telecommunication market was characterized, like in other countries in Europe, by having national monopoly where the competition was almost impossible. In order to solve that situation, the Government forced an evolutionary deregulation step by step. From that moment on, reduction of barriers to entry made it possible for new companies to enter into the market, which fostered competition and put an end to the former monopolies. The deregulation on this market was very

beneficial to the consumers since it slashed down the prices of the services: between 1996 and 2000 the prices of telephone services in Germany fell by approximately 23%, according to figures calculated by the Federal Statistical Office.\textsuperscript{10}

Air transportation market is one of the public utilities industries that was heavily regulated, in spite of the fact that in the last years the regulatory framework has been more relaxed since the deregulation in US and more recently in Europe. The failure to reach international multilateral agreements in Chicago Convention in 1944 mirrored protectionist policies from most countries and generated a strict market where transportation began to be governed by bilateral agreements that dictate the main aspects of the marketplace.\textsuperscript{11} These rules created distortions in the industry, hindered competition and entrepreneurial activity, and brought difficulties to achieve efficiency and socially optimum prices, since it enabled monopolistic state-owned carriers to set high fares and to restrain capacity. Some of these rules still prevail for most of international flights but have been relaxed since the deregulation of US Airlines in 1978 and more recently, the Single European Market in 1993.

Furthermore, this new environment triggered a handful of effects for airports, communities and aircraft manufacturers.\textsuperscript{12} One of the drawbacks of the deregulation in the airline industry was that since allowed entrepreneurs to create their company, lots of new comers arrived on the market, nevertheless they do not last and go rapidly on bankruptcy. They disappeared as fast as they arrived. So, only the strongest companies have been surviving and forged cartels and alliances with other companies, which in turns lead to less competition and to an increase in prices.\textsuperscript{13} To prevent these situation, antitrust regulations have been created, which ban monopolies or other collusion. Fifteen years later, the European skies would experience these same effects.

The deregulation of European Union (EU) air transportation market was a result of the attitude towards economic deregulation in Europe\textsuperscript{14} during the late 80s, the experience of the deregulatory reforms in US that proved the efficiency of liberalized market\textsuperscript{15} \textsuperscript{16}. Despite of the fact that the Treaty of Rome steered the economy into a more competitive road, air transportation competitive distortions from strict regulation only started to fade in 1987.\textsuperscript{17} Contrary to US market which from night to day went from a regulated to a deregulated market, in EU this transition went through a soft process during nine years where three different liberalization packages were implemented by EU institutions. In spite of the still existing limitations concerning ownership of EU carrier by non-citizens that limits entrepreneurial activity in the 27 countries,\textsuperscript{18} the slow change in the industry infrastructure that decentralized the powers of national governments concerning airline strategies, created more advantages and opportunities for entrepreneurial and innovative behavior that were not possible before.\textsuperscript{19} \textsuperscript{20} Several new entrants challenged the status quo of the industry with one third of the costs of the old carriers, low fares with price discrimination, second-hand airplanes, non-union labor and point-to-point routes.\textsuperscript{21} This change in the market and industry

\textsuperscript{17} Ibid, p. 113
structure is, according to Drucker, a source of innovation and entrepreneurship. And in fact, this more competitive environment fostered incumbent airlines to innovative strategies such as hub-and-spoke networks; frequent flyer programs and made an efficient use of computer reservation systems (CRS).

SAS and Ryanair are two examples of companies with distinctive business models that saw in deregulation opportunities to come with entrepreneurial behavior and innovations. SAS, the Scandinavian flag-carrier that had enjoyed exclusive monopolistic rights in many routes suddenly had to adapt to the new market structure that fostered competition. Opening of new markets (like exploring the newly deregulated Baltic markets) creation of new products and services (like the self check-in) are examples of entrepreneurial behavior that was fostered by deregulation.

In Ireland, the new-entrant Ryanair saw in deregulation an opportunity to introduce a new business model in Europe, new services to new markets and low fares to 300 million people that were being explored by the high fares of flag carriers. The dominance of sources of supply (previously unused airports) was also a contribution to the success of this new model that was not possible to introduce with previous regulation that restrained capacity, fares and routes. Ryanair was also able to change the regulation in its favor through a process of institutional entrepreneurship, in order to introduce its business model in new countries. Ryanair business model is an example of creative destruction and challenge of the previously established market equilibrium.

Deregulation brought great changes to the European air transportation market and to European travel market. The curiosity in knowing the causes of this change and the willingness to explain them, led us to look at the airline industry with more interest and to come with the following research problem that would lead us to elaborate this thesis.

1.2 Research Problem

The research problem of our thesis is the fact that since the 80s European airlines have gone through financial difficulties mainly due to changes in the regulatory context. The different deregulation packages opened the doors to new entrants in the industry like Ryanair and more opportunities for different strategies, mainly fare reductions. In turn, this promoted a more competitive environment and a price-war.

The competition is only at the beginning since it is only since 1 of April of 1997 that flag carriers were allowed to practice cabotage (that is, the right of a carrier from country A to transport people between two points inside country B). Therefore, plenty of innovative and entrepreneurial behaviors have occurred in the industry since then, like the introduction of franchising in the airline industry, self check-ins and alliances, and still more are to occur like the development of a new generation of CRS (computer reservation systems). These new strategies were needed to survive in the new competitive environment and to assure profitability to assure big amounts of money in investment that is characteristic of the airline industry.

The dark Tuesday 11th of September 2001 was the darkest day for the airline industry. The consequences of that day were disastrous for the aviation industry. A couple of minutes after the
planes had crashed; all the flights from/to the United States of America were cancelled and forbidden until FAA will give its “green light”. Thousands of planes were pined down and suddenly the American sky was empty. As other many world citizens, we were shocked and sad with this tragedy and wondered what would be the next sequence of events – were we will be able to travel safely again?

Unfortunately fear was the key word that can best describe followed these events. Passengers were afraid and reluctant to fly. The aviation industry was badly hit and saw a heavy decrease in the number of passengers. Within this, thousands of planes became useless and are still ditched in deserts around the world, brand new airports and terminals became empty, the average seat load factor of aircraft dropped drastically, dozens of airlines disappeared and went on bankruptcy, such as the eminent Swissair (Suisse) or Sabena (Belgium) because of the economic crisis and the intense competition in the industry fostered by the recent deregulation. Thanks to the numerous slots that flag-carriers left, there were possibilities, as we will see through the thesis, for companies like low-cost carriers to enter into the market. Flag-carriers had to face a new generation of competitors with new strategies and they wanted to take urgent measures or they would disappear. Therefore the old airlines had to gather in alliances (Star Alliance, SkyTeam or oneworld) and began to innovate. In the beginning of the 21\textsuperscript{st} century large lay-offs occurred in the airline industry.

Taking all these facts into account, our main research question can be stated as the following:

\begin{quote}
How did the deregulation of air transportation in Europe foster entrepreneurial behavior and innovation in the European airline industry over the last twenty years? The case of SAS and Ryanair.
\end{quote}

1.3 Research Objectives

The main objective of this study is to know how the deregulation of air transportation in Europe fostered entrepreneurial behavior and innovation in the European airline industry. For that reason we start with the assumption that deregulation implies more entrepreneurship and innovation. This entrepreneurial behavior that brought innovation to the industry was both from individuals who created their own airlines but also from the old carriers that had to adapt to the new business environment that now is characterized for having “new competitive environment forces”\textsuperscript{25}.

Thus we will compare the strategies of the firms in the regulated environment with the firms in the deregulated environment and point the new opportunities and innovation that arose with the change in the regulatory context how did the carriers adapt to these changes. Within this study we will provide a comparison with other deregulated industry like telecommunications or electricity and build a framework applicable to deregulation and entrepreneurship.

We will divide our thesis in two different case studies from two different companies (Ryanair and SAS) that correspond to the two main business models in the airline industry – the no-frills model (used by low cost airlines) and the frills model (used by flag carriers and old airlines). For each case study we will analyze the opportunities that deregulation provided for entrepreneurial behavior and innovative strategies, and how the firms adapted to these change.

The three primary objectives of our thesis can be defined as the following:

- **Explorative**: the link between deregulation-institutions-entrepreneurship-innovation in the airline is not often mentioned in previous research (as we will explain in chapter 4.1); therefore we aim to introduce new knowledge within this area. Furthermore our thesis will be focus on two specific companies, Ryanair and SAS that correspond to two distinct business models. However, since we are focusing in past events, different regulatory frameworks (each EU country had a different regulatory regime), different contexts (Ireland and Sweden) and two specific companies (limited number of case studies), we are aware of the problems in generalizing this study to other companies in other contexts within the airline industry.

- **Descriptive**: we will be also describing a situation (the behavior of Ryanair and SAS within the deregulatory context) and a process (the evolution of deregulation in the EU), our second research objective is also descriptive

- **Predictive**: basing our analysis on the past events of deregulation, at the end of the thesis we will anticipate what would be the future trends of the regulatory framework in the EU as well as the next moves of SAS and Ryanair in this new context. For predicting the consequences of the phenomenon of deregulation in EU and anticipate what will come, our third research objective is predictive

### 1.4 Demarcations and Limitations of the Study

Since we are only interested in SAS Airline and Ryanair, entrepreneurial and innovative behavior in the deregulatory context, this has some implications for our study. Our geographical limitation from focusing solely in SAS and Ryanair gives us an understanding of their specific environments – Scandinavia and Ireland-UK – and thus makes more difficult to generalize the conclusions of our study to other environments in Europe. In order to know the degree the deregulation in Europe fostered entrepreneurial and innovative behavior, one would have to investigate all the different regulatory environments from each EU country. This would require a significant amount of time in order to first get an understanding of airline industry domestic rules of each EU country and then to have knowledge of both flag-carriers and new entrants, in order to get two different perspectives of the main business models.

This generalization constitutes the main limitation of our study. Even if we have only talked about Scandinavia and Ireland-UK environment, if we would generalize from SAS to all other Scandinavian airlines or from Ryanair to all others Irish or British carriers, this would be a problem. This is due to the fact that there are plenty of characteristics that are specific to one company. That is, there is an unknown degree of specificity.

Another aspect to consider is the time perspective. Within our study we only considered the changes in European deregulation from the implementation of the First Aviation Package implemented in January 1988. Despite of changes in regulation had started in the 60’s, they are out from the limits of our study. Furthermore, bearing in mind the age difference between the young Ryanair and the old SAS, analyzing prior changes to the aviation packages, no further comparison

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could be possible since Ryanair was only born in late 1985, whereas SAS was found in 1946. Therefore, when we mention deregulation we are referring the implementation of the three aviation packages in 1988, 1990 and 1993, plus the full cabotage in 1997 (that was integrated in the last package).

1.5 Definitions and Abbreviations

**AEA**: Association of European Airlines – association with 30 members that includes most of the flag carriers in Europe

**Airline alliances**: agreements between airlines to coordinate their services in various ways such as code-sharing, common frequent flyer programs and lounge facilities, coordinated scheduled, etc.

**BA**: British Airways

**BAA**: British Airports Association

**CAB**: Civil Aeronautics Board

**Cabotage**: right of an airline from a country A to provide domestic flights in country B

**CFROI**: Cash Flow Return On Investment

**Charter**: air services that operate out of the scheduled (see also non-scheduled flights) in a seasonal base

**Code-sharing**: marketing agreement made by airlines that enables them to sell seats on each other’s flight under their own designator code.

**Consolidation**: reduction in the number of market players through firm closure or through acquisition. Firms that remain in the market achieve a greater market concentration

**Computer Reservation System (CRS)**: electronic data management system that distributes information, availability status and price of travel services to retailers and directly to consumers.27

**Economies of scale**: average unit cost of production declines as output increases

**Economies of scope**: an organization can produce two or more services cheaper than if organizations that produce them in separate ways

**Economies of traffic density**: average unit cost of production declines as the amount of traffic increases between any given set of points served28

**ERAA**: European Regions Airline Association

**ELFAA**: European Low Fares Airline Association

28 Ibid, p. 120
Frequent Flyer Program (FFP): marketing strategy which aims to gain consumer loyalty. Within these programs the traveler earns miles in each flight and later on can exchange them for a ticket, on-board services, upgrade services, etc.

Hub-and-spoke networks: operating structure of an airline where it focus its operations in one or two airports – hubs – which are fed by routes to and from other points – spokes. The traffic is consolidated at the hub and then redistributed through connection flights to other destinations.

IATA: International Air Transport Association – global airline association that includes most of airlines

Interlining: two airlines made a formal agreement (an interline agreement) that enables the carriage of passengers and freight by one airline on behalf of another airline. Both carriers need to honor tickets issued by other carriers.

Landing fees: price aircraft have to pay to the airport in order to be able to land

LFV: Luftfartsverket – Swedish state owned company that controls most of Swedish public airports

Long-haul flight: transcontinental flights those last more than 7 hours

Lounge: waiting room that is owned by an airline or by an alliance which offers free different services (snacks, drinks, internet access, fax, etc) to its business, first-class passengers, and passengers with a certain level in FFP.

Low Cost Carrier (LCC): airlines that compete in a price base through the slashing of their cost base using a no-frills strategy

No-Frills: strategy that consists in removing all the on-board services and other auxiliary services that provide an added value for the passenger and that some airlines consider being more than essential and thus removing them

Flag Carrier: state owned airline which benefits from special concessions from the state like monopolistic routes and favorable domestic regulatory regime that hinders new entrants to challenge their air transport monopoly.

Full Service Carrier (FSC): an airline that competes both in price and in differentiation and provide added value to their passengers, that is, it has a with-frills strategy. They are network carriers that provide a diversity of hub-and-spoke services (but operate point-to-point services too) and offer different quality services. It can be private or public owned. Flag carriers are considered to be FSC.

MNC: Multinational Company

Non-scheduled services: flights that operate in an irregular base, most of the times seasonal and according to specific demand. Charters are the most well known non-scheduled services.

One-way ticket: ticket that is sold only between two points (one route)

Point-to-point route: route between two secondary or regional airports

SAS: Scandinavian Airline System
**Chapter 1**

**Introduction**

**Scheduled services**: flights that operate regularly and systematically and that are listed in a published timetable

**SEM**: Single European Market

**Self check-in**: machines that allows the passenger to make its own check-in

![Figure 1 - Self check-in](http://www.flysas.com/en/Travel-info/Check-In/Automats/Cards_for_check-in/)

**Short-haul flights**: flights which last less than 3 hours

**Slot**: right to land and to take-off from an airport at a specific time previously allocated to the airline.

**Yield management**: form of price discrimination where customers are charged different prices for the same product based on their willingness to pay

### 1.6 Disposition of the Thesis

In order to be really clear in the mind of the reader and to have quick glimpse, we have decided to show the disposition of the thesis with a slight summary of each chapters.

**Chapter one: Introduction**

*In chapter one, we will present the background of the study. We start by introducing the airline industry, and then we continue by giving our research problem and objectives. Afterwards, we will clarify the demarcations of our thesis and explain some terminologies. Finally you will find the disposition of the whole thesis.*

**Chapter two: Research Considerations**

*The Research Considerations will be described in chapter two. We will explain the reasons for having chosen this topic, the preconceptions that we had before starting the thesis but also the scientific ideal and scientific approach. In the end of this chapter, you will discover the research design and the perspective of the study used.*

**Chapter three: Practical Method**

*In chapter three, we will describe the practical method of our thesis. We explain how we conducted our researches. We explain how we found our sources and then we will have a critical approach and a discussion about them. The sources include both selection of scientific literature and interviews that we have conducted.*

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Chapter four: the Airline Industry and Theoretical Framework

Chapter four will present the institutions and regulation within the airline industry. Then, we will make an analysis on the context and on the industry thanks to the PESTEL framework, we will see if there are new entrepreneurial opportunities and changes in the environment. Afterwards, we will analyze how entrepreneurship and innovation can be applied to the airline industry. Finally, competitive strategies will be explained.

Chapter five: Empirical Data Presentation

In the chapter five, we will present our empirical data of the thesis. Since case study theorists argue about the importance of collecting multiple sources and types of evidence to achieve validity, we decided to hold data from different sources and tried to get the most variety of data. We start with a short presentation of the airline industry and by introducing the largest European airline companies as well as the major variations in the airline industry’s development. Then we will continue by presenting SAS’ and Ryanair’s company data.

Chapter six: Empirical Data Analysis

Chapter six will be the empirical Data Analysis on SAS and Ryanair. Afterwards, we will compare both business models.

Chapter seven: Conclusions

Chapter seven will be the conclusions of the Thesis where the problem statement, the objectives, the theoretical framework and empirical data will be combined and analyzed together. Conclusions will be organized like a conversation on the different previous chapters of the Thesis where opinions could be given.

Chapter eight: Further research

In chapter eight, we will propose future research that we have identified along our research process which could be interested to go deeper.

Chapter nine: Criteria for Evaluation

In chapter nine, we will explain and discuss about the components of trustworthiness, authenticity and transferability of our thesis.

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2 Research Considerations

The Research Considerations will be described in chapter two. We will explain the reasons for having chosen this topic, the preconceptions that we had before starting the thesis but also the scientific ideal and scientific approach. In the end of this chapter, you will discover the research design and the perspective of the study used.

2.1 Choice of Topic

The enlargement of the EU, the attacks in New-York 11th of September 2001 and the economic downturn which followed these events are some recent examples of the evolution in the aviation industry. The deregulation in the airline industry like in others (as we will see in this thesis) is a logical result of the recent economic trends that conduct to liberalization of the markets.

When we chose this topic, we were interested to discover how the situation evolved for the aviation industry during the last years and what are the reasons behind the boom of low cost carriers and their “killing fares”, as well as why only now we are watching this intense competition. Why weren’t there any low cost carriers in EU and the 80s and beginning of 90s? Why have the old flag carriers produced plenty of innovations in the last years like the self check-in or the lounges? These were some of the questions we were interested to know when we chose the subject.

After that we asked ourselves if the process of deregulation in the airline industry in EU was related with the recent trends deregulation in other industries in Europe like the telecommunication and electricity industries. For that reason, during this thesis we are also finding if there are any differences or similarities between the airline industry and other industries like telecommunications and electricity, in order to give a better answer to our research question.

As part of our thesis, we wanted to make interviews with professionals of airline industry to have their points of view in order to compare their points of view with the information that we could find in books, magazines, annual reports and other kinds of sources. As we were also interested in the airline industry and to understand and explain its evolution, we wanted to have to investigate in this industry and applying the knowledge we learnt during our courses in Entrepreneurship at the Umeå School of Business and Economics. Taking into account the available time and the obligation to focus only on a specific topic led to find a relevant research question to study, we decided to analyze the correlation between entrepreneurship and the airline industry in EU, taking the case of Ryanair and SAS into account. Briefly resuming, the reasons for making case studies about SAS and Ryanair were simple because SAS was one of the old carriers that most faster answered to the recent changes in the environment, introducing a handful of innovations in the market like the self check-in and subsidiaries airlines, and Ryanair was the first low-cost airline in Europe and currently the most successful one.

2.2 Preconceptions

This essay is written as a Master thesis at Umeå School of Business and Economics (USBE), Spring Semester 2007.

As researchers from a Master thesis, we are asked to have an objective work without interfering with our personal thoughts. Nevertheless, when you are starting your thesis, you have many preconceptions on the topic according many aspects and you can be influenced by your
personal and educational background, your knowledge, etc. If you include individual knowledge into your work, it can be biased. Moreover your ideas may differ from the point of view of your partner; you may have different ways of approaching the topic. Preconceptions can come from various backgrounds: information that you have heard or read, knowledge that you have acquired during your studies but also through events that you have personally experienced.

Gilles HELTERLIN  

I am a 23 years old French student at USBE. I have been studying at USBE since August 2006 in the Master’s Program Entrepreneurship and Dynamic Business Contexts. Before attending this program, I studied at Burgundy Business School in Dijon during two years.

During my first course here in Umeå, I followed an interesting course called: Perspectives on the Business Context in which we talked a lot about the airline industry and its development thought the last decades. I really liked this course and it may have been the first good ‘springboard’ in my process of choosing a topic.

The second reason is because I am passionate in the airline industry. Since my childhood, I have always thought of being a professional pilot but the opportunity has not come yet. But we do not know what the future will be; being an entrepreneur means taking risks and believing in what you are doing!! Does not it?

Furthermore, since I am a child, I have had opportunities to travel whether on scheduled, low-cost or charter flights on short-haul, medium-haul and long-haul flights. So, let us say that I am used to flying and I like that so much.

When I started my Master Thesis, I had many preconceptions on the airline industry; however I wanted to go further in the discovery of this wonderful industry and see if there were similarities with my own perception of it but on always being objective.

Nuno BERBERAN  

I am 22 year-old Portuguese student and since August 2006 I’ve been studying in Umeå, Northern Sweden, where I’ve been enrolled in the Master’s Program in Entrepreneurship and Dynamic Business Contexts. Before attending this program, I studied Business Administration during three years in Lisbon.

The first subject I attended here in Umeå was decisive for the choice of the topic since for the first time I studied the airline industry, one topic I had always wanted to study but never got the chance to. Even though in Lisbon I studied subjects where examples of airline industry were given like Marketing or Strategy, however I had never had a deeper knowledge of the topic.

Despite I had never worked in the airline industry or had studied it, having relatives working in the industry planted a special affection to air transportation. The easiness in traveling contributed to the development of my interest in the traveling. My traveling experience mainly concerns European routes, mainly operated by TAP. However, since in our study we do not focus in TAP, my preconceptions did not affect the objectivity of our study.

Regarding my theoretical preconceptions, after the Master Program I my knowledge in Strategy was reinforced and, because of the focus of the program, my interest for Entrepreneurship
rose. I argue the knowledge I gained in Umeå contributed more to my abilities and to the
development of this thesis than the knowledge I gained in previous years. The focus in
Entrepreneurship and the critical spirit towards academic work that is cultivated in the program had
a positive effect on my abilities to understand the relevant theories and to linking the different
theories with each other, relating them with the empirical data.

2.3 Scientific Ideal (Epistemological considerations)

Epistemological issues are related with the question of what should be considered an
acceptable knowledge in a discipline. Within epistemological considerations there are two
doctrines: positivism and interpretivism. We will now give a brief description of each one and
explain our choice.

Positivism applies the same methods and principles of the natural sciences in the study of
social issues and focus on giving explanation of human behavior. It follows five principles:
phenomenalism (senses are the judges of knowledge), deductivism (theory should generate
hypothesis to be tested), inductivism (gather of knowledge is the basis for laws), objectivism
(science should be value free) and puts emphasis on scientific statements.

Interpretivism is the opposite doctrine of positivism. It argues that because the subject of
social sciences is different from the one of natural sciences, a different strategy and logic should be
used. It focus on the understanding of human actions rather than it explanation.

In our thesis we will apply some principles of positivism such as deductivism. Furthermore,
we will also have three main research objectives are exploratory, descriptive and predictive.
Therefore we argue the most adequate scientific ideal is the positivism.

2.4 Scientific Approach

When you are talking about the scientific approach, you can approach it by three different
ways. The first approach is the deductive one. It means that you confront existing theories with
empirical data. You start from theories and you end with hypothesis. The theories will be verified or
falsified according the data you will provide. The second one is the inductive approach. It is the
opposite; you start from hypothesis or empirical data and you end by formulating a theory because
there is no theory on the study you are working on. So you collect and gather data in order to
produce new problems or theories. The last approach is the abduction approach. It is an interaction
between the deductive and the inductive approaches.

The purpose of our thesis, as we said previously, is to define how the deregulation of air
transportation in Europe fostered entrepreneurial behavior and innovation in the European airline
industry. We would like also to relate to this main objective other goals like describing how Ryanair
and SAS were influenced by the changes in the context, if they could steer this change to their own
benefits, if the final effects of deregulation benefited them, how further deregulation will influence
entrepreneurship and innovation.

32 Ibid, p.12-13
33 Ibid, p.15-19
34 Ibid, p. 9-13
Chapter 2 Research considerations

Having these two approaches in mind, we decided to choose the deductive approach because we will start from different theories on our topic like the ones from Schumpeter, Shane and Drucker that assume changes in context foster entrepreneurship and innovation, more precisely changes in innovation. Then we find empirical data to demonstrate this theory through interviews with companies, public documents and bibliographies. With all the information that we collected, we integrate them in the theories and present our findings on the topic35.

2.5 Research Method

There are three different ways to analyze a specific problem. The researcher is the responsible to select the best method that will fit in the research problem and that will solve the research objectives. Within the possible choices, there are three different methods the researcher can use to solve the problem: quantitative method, qualitative method and multi-strategy research, which is a combined version of the two previous methods. Now we will briefly describe each one of them:

The quantitative method, as the name suggests, is more focused in the quantification of data through numbers and causal relations. It is closely linked with the deduction theory (it departs from existent theory and not from empirical facts), positivism theory (adapts the processes used in natural sciences to test the validity of a theory) and objectivism theory (the social reality is external to the researcher)36.

The qualitative method uses words and empirical facts when collecting and analyzing found evidences. It is closely linked with the inductive theory (the collecting of data is the departure point in order to afterwards generate a theory), interpretivism theory (gives a subjective meaning to the empirical data in order to generate a theory) and constructivism theory (the social reality is being constantly built by the individuals and so it is subjective)37.

Finally, the multi-strategy method, can present multiple formats depending on the epistemological and ontological theories from the previous two methods the researcher wishes to combine as well as the methods of collecting data used on them38.

To collect data we adopted a qualitative approach since its methods were much more suitable for the purposes of our research. For instance, departing from any question, inverting their order are some advantages of using of semi-structured interviews39. For our purposes, the flexibility of qualitative interviews suited much more than the rigidity of quantitative interviews, since we could adjust the emphasis of interview in significant issues that rose during the interviews. Furthermore, we wanted detailed answers in order to better fulfill our descriptive objective and to gather the greater amount of information. Taking this into account, semi-structured interview proved to be a better tool.

Besides using semi-structured interviews, we used another qualitative method to gather data – personal, public and organizational documents. For instance, to write the story of Ryanair for one of our case studies, we based in two sources: SiobhánCreaton’s Ryanair – How a Small Irish Airline Conquered Europe (2005) and Simon Calder’s No Frills, The Truth Behind the Low-Cost Revolution in the Skies (2006). The first one was the main source to Ryanair case study. These two

36 Ibid, p. 25
37 Ibid, p. 25
38 Ibid, p. 465-494
39 Ibid, pp. 341-343
sources were selected since they proved to be the most current sources at the time we wrote the case studies, with the most detailed picture of Ryanair culture and evolution of strategies, besides providing useful information. The second book was used as a complementary of the first one.

We used also public documents in our thesis such as EU publications, international aviation treaties, airline association’s statistics and newspaper and magazines news. Organizational documents include several annual reports, quarterly results and strategy documents that were obtained from airlines web page.

We will now explain how we used constructivism:

Another reason concerns practical ontological issues. Connecting with what was said before; constructivism theory does make more sense from our point of view. Deregulation is produced by the actors in the reality (in our case, the EU institutions) through their interaction therefore is a social phenomenon. Invoking Institutionalism theories and bringing Douglas North arguments, institutions interact with organizations and correcting their models of action (in which they act with incomplete information). It is this interaction between institutions and organizations that steers the way institutions change in an economy. Institutions are like the rules of the game and organizations and entrepreneurs are the players. Also Meyer and Rowan approach supports a constructivist approach of environment in the interaction between institutions and organizations, arguing that organizations structurally reflect the socially constructed reality where they operate and are conditioned by institutional environment. This implies that the existence of deregulation (or regulation) is dependent upon the actors (without EU institutions there would be no legislation and therefore no further EU deregulation) and not an external existence separated from them.

Furthermore, this deregulation is in a constant state of revision (through the different packages, regulations and decisions), which supports the argument that this social phenomena results from social actors. This constant construction is present in the neo-institutional theories (that we will use in this thesis) which argue changes can occur from environmental jolts, which are simply changes in environment. Actors are able to contribute to constructions in their reality, that is, social phenomena results from social actors. This action where actors change the current characteristics of the industry or society and thus change institutions is called institutional entrepreneurship. This approach considers the agents as sources of change (the institutional entrepreneurs), that is, it focuses on the endogenous sources of deliberate change. The concept of creative destruction used in Schumpeter’s entrepreneurship theories that was previously presented in this chapter is integrated in the explanation of this approach and highlights the constructivism theory. That is, the entrepreneur will carry out new combination of resources, in order to fix the current situation in his/her environment that is hindering him/her actions.

2.6 Research Design

A research design can be simply explained as the name given to the link between the empirical data collected for a study and its research questions, and at the end with the conclusions.

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generated from the study\textsuperscript{45}. As Yin simply puts, “\textit{a research design is an action plan for getting from here to there}”\textsuperscript{46}. There are five main types of research designs: experimental design, cross-sectional design, longitudinal design, case study design and comparative design. Following this introduction of the different types of research designs, we will briefly present each one of them and argue the reasons that led us not to choose or to choose them (depending on each case).

The \textbf{experimental design} is many times regarded as a field experiment, are most of the times related with quantitative methods and are rarely done in business research. One of the main reasons why it happens is that it involves a manipulation of independent variables in order to determine its influence on the dependent variable. It also implies that experimental groups and control groups are needed to make a further comparison before and after the manipulation\textsuperscript{47}. Since our thesis is focused in a timeline and it involves historical and economic facts out of our control (since they have already happened in the past), these empirical data is also unable to be manipulated. Therefore, this type of design can not be used in our investigation.

The \textbf{cross-sectional design} can be also referred as social survey design and it involves the collection of quantitative or quantifiable data (through questionnaires, interviews, surveys, etc) within several cases at a specific point in time, establishing patterns of associations between two or more variables. Later, comparisons are made with the surveys formed in other points in time\textsuperscript{48}. Connecting with our thesis, the problem with this type is that the collection of data is made at least two times through different periods of time. Since our limitation of time to write this thesis, this approach is impossible to be followed. One could argue that past data from other researchers could be used, but that will hinder us to obtain the specific information needed (since the researchers looked for other type of information related to their topic of investigation) and then to make a comparison.

The \textbf{longitudinal design} is used to find specific alterations in contexts, organizations or industries. A sample is surveyed several times in different occasions in order to find the effects of the independent variables within the time period\textsuperscript{49}. Due to time and cost involved, and for similar reasons as the cross-sectional design, we avoided to use this type of design.

The \textbf{case study design} describes the analysis of a specific single case that can be a single organization, a single location, a person or a single event. Therefore, the empirical data is retrieved specifically from that case and for that case\textsuperscript{50}. A case study investigates one of the single cases mentioned above and seeks from different types of empirical data in the case setting in order to answer specific questions. The use of various sources of evidence is the main characteristic of case studies, since it using only one type or source of evidence is not enough to achieve validity\textsuperscript{51}. For our thesis, in part we selected this type of design, since the aim of the case study fits with the research objectives and the research problems of our thesis – an analysis of the consequences for entrepreneurs of specific events that happened on the European air transportation industry (three different deregulation phases). The \textbf{comparative design} makes an analysis of at least two contrasting case using more or less the same methodology. It can be realized through a quantitative or qualitative approach and it is focused in a comparative study of social phenomena. When it is applied to qualitative method, the

\begin{itemize}
    \item \textsuperscript{45} Yin, R. (1989) \textit{Case Study Research – Design and Methods}, Sage Publications, p.28-29
    \item \textsuperscript{46} Yin, R. (1989) \textit{Case Study Research – Design and Methods}, Sage Publications, p.28
    \item \textsuperscript{48} Ibid, p.48-51
    \item \textsuperscript{49} Ibid, p.52-53
    \item \textsuperscript{50} Ibid, p.53-56
    \item \textsuperscript{51} Gillham, B. (2000) \textit{Case Study Research Methods}, Continuum, pp.1-2
\end{itemize}
multiple-case-study is the chosen approach to the researcher investigation. In spite of the critics concerning this approach (that will be presented later on) we adopted this design. The following section will explain the reasons that led us to choose the comparative design at the cost of other types of design.

The main reason is that to study the effect of the deregulation of air transportation in Europe on entrepreneurial activity, one should take into consideration the three different packages of deregulation that came into force through EU Commission. To analyze the opportunities it provided for the entrepreneurs, one should also make a comparison with the previous situation in order to argue that in fact the deregulation brought a new situation to the industry, which in turn provided entrepreneurs to exploit opportunities that until the date were not possible. Therefore, we found that using one single case study to answer our research question and to fulfill our research objectives would be too inappropriate since it would have to be focused in several events, which goes against the main purpose of a case study. Even if we have divided the one single case study into several parts, it would have been complex for the reader to understand the specific effects of each deregulation. Thus, the multiple-case study was the design that offered the best possibilities to link the empirical data with our research problem and objectives.

The following figure provides the research approach to multiple-case studies that we will follow through our thesis:

![Figure 2 - Replication Approach to Multiple Case Studies](image)

Of the critics of multiple-case-study made by Dyer and Wilkins regarding Eisenhardt the argument to use this approach to better generate theory, is that the researcher will be less focused on the specific context of each case study and more focused on the contrast between the different cases. Therefore the researcher will be doing a less deep analysis instead in order to do a more comparative analysis, and will end up losing the “essence of case study research”. Since we are

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aware of this problem, we focused first in the context of European airline industry, and afterwards started a deeper analysis of Ireland and Scandinavian regulatory environment. We provided different sources of empirical data concerning these two contexts in order to have a deep understanding of the environment were SAS and Ryanair operated. After this we provided a comparison between the two organizations taking into account the specific context of each one.

### 2.7 Perspective of the Study

This part concerns how we look at a specific problem. This is important since when presenting a problem, a theory, a framework and a statement, people can look at them and interpreting in a different way. Thus, we argue that is important to clarify which perspective we will take when we write this thesis.

Our thesis aims at explain how did the deregulation of the airline industry in Europe fostered entrepreneurial behavior in Ryanair and SAS. To do that, we collect both existent information in books, journals and scientific articles and information from interviews with people inside the industry and the firm (SAS). We assume that the people interviewed as well as the ones that have been already interviewed by other persons present a completely reliable source of information and thus have the best overview and knowledge about the industry and the firms we purpose to write the case studies. However we should bear in mind that if we had interviewed other people the results probably would be different since everyone has his own perspective and interpretation of a certain problem.

As we are dealing with two different business models, we will have two different perspectives of the problem – one from the already established airlines that suddenly faced a totally different business environment and other from the new comers that entered in a industry where many entry barriers had been broken down and the market provided a handful of opportunities for business.
Chapter 3 Practical Method

In chapter three, we will describe the practical method of our thesis. We explain how we conducted our researches. We explain how we found our sources and then we will have a critical approach and a discussion about them. The sources include both selection of scientific literature and interviews that we have conducted.

3.1 Selection of Sources

The selection of sources is really essential when you are writing a thesis. It must be interesting for the thesis and bring scientific information. The outcome of the thesis depends on the quality of the sources. Sources are divided into two types of sources, primary and secondary sources. Primary data consists of original data collected by the researcher himself and created during the whole process of the study; secondary data consists of information gathered by other researches for similar or different purposes than their own or by various institutions in the course of their business but also official statistics collected by government departments for statistical purposes\(^{55}\).

Sources can be present in different forms. You can find information in books, journals, newspapers, articles, essays or even in other thesis. However you can also find useful information in media like television, advertisements, Internet... In the same time, the information that you collect during an interview is a primary key source as well.

Now, we will describe how and why we selected the sources that we used for our thesis.

3.1.1 Selection of Literature and Scientific Articles

Once we had found our topic, we started searching for literature, articles and books. The goal was to have a better idea of the thesis’ structure and to gain more knowledge on the topic we had chosen. We started with secondary sources, such as books or articles, in order to extent our self-knowledge on the topic. In the beginning, we used search engines like Google Scholar\(^{56}\) to find interesting articles. Then, we used databases provided by the University Library\(^{57}\) such as EBSCOhost to find peer-reviewed articles, Emerald and Jstor for E-journals, which provided more scientific articles. When we used these databases, we taped keywords or combinations of keywords such as: deregulation, aviation, airlines, market, SAS Airline, Ryanair. We also used other theses which were dealing with more or less our topic that we found either at Studentexpedition or one the website of Diva-Portal\(^{58}\) to get ideas about the structure of the thesis, the relevant literature they used and authors who wrote interesting theories in correlation with our topic. Ideas that we used were only secondary data.

To define our topic, we also took ideas and definitions that we have been taught during the autumn semester. The entrepreneurial course literatures but also the research methodology courses lead us to define our topic as well. The guidance information that we received during these courses was precious in order to well structure our thesis. To have a perfect and not an influenced-point of view, it was of primary importance to use different sources and not only focus on one author. It is


\(^{56}\) http://scholar.google.com/

\(^{57}\) http://www.ub.umu.se/eng_infosok/eng_databaser.htm

\(^{58}\) http://www.diva-portal.org/
for the reason that we searched many authors to have varied aspects of our topic. To goal was to give a precise answer to our problem statement.

### 3.1.2 Selection of Primary Sources

Primary data, as we saw previously, are information that has never been collected. They can be collected by one of the following primary data collection processes:

- Interviews
- Surveys
- Questionnaires
- Observation

We chose to collect primary sources thanks to interviews (Chapter 3.3).

### 3.1.3 Selection of Other Sources

When we wrote our thesis, we tried to get as much primary sources as possible in order to get the most current day information about our topic thanks to interviews. Nevertheless, we used also secondary sources, especially to define the starting theories on which we based our thesis.

As we said before, other sources included personal, public and organizational documents. Personal documents were basically used to write Ryanair’s case study since we could not get any interview with the firm (Ryanair does not allow interview with students: “We regret that we cannot ascertain requests for individual meetings with our staff for school/college projects.”) We based our researches on two sources: Siobhán Creaton’s *Ryanair – How a Small Irish Airline Conquered Europe* (2005) and Simon Calder’s *No Frills, The Truth Behind the Low-Cost Revolution in the Skies* (2006). The first one was the main source to Ryanair case study. These two sources were selected since they proved to be the most current sources at the time we wrote the case studies, with the most detailed picture of Ryanair culture and evolution of strategies, besides providing useful information. The first book was based in several days of conversations with O’Leary, Tony Ryan and many other central actors to the firm. The second book was used as a complementary of the first one. The second book included diverse chapters with diverse LCC and was used not only as a complementary of Creaton’s book but as a source of information of the entire LCC business model. The book was made with interviews from LCC CEO’s like Sir Richard Branson (Virgin Airlines), Barbara Cassiani (former CEO of GO), Stelios Haji-Ioannou (CEO of Easyjet) and Michael O’Leary (CEO of Ryanair).

We used also public documents in our thesis such as EU publications, international aviation treaties, airline association’s statistics and newspapers and magazines news. Organizational documents include several annual reports, quarterly results and strategy documents that were obtained from airlines web page.

These sources were all the articles and books we found and read but in addition we analyzed Annual Reports, various statistics and ratio of airline companies like SAS and Ryanair over the last decade.

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Chapter 3 Practical Method

The benefits of the secondary sources are that they generally cost nothing and they are easy to find with search engines or directly on the websites of companies, so you save time and money. Furthermore, most of the secondary sources are high-quality data for many reasons: the sampling methods used are well representative (it covers the whole country or region for instance) and the sources are quite often experienced researchers who have an excellent background (e.g. http://europa.eu.int).

3.1.4 Types of data

There are two types of date collected; they can be either qualitative or quantitative. Qualitative data describe rather nominal data (semi-structured interviews…), and on the opposite quantitative data describe rather numerical data (turnover, annual reports…)

Quantitative or numerical data research must “be prepared so that it can be quantified” and easy to measure; for instance, a person’s age, incomes and so on. Thank to the data collected from questionnaire or structured interviews for example, we can use statistics. Quantitative data can also be found in tables, charts and graphs. Statistical data may also be used in order to test theories. Nevertheless, this type of data research may be or may sound difficult to conduct due to its complexity; however one of its advantages is that it is structured and easy to generalize.

Qualitative data, on the other hand, is “unlike the quantitative data analysis clear-cut rules about how qualitative data analysis should be carried out have not been developed”. This type of data may be gathered through interviews, participant observation or secondary data sources. However, it may be even more difficult to collect and analyze qualitative data than quantitative data. Qualitative data may also be used in order to give further information to numerical methods. So, each type of data is complementary to the other.

3.2 Criticism of Sources

3.2.1 Criticism of Primary Sources

The problem with the primary sources is that it is hard to know if the information is true or not. For instance, when we conducted our interview with the Marketing Director of the LFV group, he gave us general and more specific knowledge about the low-cost market. As Mr. Lundvall does not work in the airline low-cost industry, he could have given us wrong information. It was our duty to check after the meeting the accuracy of his speech. By definition, a primary source is a source that has never been studied before and consequently nobody has checked it.

3.2.2 Criticism of Other Sources

We saw previously that the other sources of information are easy to find, nevertheless there are still limitations you would better be aware of when you use secondary sources. First of all, it is not easy to find information that they are well-known for you. We mean that you have to understand

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63 Ibid, p.69-70
64 Ibid, p.25
65 Ibid, p.424
66 Ibid
properly the data you have collected in term of time of adaptation to analyze them or in term of scientific vocabulary employed. Second of all, the secondary data you have collected could be complex and difficult to break down especially when the data are huge with large numbers; once again you may need time to feel comfortable with them. Third of all, you are not always sure of the quality of the data; you have no control on them. They could be biased or totally wrong and it is hard to see the true and false, you cannot control the reliability and validity for instance.

We tried also to find original secondary sources from authors and not only some quotations in the work of other authors.

Moreover, the disadvantages of the data gathered from official statistics are that they have been collected for another topic than ours. We mean that sometimes they do not really fit our thesis. “The idea is to take our research problem as the starting point for secondary data we need, and not the other way around.”

In addition to all the drawbacks above, secondary data rapidly become obsolete because we live in a world where the environment is constantly evolving and information gathered yesterday will not be true tomorrow.

3.3 The Interviews

Upstream an interview, it is really essential to prepare appropriately the questions you want to ask to the interviewee in order to get the empirical results that will help you to confirm or falsify your hypothesis; that is the reason why it is important to respect the following process.

We gathered information from professionals in the airline industry and more specifically in Scandinavia. That is the reason why we have decided to conduct interviews. We interviewed not only professionals working in airlines but also in airports in order to have a wider overview of this industry.

3.3.1 Creating the Interview Guides

An interview guide is like a list of words or sentences that help you to cover a semi-structured interview. So, we have constructed three different interview guides, we did the first one for the Marketing Director of LFV, the second and third one were for the airline companies. It was really imperative that the interview guide fits the interviewee; we asked specific questions for the LFV group (State-owned civil aviation airports) but also for the airline companies. Moreover, the structure of the questions had to be simple and easy to understand, additionally it should not lead the interviewee to answer in a certain manner; he must not be influenced. The guides were here to get the maximum feedback as possible (points of view, ideas, opinions, thoughts, critics…).

The goal of the interview is to bring out new and relevant information that will help you to investigate toward your topic. Once again, interview guides took us a couple of hours to formulate and reformulate the questions to be simple and without bias or leading questions.

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69 Ibid, p.349
Chapter 3 Practical Method

The questions were constructed like a ‘funnel’: we started with very general questions, then during the interview we asked more specific questions and we finished by asking how the interviewee saw the future for the airline industry. The more time was passing by, the bigger flow of information the interviewees gave us. You can find our interview guides in Appendixes 2 to 4 in the end of this thesis.

While we were creating our questions, we try to formulate as much as open questions as possible with specific key words in order to get broad answers. We aim to get a maximum numbers of answers which would help to answer our research question.

In the purpose to make the interviewee confident and talkative, we sent them the interview guide a couple of days before the meeting, so they had time to prepare the discussion and they knew that you will not going to ask ‘embarrassing’ questions.

Hereunder, you can have a look at how you should act when you formulate the questions for your interview guide.

![Figure 3 – Formulating Questions for an Interview](image)

### 3.3.2 Performing the Interviews

As we are doing a qualitative research, the type of interview we chose was the semi-structured interview. It is less demanding than the structured interview for a quantitative research: “There is an emphasis on greater generality in the formulation of initial research ideas and on interviewees’ own perspectives.”

If during the interview new questions popped up, we had the ‘latitude’ to ask new ones and fit better the interview. The interview guide was used mostly as a support. Moreover, we did not have to take care about the time. For instance, we knew that the first interviewee had time for us, so we did not respect a specific schedule for each question. It probably enabled the interviews to be more fluent.

The advantages of a semi-structured interview are that on one hand it brings structure but on the other hand the interview in more flexible and easy to conduct. We never restricted the answer that we got. It was possible to talk freely. Another advantage was that we still had the possibility to ask the interviewee after the meeting in case of we had forgotten to talk about a topic.

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71 Ibid, p.341
Before each interview, we searched information about the interviewee, such as his position in the company and about the airline he is working for because this information is useful to understand the answers\(^{72}\).

The first interview, after approval of the interviewee, was tape-recorded to be sure that we had the interview as a whole and on his own terms, then we did a transcription on the software Word. We took care that the microphone was situated at an equal distant between them and us to have the best quality and to be audible.

Unfortunately, we had to conduct the two other interviews by mail because of specific demand from the interviewees. Normally when you are doing a qualitative research, interviews could be of higher quality if they are conducted face-to-face. Nevertheless there are two other possibilities. The first one is telephone interviewing; it is particularly useful because the cost of telephone is much cheaper than traveling, the other one is email interviewing\(^{73}\). Online communication, such as emails, has advantages but also drawbacks. It is the cheapest way to communicate and it is not time consuming, you can reach a larger number of employees inside the company, you can contact easily people around the world and data collection are very quick. Nevertheless there are also drawbacks; still today there are people who do not have internet connection yet, interviews by email could be regarded as spam and could be deleted without being read, when you are conducting the interview you are not in front of the interviewee, so you could lose visual or oral gestures that you could not see and finally, the interviewee might be afraid of the identity of the interviewer and could be reluctant to give confidential information\(^{74}\).

→ Interview 1 (Appendix 2)

Concerning our first interview that we have conducted March 30\(^{th}\) 2007 from 9.50 to 11.55am, with the Marketing Director of the LFV Group (Mr. Dan Lundvall), we took contact with the manager director of the airport of Umeå (Madam Karin Larsson-Tängdén; Flygplatschef) to explain her the situation and ask her if we could book a meeting room at the airport. When you conduct an interview, it is really important to be in a quiet and private room. There must not be background noise disturbing the process\(^{75}\). Ms. Larsson- Tängdén proposed us to book the VIP Room of the airport. How could we say no to such a nice proposition? This interview lasted approximately two hours. The quality of this interview was quite high. He gave us some specific terms and vocabulary about the airline industry and LCC. However, what we did not know is that Mr. Lundvall came only for our interview in Umeå and flew back to Stockholm right away we had finished it.

→ Interview 2 (Appendix 3)

We have conducted the second interview with Mr. Mats Valinger, Vice President Corporate Development from the SAS Group. He is in charge of the strategic development and organizational issues for the whole SAS Group. Unfortunately, we could not organized a face-to-face interview with him at SAS headquarters because he was really busy during the period we wanted to interview him and especially because the SAS Group is currently experiencing deep changes and major revisions of their strategies\(^{76}\). So, we agreed to organize the interview by email. Like for the first

\(^{73}\) Ibid, p.350
\(^{74}\) Ibid, p.498
\(^{75}\) Ibid, p.348
\(^{76}\) Interview with Mr. Mats Valinger, Vice President Corporate Development from the SAS Group
one, we created an interview guide that we sent to him on April 13\textsuperscript{th}. We had answers on most of the questions we asked him the April 20\textsuperscript{th}, nevertheless he proposed us to take contact with another manager from SAS, but we never had reply from him.

\begin{itemize}
\item \textbf{Interview 3} (Appendix 4)
\end{itemize}

We have conducted the third interview with Mr. Kjell Wilsberg, Director Government relations from SAS Braathens (Norway). Unfortunately, we could not have organized either a face-to-face interview with him at SAS Braathens headquarters in Norway because of lack of time and because he told us that he prefers to conduct the interview by email rather than by phone: “I would prefer to contribute by email; May and June are busy months”. Like SAS Airline, SAS Braathens is currently experiencing deep changes and major revisions of their strategies\textsuperscript{77}. We created a specific interview guide for SAS Braathens that we sent him on May 11\textsuperscript{th}. Mr. Wilsberg answered on May 18\textsuperscript{th} all our questions we asked.

\subsection*{3.3.3 Processing and Analyzing the Interviews}

As we said previously, once we had finished the interview, we started making transcription of them. For the first interview, tape-recording was really helpful because you did not have to be concentrated on writing word by word what he said\textsuperscript{78}.

To transcript the interview, we proceed like this. Firstly, we carefully listened to a part of the tape to see if the recording was good, then we turned each sentences they said into words. After that we listened once again the sentence to check if what we wrote was the exact sentence and finally at the end, we listened once again to the tape as a whole to be sure that the complete transcription was done.

Transcription of an interview is really long and you have to be well concentrate not to miss a single word. The first interview took us one day and fifteen pages on Word for the transcription.

Concerning the two other interviews, we did not have to transcript them; however we analyzed them scrupulously like the first one.

\footnote{\textsuperscript{77} Interview with Mr. Kjell Wilsberg, Director Government relations from SAS Braathens}

Chapter 4 The Airline Industry and Theoretical Framework

Chapter four will present the institutions and regulation within the airline industry. Then, we will make an analysis on the context and on the industry thanks to the PESTEL framework, we will see if there are new entrepreneurial opportunities and changes in the environment. Afterwards, we will analyze how entrepreneurship and innovation can be applied to the airline industry. Finally, competitive strategies will be explained.

Within this theoretical framework, Figure 5 provides an elucidative scheme on the development of this theoretical part. We will start from a broad macroeconomic perspective towards a microeconomic one.

In the first part we start explaining the role of institutions in economy, how they change and how they affect organizations and entrepreneurs through their constraints. Then we will give examples of these constraints – two different theories of regulation.

In the second part we will start analyzing the macro-environment of the company, that is, the context where it operates. We will start by with theories concerning macro-environment context such as environmental jolts and the PESTEL framework, then we will move towards a more microeconomic level and will analyze the industry through Porter’s concepts of Five Forces Framework. Then we will explain how these changes that occur outside the organization can influence entrepreneurship, focusing in the specific event of deregulation. This last part makes the transition to the next one.

After explaining the connection between entrepreneurial behavior and change in the last chapter, we will move towards a deeper explanation of entrepreneurship. We will present basic entrepreneurship concepts from Schumpeter and then make the link between them and the concept of innovation explained by Drucker. At the end we will make the link with the first chapter, explaining the concept of corporate entrepreneurship and institutional entrepreneurship, which tells us how entrepreneurs can change the rules of the game.

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Chapter 4  The Airline Industry and Theoretical Framework

The last chapter is dedicated to microeconomic strategies, that is, the strategies of an organization. We will focus in Porter’s definition of strategies and examples of competitive strategies – cost leadership and differentiation – and explain how a firm attains sustainable competitive advantage.

To illustrate the path we will follow, we created the following theoretical framework:

![Theoretical Framework](image)

To prove that all the chosen theories are relevant for our topic, after presenting each one we will provide an example on how it can be applied to the airline industry. Thus we will make clear what this theoretical framework of reference is going to be used for. Despite of the theories we used in our work, we could have used others that we will present now.

4.1 Previous research

There are other theories and concepts we could have used to explain and describe our research area. Previous research analysing the effects of airline deregulation often uses economic theories and models, using statistical methods. For instance, Morrison and Winston studied the economic effects of airline deregulation in USA context using econometric and statistical procedures such as maximization, economic efficiency, sampling, standard deviation, deflators to predict revenues, fares and welfares to a hypothetic regulated context after 1978 and to calculate the efficiency and distributional effects of deregulation, social optimum, and maximization of travellers’ welfare. Similar theories are used by Seristö in his study concerning airline performance and costs where he makes an analysis of performance measurement, efficiency and cost reduction in major airlines and applies it to the specific case study of Finnair; in Franke’s context and industry analysis, entrepreneurship and innovation, strategic position, institutions and regulation, environmental jolts, 5 forces framework, PESTEL, public interest, entrepreneurship theory, economic theory of regulation, institutional theory, entrepreneurship, innovation, institutional entrepreneurship, corporate entrepreneurship, strategic position, swot, competitive strategies.

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Chapter 4                      The Airline Industry and Theoretical Framework

study regarding level of efficiency of airline in the deregulated context\textsuperscript{82}; and in Barbot’s economic assessment of state aid to Ryanair where she presents a economic model to discover the effects of state aid in competition\textsuperscript{83}.

Economic concepts are applied to airline industry in a series of studies. For instance, references to economies of scale, of density, of stage length and law of diminishing returns are used in several works that we used concerning airlines strategies such as the studies from Weber and Dinwoodie\textsuperscript{84}, Melville\textsuperscript{85}, Starkie\textsuperscript{86}, Gillen and Morrison\textsuperscript{87}, Barrett\textsuperscript{88}, Fridstrøm et al\textsuperscript{89}, Dobruszkes\textsuperscript{90} and Holloway\textsuperscript{91}. However for our study, we did not include them in the main theoretical framework for three reasons: first, our background is businesses and so our studies are focused on this area and not economics, which presented a restriction to use these concepts; second, we found these concepts and theories were outside the main theoretical framework, so we barely use them to complement the main theories, specially concerning strategic framework; third, we wanted to collect our data in qualitative methods, thus econometric and statistical calculations were not appropriate and could compromise the deadline to deliver our thesis. Some of these concepts are presented in the list of definitions, chapter 1.5.

Despite of all economic theories involving econometric and statistical models there are also other previous studies that include at least two of the main. For instance Sinha’s\textsuperscript{92} and Button’s\textsuperscript{93} books concerning airline deregulation in various parts of the world make reference to market regulation theories such as the economic theory of regulation and public interest theory, the same we used when talking about deregulation in airline industry. However these books are more focused in providing a link between these historical facts and the effects on competition (which we also refer in our theoretical framework when talking about the five forces framework and environmental jolts).

Seristö in another study also relates deregulation in Europe with their strategic position, focusing in competitive strategies as cost leading and differentiation. He also makes a comparison between competition in the European regulated environment and competition deregulated environment, presenting the main trends in the new context\textsuperscript{94}. This study has some similarities with our, since we also make a comparison between the two environments and the different strategies SAS and Ryanair followed. We also used the same theories regarding strategic position – cost

\textsuperscript{86} Starkie, D. (2002) \textit{Airport Regulation and Competition}, Journal of Air Transport Management, 8, pp. 63-72
\textsuperscript{89} Fridstrøm, L. et al, \textit{Towards a More Vigorous Competition Policy in Relation to the Aviation Market}, Journal of Air Transport Management, 10, pp. 71-79
\textsuperscript{90} Dobruszkes, F. (2006) \textit{An Analysis of European Low-Cost Airlines and Their Networks}, Journal of Transport Geography 14, pp. 249-264
\textsuperscript{91} Holloway, S. (1997) \textit{Straight and Level – Practical Airline Economics}, Ashgate
leadership and differentiation (presented by Porter). Other authors like Melville, Weber and Dinwoodie, Barrett, Driver, Glisson et al., Gillen and Morrison, and Franke also present a cause-effect relation between deregulation and new airline strategies. One of the studies of Barrett is looks at these effects in the Irish market, presenting a case study of Cityjet. This last work somehow resembles our case study from Ryanair, however with an emphasis in microeconomic features, looking more inwards the firm and not focusing in entrepreneurship and innovation. But Barrett also presents a case study of Ryanair, connecting it to the deregulated European aviation market. This study served as a complement for other specific sources about Ryanair we obtained.

Regarding the link between institutional theory and regulation in the airline industry, few studies are available. We could only found two works of Richards with respect two this relation, both in the context of international aviation markets and explaining how states built an institutional design in international institutions and how they could influence it to capture benefits for their airlines. Regarding this last issue that can be considered behaviour of institutional entrepreneurship, other authors refer this regulatory capture in the European airline industry like Sinha and Button, and others like Barrett give specific examples of European carriers that achieved this benefit. In our thesis we also present a relation between change in the institutional design by Ryanair and the regulatory capture by SAS.

Studies regarding two other key words of our problem statement – entrepreneurship and innovation are less available. A recent study from Franke focus in innovation in the new deregulated environment (although world-wide), presenting this as a decisive driver of progress for the legacy carriers and as a key weapon to face competition nowadays. Regarding entrepreneurship, we could only find two study that relates deregulation in airline industry with entrepreneurship, although both in the USA context. The first work we found was made by Meyer and Oster, and presents the differences in context between the regulated and the deregulated period, entrepreneurial opportunities that were created, strategies in various fields, public policy issues (including airports and small regions policies). It also uses Schumpeter theories in the field of

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entrepreneurship\textsuperscript{110}. This was the most similar work we found similar to ours. Although, contrary to our thesis, this study focus on the opportunities created for various actors – airlines, airports, governments - and not only for airlines like we did. The work of Bilstein\textsuperscript{111} describes the story of deregulation in USA, focusing in different agents like Meyer and Oster, and presenting the main differences in many fields such as finances, labour productivity, marketing and new strategies. However entrepreneurial theories are not present, in contrast to Meyer and Oster work.

As we could see there are several studies in the airline industry that refer at least two of the key words of our work (based on the theory we chose). We have deregulation-economic concepts, deregulation-new strategies (which is the most common pair), institutions-institutional entrepreneurship, deregulation-innovation, deregulation-entrepreneurship. Taking this into account and the key words of our study (based on the theory we chose) there are some theoretical gaps. The link deregulation-institutions-entrepreneurship-innovation can not be found in the academic work in any geographic and time context. Thus, the theories we chose for our study help us to achieve the exploratory objective we set before in chapter 1.3. That is, our thesis would fill a gap in existing literature.

\textbf{4.2 Institutions and Regulation}

\begin{quote}
“Deregulation is a world that appears offensive to most national airlines. Nevertheless, in the long term deregulation combined with competition is the only method by which the traveling public will enjoy low fares.”

By Michael O’Leary in “Ryanair – How a Small Irish Airline Conquered Europe” by Siobhán Creaton
\end{quote}

Since our topic concerns regulation and deregulation, we thought that would be important to clarify some of the basic aspects. What is the role of institutions? Why is an industry regulated? What were the reasons behind a strict regulatory regime like the one who governed the airline industry? Does regulation bring any benefits? What are the objectives of a regulation? Within this topic we will start with a presentation of institutional theory and then we will present the two main theories of regulation. Then we will show and justify how it was applied to the airline industry.

\textbf{4.2.1 Institutions}

\begin{quote}
“Institutional change plays an important role in the generation of opportunities for entrepreneurial activity.”

By Wesley D. Sine and Robert J. David in “Environmental Jolts, Institutional Change, and the Creation of Entrepreneurial Opportunity in the US Electric Power Industry”
\end{quote}

First we will present the definition of institutions according to Scott: “Institutions consist of cognitive, normative, and regulative structures and activities that provide stability and meaning to social behavior. Institutions are transported by various carriers – cultures, structures, and routines – and they operate at multiple levels of jurisdiction”\textsuperscript{112}. In turn, institutions can be view through three different perspectives: regulative, cognitive and normative. The regulative approach is most adopted by economists and the cognitive is more famous among sociologists and anthropologists\textsuperscript{113}. However, in our study we will only use the regulative and cognitive approach since nowadays there


\textsuperscript{113} Ibid, p. 35-45
are the main used perspectives (special the cognitive perspective that sometimes is regarded as “the institutional theory”) and thus the majority of studies concerning institutionalism concern these two approaches and not the normative one.

According Douglas North, a supporter of the regulative perspective of institutions, institutions are developed constraints that influence human interactions. North argues they interact with organizations correcting their models of action (in which they act with incomplete information), so they can reduce transaction costs and achieve efficient economic markets that are typically imperfect and beset by high transaction costs. To do that, they possess three tools: formal constraints, informal constraints and enforcement characteristics. It is this interaction between institutions and organizations that steers the way institutions change in an economy. Institutions are thus like the rules of the game and organizations and entrepreneurs are the players.¹¹⁴

Most of institutionalists nowadays like Meyer, Di Maggio, Powell and Berger adopt a cognitive perspective, focusing in the cognitive elements of institutions: rules that form reality and frames through which meaning is made.¹¹⁵ This perspective argues that as institutions are highly resistant to change, the behavior of organizations is characterized by the “taken-for-granted” of their reality (where exist institutions that impose constraints) and not by strategies to maximize their performance.¹¹⁶ This taken-for-granted is related with the fact that organizations force their structures and activities to be isomorphic with patterns in their environment.¹¹⁷ Meyer and Rowan present two explanations for the isomorphism that results from organizational environment: one is that organizations “become matched with their environments by technical and exchange environments”, other is that organizations structurally reflect the socially constructed reality where they operate and are conditioned by institutional environment.¹¹⁸ In turn, this isomorphism implies routinized structures and behaviors that constraint actors strategies¹¹⁹ and, as economic theory assumes, actors are faced by such constraints when they try to reach optimal decisions.¹²⁰ This isomorphism has consequences for the organizations, such as disregarding efficiency in order to incorporate elements that are legitimated externally and dependence on these institutions that provides stability. Stability in market conditions, inputs, outputs, technology are assured within institutional enforcement power. These institutionally controlled environments cushion organizations from turbulence and the taken-for-granted institutional rules assure a low degree of instability in markets, products, technology and so on.¹²¹ However, by adhering to these formal structures, institutions are given legitimization and they use them to secure its survival and assure a success in the environment.¹²²

The question of isomorphism, taken-for-granted rules and stability is especially visible in public utilities organizations such as airlines. In Europe, flag carriers operated within the taken-for-granted rules of their domestic and European markets, and governments provided institutions that assured stability in the environment. For instance, even after deregulation, institutions cushioned the

Chapter 4 The Airline Industry and Theoretical Framework

effects of September 11th (that is, provided stability), providing airlines with money and saving them from bankruptcy.\textsuperscript{123}

Although even in strictly institutionalized environments changes can occur by actors that are shaped by institutional structures - this is an argument that in the last years has been challenging the institutional theory\textsuperscript{124}. Neo-institutional theories say these change can occur from environmental jolts, which are simply changes in environment\textsuperscript{125}. In turn, these environmental jolts (changes in environment) often lead to processes of deinstitutionalization that occur because since institutional rules are not coherent and present conflicts and contradictions with each other (when there are competing institutional frameworks), institutions fail in providing a scheme about the way the actors should act within their environment\textsuperscript{126}. Therefore, institutional change arises from organization’s environmental pressures\textsuperscript{127}. These changes are important as Sine and David argue, “Institutional change plays an important role in the generation of opportunities for entrepreneurial activity”\textsuperscript{128}.

Despite of the propensity for an institution to change, its actors (that operate under an institutional design governing a certain industry) have to these rules. A state or governmental or intergovernmental institutions are the main actors who have the power to create the regulatory framework firms have to follow if they want to stay in the industry. Therefore, disregarding the resources a firm possessed or their success in the market or the industry where it is in, a state through the introduction or cleansing of regulation, has the power to benefit or to warm a firm or industry\textsuperscript{129}. Concerning the way the state or a superior authority intervenes in an industry, Sinha distinguishes two distinct theories of regulation: the economic theory of regulation (sometimes called “capture theory”) and the public interest theory\textsuperscript{130}.

4.2.2 Economic Theory of Regulation

The first theory incorporates political issues and behavior within the regulation of an industry and for that reason argues that the benefits from regulation are only taking by a small group (with similar political and economic interests as the government) and not by the whole society\textsuperscript{131}. This small group usually is the monopolistic firm that dominates the industry or the two big firms that operate in a duopoly market. Despite of the fact that the rules of the game can be offered by the government (if the firms are seeking beneficial rules) or be forced to be accepted by the government (if the government is seeking to maximize their own specific interests), Stigler conceptualization of this theory is focused upon the fact that "regulation is acquired by the industry and is designed and operated primarily for its benefit"\textsuperscript{132}. These benefits can have four different categories: direct subsidy of money, control over entry by new rivals (barriers to entry), policies

\textsuperscript{127} Ibid

31
affecting substitutes and complements, and price-fixing\textsuperscript{133}. Within this positive theory, there is a strong link between the benefited groups and the legislators and politicians, as they contribute to each other providing financial support, votes and adequate rules of the game for their own interests. Thus both groups seek to maximize their own utility\textsuperscript{134}.

The airline industry in Europe and in USA are examples where the regulation brought benefits only for a small group (the flag carriers of each member state) while harming a bigger group (the consumers and the entrepreneurs). We will present some examples of benefits for the airlines: regarding subsidies, in Europe flag carriers received money whether they were facing financial difficulties\textsuperscript{135} and in US air mail subsidies were given to domestic airlines in 1968\textsuperscript{136}; the control over entry by new rivals in Europe was done by restraining multiple designation routes (routes where more than one carrier per country is flying) between European countries\textsuperscript{137}, while in US the Civil Aeronautics Board (CAB) excluded entry of almost one hundred petition for new routes\textsuperscript{138}; the policies affecting substitutes and complements is witnessed in this industry through the active support of governmental subsidies to airports\textsuperscript{139}; finally the price-fixing was dictated by IATA fare conferences which hindered airlines to freely set their own fares\textsuperscript{140} (although one can say that this price-fixing was not a benefit for the airlines, due to the revenue pooling that was also present in IATA fare conferences small airlines could make profits that otherwise could not make when competing with a big airline). The introduction of rules that provide these kinds of benefits were sometimes forced by the monopolistic firm of the industry itself through lobbying the Government – Aer Lingus is an example of an airline who could achieve regulatory capture of the Irish department of transport and thus maintain potential competitors out of its way\textsuperscript{141}. Seristö argument to justify this as its base on the assumption that regulation of the industry was sought by the flag carriers as free competition could have devastating consequences for the industry and could result in several bankruptcies\textsuperscript{142}. Summing up, the main reason for regulating air transportation market was to protect national airlines\textsuperscript{143}.

Giving benefits to the airlines also brings benefits to the state itself – as we saw before, the maximization of utility is the main aim both for the state and for the industry. When regulating the industry and giving a favorable environment for the flag carrier, the State could use the flag carrier as an ambassador of the country and as a symbol of national prestige and pride\textsuperscript{144}. The flag carrier was also an instrument for the State to ensure its presence and power in the colonies, taking advantage of its colonialism, like happened with Air France or British Airways in their early days


\textsuperscript{138} Ibid, p. 6


32
(despite of the fact that many of those routes were not profitable at all)\textsuperscript{145}. Therefore, within the airline industry, the regulation in European, American and international markets brought benefits for a small group of firms (the flag carriers in Europe and the biggest carriers in US) and for the governments, and harmed other groups of society such as small airlines from small countries (Melville shows in his study of the national airline of Trinidad and Tobago that under a restrictive regulatory regime there is little opportunity for a small airline to have any market power\textsuperscript{146}), which goes in line with the economic theory of regulation.

### 4.2.3 Public Interest Theory

The public interest theory argues that the aim of regulation is to correct the market failures, adjusting the distributional effects that arise from market power (such as natural monopolies that most of the times do not conduct to economic efficiency and creates barriers to entry), asymmetric information (from the consumer’s and from the regulator’s point of view) and externalities (like pollution, noise or congestion)\textsuperscript{147}. Trembling built an Institutionalist model of the public interest theory and his model is based upon five major postulates: 1) government intervention (through regulation) is justified to correct malfunctions of market like concentrations of power, increasing uncertainty, performance failures and adverse distributional effects, that markets can not correct by themselves; 2) regulation is used to promote public interests that can not be promoted by market-oriented measures, in other words, this intervention is necessary to solve the dichotomy between public and private goals; 3) proper regulation is able to promote higher levels of efficiency and greater individual choice, thus Government intervention is needed to allocate resources in a way that is more consistent with public interest objectives; 4) the success of regulation in promoting public interest goals is dependent on a public consensus regarding the need for action and political support for the regulator; 5) regulation goes through changes over time as the regulatory process is evolutionary (because market forces are determined by the development cycle of the industry)\textsuperscript{148}. However, even if the Government intentions seem to be the best ones, this kind of regulation introduces distortions in the market and creates a trade-off to be made between imperfect competition and imperfect regulation. As this balance changes over time, economic regulation should be examined regularly\textsuperscript{149}.

The public interest theory deals with public utilities\textsuperscript{150} and in the transportation sector was used by many authors to explain the reasons behind the strict regulatory regime in airline industry. Sinha uses this theory to justify the rationale behind the regulated airline industry in US – the American government favored a strict regulated industry to ensure an adequate service and safety in air transportation, thus promoting the public interest\textsuperscript{151}. Burton arguments follow Sinha’s and add that public interest consideration was the main logic in the strict regulation that most countries adopted to regulate main domestic transportation during the Second World War – some examples of this fact are the Civil Aeronautics Act in USA in 1938, the Air Navigation Act in Australia in 1920, the Trans Canadian Airlines Act in 1937 and the Civil Aviation Act in UK in 1946\textsuperscript{152}.

\textsuperscript{149} Starkie, D. (2002) *Airport Regulation and Competition*, Journal of Air Transport Management, 8, p. 63
\textsuperscript{151} Ibid, p. 47
In Europe the same policy was followed. Despite of the fact that the flag carriers argued that the monopolistic situation of the market brought lower fares,\textsuperscript{153}, the real situation was pretty different. The following table made by Barrett compares the benefits perceived by Aer Lingus as a result of the national airline policy in Ireland (that favored the flag carrier) and the actual results of each benefit:

<table>
<thead>
<tr>
<th>Benefits Sought</th>
<th>Results</th>
</tr>
</thead>
<tbody>
<tr>
<td>A national airline</td>
<td>Ban on new entrants</td>
</tr>
<tr>
<td>Serving the national interest</td>
<td>Serving the national airline interest</td>
</tr>
<tr>
<td>National pride</td>
<td>Excess access costs</td>
</tr>
<tr>
<td>Irish representation abroad</td>
<td>Very high fares for emigrants returning for short notice reasons and emergencies</td>
</tr>
<tr>
<td>Tourism promotion</td>
<td>Tourism restricted by high access fares and controlled capacity</td>
</tr>
<tr>
<td>Employment</td>
<td>A low productivity airline</td>
</tr>
<tr>
<td>Foreign exchange</td>
<td>Reduced tourism due to high access costs</td>
</tr>
<tr>
<td>11-26% social return</td>
<td>Negative impact on economy due to high access costs and loss of national competitiveness</td>
</tr>
<tr>
<td>An efficient monopoly</td>
<td>Excess costs and fares compared to the denied market alternative</td>
</tr>
</tbody>
</table>

Table 1 - The benefits sought and actual result of the national policy in Ireland\textsuperscript{154}

This example shows how the rules implemented by Government with the best intentions for its country (promoting tourism, give employment, bring welfare, etc) result in the opposite effect of the desired one. More examples of negative effects that arose with the regulation are given by Barrett in another study that shows how public dissatisfaction with the high fares on the Dublin-London route led to a negative growth of air travel between Ireland and UK in the five years prior to the deregulation. Furthermore, those air routes are characterized by having high fare growth, high costs for the flag carrier and low productivity.\textsuperscript{155} In US the situation was similar. Button shows that CAB fare setting policies led to a rise of 53% in the average fares paid by the consumers during 1967 and 1977.\textsuperscript{156} Other studies show that effects of the regulation in the industry did not contribute to achieve the objective of maximizing the public welfare: Jordan concluded that the regulation did not protect the consumer while Douglas and Miller argued that airline fares were inefficient regarding price-quality combinations and its cost minimization to the consumer. Furthermore, they found that inefficient carriers took advantage of entry barriers (as it hindered competition and protected the old carriers) and that the labor cost were higher due to regulation.\textsuperscript{157}

\textsuperscript{154} Ibid
4.3 Context and Industry Analysis

In this second theoretical chapter we provide explanations on types of changes in environment (sometimes known as environmental jolts) and explain how organizations, and more specifically entrepreneurs, can take advantage of them. We will start with the PESTEL framework to show how different factors that lie outside the company may affect the latter. Then we will show how a change in these factors has an impact on institutions, organization and entrepreneurs. We will also see when such alterations occur entrepreneurs are given opportunities to act. At the end we will present Porter’s Five Forces Framework, a model used to analyze competition and attractiveness in an industry.

4.3.1 The Pestel Framework

The main objective of the PESTEL framework is to identify and analyze the environment surrounding the company. We can categorize and identify six different types of factors: political, economical, sociocultural, technological, environmental and legal\textsuperscript{158}.

These six factors can considerably affect and influence the strategies of a company. Moreover, there are not independent but rather interdependent; many of them are linked. For instance the increasing number of technological factors, such as the arrival of 100\% automation, may influence the economic factor and more specifically the rate of unemployed people.

If only one factors changes positively or negatively, it changes the whole competitive environment of organizations. That is the reason why it is primary to monitor it and to set an ‘environmental intelligence’ in order to react rapidly in case of modification to keep your competitive advantage on your competitors. As we will explain later in this chapter, entrepreneurs have to identify the key drivers of change which are the forces which affect the structure of an industry, a sector or a market\textsuperscript{159}.

\textsuperscript{159}Ibid, p. 69
4.3.2 Changes in the Environment and Entrepreneurial Opportunities

"People do not make decisions to exploit entrepreneurial opportunities in a vacuum, but instead are influenced by the context in which they operate."

By Scott Shane, in “A General Theory of Entrepreneurship”

Environmental pressures are often called environmental jolts, which Meyer defines as “Transient perturbations whose occurrences are difficult to foresee and whose impacts on organizations are disruptive and potentially inimical”. Environmental jolts can assume various forms, depending on their source. According to Shane, changes in the environmental context can take three different forms – they can be technological, political-regulatory and social-demographic. Despite of their source, the outcomes are often the same – the entry of new players, ascendance of existing players, change of intellectual climate, disturbance of current logics and enablement of possibilities to change. These possibilities of change constitute sources of Schumpeterian opportunities (entrepreneurial opportunities). This concept will explain in the next chapter.

Meyer argues that organizations face a process of adaptation to jolts that involves three phases: an anticipatory phase when actors can foresee the jolt, a responsive phase when the first jolt effects hit the organizations and a readjustment phase after the shocks had gone. The second and third phases are characterized by a re-examination of institutionalized logics and practices and a reorientation of organizational strategies and process with environmental demands, respectively. Schumpeter presents two main different reactions to changes in environment: the adaptive response takes part when an economy or a sector of the economy reacts to a change in its data and the

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160 Ibid, p. 68
creative response; the creative response is a behavior that is distinct from the typical range of practice that is normal within an industry. In turn, creative response has three characteristics: impossible to be predicted taking into account past and present facts, it has consequences for next events and their long-run outcome, is related with quality of personnel within the society, with their relative quality and with individual decisions, actions and behavior\textsuperscript{166}.

These last arguments regarding reaction to changes in environment are in line with Shane theories that relate environment change to entrepreneurship. Shane states “People do not make decisions to exploit entrepreneurial opportunities in a vacuum, but instead are influenced by the context in which they operate”\textsuperscript{167}. For our thesis, the relevant effect of the institutional environment on opportunity exploitation is the centralization of power. This centralization of power can be defined as “the degree to which one political actor coordinates the economic, political and social activity in a society”\textsuperscript{168}. Shane argues that decentralization provides better conditions for entrepreneurial activity. This since all the information of a market system is scattered through different economic actors, a central actor that attempts to make all decisions is not able to make better decisions for it will lack information to make efficient decisions and thus it will decrease the level for opportunity exploitation. Within our thesis we will consider the centralization of transport legislation within the EU area.

Since our thesis is focused on the regulatory changes within a specific context where transport regulation was centralized (Europe), we will now give an explanation and arguments on how it influences entrepreneurship. After a regulatory change in a certain context, more productive combinations of means of production are possible to be carried out by the entrepreneurs (this concept will be present next chapter). That is, there are new opportunities for entrepreneurs since it creates an environment for productive entrepreneurship. Shane illustrates some examples of how deregulation of utility industries in US created opportunities for entrepreneurs and argues that regulation limit the free use of all means of production which hinder firms to use the resources in a productive way in order to produce innovation\textsuperscript{169}. The same happened in the airline industry in US (and also in Europe) when the status quo was challenged by the new firms that entered in the market and started operating with costs 30-40\% lower than the old carriers\textsuperscript{170}. This mean the old firms, due to regulation that was restraining competition, were not using the resources in a productive way or innovating enough. With the change in the regulatory environment, these entrepreneurs could use the existent resources in a more productive way and this made possible to have an introduction of a new service – the low cost flights, and a new method of production – the no-frills concept.

\subsection*{4.3.3 Structural analysis of an Industry}

We found that it would be mandatory to talk about competition within an industry and its competitive forces and explain how the deregulation affected them. Within the topic of structural analysis of an industry we picked Porter’s matrix of the Five Forces Framework. Understanding the structure of an industry is not only important to explain and analyze the behavior of organizations within it, but it also helps to understand the competitive rules of the game\textsuperscript{171}, which is an issue that will be important for our thesis.

\textsuperscript{168} Ibid, p. 156
Competition within an industry is related to performance, which in turn is related with innovations. According to Porter, competitive strategy (which we will give a definition in the next section) is related with the attractiveness of industries and the determinants of relative competitive position. More attractiveness does not imply a good competitive position and vice-versa. To analyze such concepts, Porter developed the Five Forces Framework that describes the attractiveness of an industry and their causes, as well as how the change of these five forces along a time period influence a firm’s competitive strategy. The five players in an industry and the respective forces associated with them are the potential entrants (threat of new entrants), the substitutes (threat of substitute products or services) the suppliers (bargaining power of suppliers), the buyers (bargaining power of buyers) and the industry competitors (rivalry among existing firms). These are the forces driving industry competition and they determine profit potential through their influence on prices, costs and investment. The following figure presents the relation between a firm and the players of an industry (and its associated forces):

![Five Competitive Forces Diagram]

In turn, the strength of each of these five competitive forces is a function of specific economic and technical characteristics of the industry. The determinants of each player are not specified in the figure above for they are too many to be included in it. However we will give some examples of these determinants for each player: economies of scale and government policy for new entrants, brand identity and product differences for buyers, switching costs and propensity to substitute for substitutes, switching costs and supplier concentration for suppliers, exit barriers and industry growth for industry competitors.

4.4 Entrepreneurship and Innovation

"The mechanisms of economic change in capitalist society pivot on entrepreneurial activity.”

By Joseph A. Schumpeter in “The Creative Response in Economic History”

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174 Ibid, pp. 7-29
Since our Master Program concerns entrepreneurship (and our thesis does so) we found indispensable to refer theories of entrepreneurship. For that reason, we picked theories from three authors we consider relevant to build a strong theoretical framework on entrepreneurship: Schumpeter, Drucker and Shane. The first one can be considered the most important author in the field of entrepreneurship and his work will be used to define and explain entrepreneurial behavior and to identify and explain the causes of economic development in the context of the airline industry. Drucker’s work linking innovation and entrepreneurship will help us to identify and justify the innovative behavior that was triggered in the post-deregulated period of European airline industry. Finally, the work of Shane will not only be used to describe and identify the Schumpeterian opportunities but also to explain the sources of those opportunities, in our case the change in regulatory context. Apart from the theories of these three main authors, we will present theories within the field of institutional entrepreneurship to explain the behavior of EU institutions and the role of airlines in its deregulation.

4.4.1 Entrepreneurship

“There must be an opportunity here, someone must be able to do better than this – offer low fares and maybe make money in the process.”

By Herb Kelleher, (founder and CEO of Southwest Airlines) in “No Frills – The Truth behind the Low Cost Revolution in the Skies”, by Simon Calder

We will start presenting entrepreneurship theories by using Schumpeter’s basic concepts of entrepreneur and entrepreneurial behavior. Using the words of the author, the entrepreneur is someone who “gets new things done”, a behavior that covers a vast amount of activities that can go from the simple activity of “setting up” or organizing, bending the hindering factors of the environment, leadership, salesmanship. However in the modern economic history, the entrepreneur has the role of “fixer”\(^\text{175}\). According to the author, “The carrying out of new combinations [of means of production and credit] we call ‘enterprise’; the individuals whose function it is to carry them out we call ‘entrepreneurs’”\(^\text{176}\). From here we should clarify some concepts: first, the “carrying out of new combinations” is nothing but the different allocation of supplies of productive means that already exist in a specific economic system; second, this employment of existing resources is the cause of development; third, development caused by the carrying out of new combination by the initiative of the entrepreneur can be due to five distinct cases:

- the introduction of a new good or of a new quality of a good,
- the introduction of a new method of production,
- the opening of a new market,
- the conquest of a new source of supply,
- the carrying out of the new organization of any industry\(^\text{177}\).

Taking into account this last concept of the causes of development, we will briefly present some examples that we can find in the European airline industry today and prove that Schumpeterian theories are relevant for our work:


\(^{177}\) Ibid, p. 63-74
Chapter 4  The Airline Industry and Theoretical Framework

<table>
<thead>
<tr>
<th>SCHUMPETER's combination of new means of production that cause development</th>
<th>Examples</th>
</tr>
</thead>
</table>
| The introduction of a new good or of a new quality of good or service | Services: Low cost flights
Goods: self check-in |
| The introduction of a new method of production | No frills concept |
| The opening of a new market | Regions served by small airports (new routes), first time flyers (for income reasons) |
| The conquest of a new source of supply | Entering in previous non-used regional airports or/and dominance of secondary airports |
| The carrying out of the new organization of an industry | Making alliances, breaking exclusive routes |

Table 2 – Application of Schumpeter combination of new means of production to the airline industry, authors’ creation

The economic development of capitalist societies it’s an evolutionary process. These changes are characterized for rising in a spontaneous way and for being discontinuous with the previous economic situation. Furthermore, they are responsible for disturbing and altering the previous economic equilibrium. Thus, this process of destroying the structure of the old economic system is considered by Schumpeter, a process of creative destruction. Within the airline industry in Europe, a process of creative destruction can be considered the fact that Ryanair introduced the low cost model in Europe (in spite of this fact, Skytrain was the first low cost that was created in Europe, making a transatlantic flight between UK and US, which leads authors like Button to have another opinion saying that “Ryanair […] is generally seen as the first no-frills European carrier” which changed the previous competitive environment and caused a disruption.

This behavior of creative destruction is triggered by changes in the environmental context where the entrepreneur works.

As we have already seen, changes in environment are important for entrepreneurs. These changes provide entrepreneurs with opportunities to combine resources in a different way and develop the organization or industry. Before developing the concept of Schumpeterian opportunities, we will develop the concept of entrepreneurial opportunities. Sarasvathy et al. ideas define entrepreneurial opportunity as “a set of ideas, beliefs and actions that enable the creation of future goods and services in the absence of current markets for them.” Thus, this notion includes innovation, beliefs and actions. In the same article, it is presented three different views of entrepreneurial opportunity: market as an allocative process (opportunity is recognized), market as a discovery process (opportunity is discovered), and market as a creative process (opportunity is created). Briefly describing, each view interprets opportunity in a different way, has a different focus, method, domain of application, assumptions, unit of competition and outcomes. These three approaches that can be integrated, because they are equally valid and they constitute three different ways of thinking about entrepreneurial opportunity. Furthermore, as they are context-dependent each view can be used separately under different contexts or situations.

Now we will give a brief explanation about Schumpeterian opportunities and their relation with entrepreneurial activity. According to Shane, Schumpeterian opportunities are characterized for causing disequilibrium, for requiring new information, for being innovative, for being rare and for involving creation. Now we will give examples how these opportunities can be found in the airline industry:

<table>
<thead>
<tr>
<th>Characteristic of Schumpeterian Opportunities</th>
<th>Example</th>
</tr>
</thead>
<tbody>
<tr>
<td>Disequilibrating</td>
<td>Ryanair reduction on ticket price was a consequence of deregulation that provoked a disequilibrium in the market</td>
</tr>
<tr>
<td>Requires new information</td>
<td>Changes in regulation provided new information for entrepreneurs</td>
</tr>
<tr>
<td>Very innovative</td>
<td>New generation of CRS for LCC will provide opportunities for airlines to improve their strategy</td>
</tr>
<tr>
<td>Rare</td>
<td>Until now there were only three packages of EU deregulation</td>
</tr>
</tbody>
</table>

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Chapter 4                      The Airline Industry and Theoretical Framework

Table 3 – Application of Schumpeterian opportunities to the airline industry, authors’ creation

So far, as we have seen, there is a special characteristic of entrepreneurship and its opportunities - doing something new, something that doesn’t exist, inventing. That is, innovation. Now we will explain the concept of innovation in the light of Drucker’s work.

4.4.2 – Innovation

"Innovation is the specific instrument of entrepreneurship.”

By Peter Drucker in “Innovation and Entrepreneurship”

The process of creative destruction and creative response that are characteristic of an entrepreneur is related with innovation\(^{201}\). For Drucker, “innovation is the specific instrument of entrepreneurship” and “innovation creates resource”\(^{202}\). Therefore, there is a strict relation between entrepreneurship and innovation. The concept of innovation can be broad. No matter what kind of innovation we may talk about, it is characterized for being systematic, in other words, an activity that is planned and organized by the entrepreneur. Sometimes it can be barely a different perception of certain existing products that leads the entrepreneur to use them in a different way (like the ship container). Also, innovation doesn’t need to be only technological – it can be also social (like the newspaper or the insurance). Innovation is something that changes the wealth-producing potential of resources that already exist\(^{203}\). Consequently, innovation implies a change, and it is change that provides opportunities for new and different products, services and resources. Putting everything together, “systematic innovation therefore consists in the purposeful and organized search for changes and in the systematic analysis of the opportunities such changes might offer for economic or social innovation”\(^{204}\). This systematic innovation is possible if one take advantage of the sources for innovation opportunity. According to Drucker these sources are:

- The unexpected (success or failure)
- The incongruity
- Innovation based on process needed
- Changes in industry structure or market structure
- Demographics
- Changes in perception mood and meaning
- New knowledge\(^{205}\)

The first four sources lie within the firm or industry, while the others lie outside the firm or industry. Every source except new knowledge exploit a change that has already occurred and satisfied a need that already exists, the last one innovation brings about the change and it aims at creating a want\(^{206}\).


\(^{203}\) Ibid, pp. 30-34

\(^{204}\) Ibid, p. 35

\(^{205}\) Ibid, pp. 30-35

\(^{206}\) Ibid, pp. 35-36
Now we will give examples of these sources in the airline industry in order to explain how Drucker theories apply and are relevant to our thesis:

<table>
<thead>
<tr>
<th>Source</th>
<th>Example</th>
</tr>
</thead>
<tbody>
<tr>
<td>The unexpected (success)</td>
<td>Ryanair success not expected by actors in the industry^207</td>
</tr>
<tr>
<td>The incongruity</td>
<td>Aer Lingus incongruity between perceived and actual customer values about air service^208</td>
</tr>
<tr>
<td>Innovation based on process needed</td>
<td>Low cost take advantage of economies of density^209</td>
</tr>
<tr>
<td>Changes in industry structure or market structure</td>
<td>Making alliances with other airlines^210</td>
</tr>
<tr>
<td>Demographics</td>
<td>Irish communities in Britain and Ryanair flights to UK^211</td>
</tr>
<tr>
<td>Changes in perception mood and learning</td>
<td>Ryanair change of perception about passenger’s values^212</td>
</tr>
<tr>
<td>New knowledge</td>
<td>New knowledge of LCC brought to Europe by Ryanair^213</td>
</tr>
</tbody>
</table>

Table 4 – Application of sources of innovation to the airline industry, authors’ creation

The sources we presented in the table above exist within a specific moment in time. The following graphic developed by Franke to study innovation within the airline industry illustrates how innovation adapts to changes in economy. For instance, in certain moments a firm can choose to innovate in the area of operations and costs and in others it can change to innovate on services and revenues. The focus on reducing costs and the focus on rising the service (and thus differentiating from its competitors) are presented by Porter as two ways to achieve competitive advantage. Strategic options theories will be further developed in chapter 4.5

^208 Ibid, p. 33
^213 Ibid, p. 77, 89-90
Whether a firm will focus on reducing its costs or on rising the quality of its service, according to Franke there are three main areas to potential innovation – advanced segmentation, new business models and new technologies. In the airline industry, changes in these three areas were dependent on the regulatory framework, as the figure below illustrates. This is coherent with Drucker theories of innovation that argues that changes in market or industry structure are sources of innovation.

Figure 8 - Innovation cycles as a response to economic cycles

Figure 9 – Three Areas of Potential Innovation

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4.4.4 Institutional Entrepreneurship

This concept is referred when there is an attempt to change the current practices of an industry or society and thus to shape the institutions; the actors of this initiative are called institutional entrepreneurs. In turn, institutional entrepreneurs are "agents who have an interest in specific institutional structures and who command resources which can be applied to influence institutionalized rules, either by committing those resources to the support of existing institutions or by using them for the creation of new institutions." This definition implies that the interest-driven actors are able to change the institutional design (in order to obtain rewards for themselves) if they have enough resources to make changes in institutions. Thus, from an actor point of view, the constraints to their strategies are not the institutional rules but the lack of resources. This approach considers the agents as sources of change (the institutional entrepreneurs), that is, it focuses on the endogenous sources of deliberate change. The concept of creative destruction that was previously presented in this chapter is integrated in the explanation of this approach. The entrepreneur will carry out new combination of resources, in order to fix the current situation in his/her environment that is hindering him/her actions. That is, the entrepreneur, moved by his/her own interest, will destroy the "taken-for-granted" rules that institutional logics impose, in order to get his/her things done. This process of deinstitutionalization is also related with the concept of embeddedness. Beckert points that creative destruction is related with a process of disembedding, which in turn goes "hand in hand with the emergence of new institutional structures." In turn, Greenwood & Suddaby, when referring to the network location theory in their article, refer that less embedded organizations (that are the ones who are peripheral organizational players) are the ones where entrepreneurship is more likely to emerge from.

As we saw, these deliberate changes by the actors occur when they have enough resources and interest in changing the current design. Apart for those facts, they can occur when there is a high degree of certainty. In one of his articles regarding strategic agency and institutional practices, Beckert argues that uncertainty has a crucial role in explaining institutional change through actor’s interventions (by strategic agency he defines “the systematic attempt to reach conceived ends through the planned and purposeful application of means” and by uncertainty he defines “situations in which intentionally rational actors cannot deduce strategies from their preference rankings”). Briefly resuming his main argument, Beckert argues that more strategic agency is expected when there is a higher degree of certainty with the institutional field, that is, actors’ willingness to change their environment changes positively with the degree of certainty of their environment.

The deregulation of the European air transportation was in part caused by actors inside the institution itself (like the individual actions of Lord Bethnell, a UK member of the European Parliament and also from initiatives from the European Commission) but also by actors inside the industry as it was the case of the tourist operator Nouvelles Frontières, which challenged the

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218 Ibid
223 Ibid, pp. 782-793
prevailing rules (which according to Beckert are often in conflict with each other\textsuperscript{225}, like it was the case of the Treaty of Rome that promoted competition but at the same type constrained it in the airline industry) concerning the fixed by fares set in bilateral agreements by double approval\textsuperscript{226}. The actor, moved by its own interests (maximization of profits), attempted to challenge the taken-for-granted rules that were hindering it to get its things done. This represented an act of institutional entrepreneurship within the industry.

Institutional entrepreneurship can be seen as a way to achieve regulatory capture, a concept we presented in chapter 4.2.2. The similarity is that institutional entrepreneurship theory says that actors with specific interests and possessing resources are able to change institutional design to their own benefit and in regulatory capture theory agents seek to maximize their own utility\textsuperscript{227}. That is, with institutional entrepreneurship interest-driving agents can achieve regulatory capture and obtain benefits such as direct subsidy of money, control over entry by new rivals (barriers to entry), and policies affecting substitutes and complements, and price-fixing\textsuperscript{228}.

\subsection*{4.4.4 Corporate Entrepreneurship}

This concept is a specific type of entrepreneurship that has been developed since the last years. Among the various definitions we could find, we selected the ones that can better describe corporate entrepreneurship. Sharma and Chrisman define it has “the process where by an individual or a group of individuals, in association with an existing organization, create a new organization or instigate renewal or innovation within that organization”\textsuperscript{229}. That is, this specific field of entrepreneurship is related with the previous concepts of entrepreneurship and innovation we have explained before. This change within the organization can be linked with strategic concepts presented by Porter, mainly the sustainability of competitive advantage (a concept that will be later explained in our thesis).

Academic research within this field agrees upon the fact that changes in firm’s environment, (like the environmental jolts we have referred in 4.3) trigger corporate entrepreneurship. Kuratko et. Al organized the triggers of corporate entrepreneurship into five different categories: internal/external source, opportunity-driven/threat-driven, technology-push/market pull, top-down/bottom-up and systematic or deliberate search/change or opportunism\textsuperscript{230}. Also Guth and Ginsberg agree upon the fact that environment fosters corporate entrepreneurship\textsuperscript{231}. These causes are coherent with Shane’s work regarding the role of environment in firms’ decisions to exploit opportunities and with Meyer’s work in environmental jolts and firms’ adaptation to them, two authors we have introduced in chapter 4.3.

These events trigger development of strategies at the corporate level. Acquisitions, diversification, turnaround, creation of SBU (strategic business units), corporate venturing, strategic

\begin{thebibliography}{99}
\end{thebibliography}
renewal, joint ventures, alliances, cooperative arrangements are some of the most important strategic adaptations firms make in order to adapt to the new competitive environment. Most of these decisions can be seen in the European airline industry today. For instance, Star Alliance, the change of strategy in Ryanair after the implementation of the three deregulation packages in EU, SAS positioning targeting business class, creation of subsidiaries by BA, Air France and SAS to face the threat of low-cost, franchising airline brands, are recent examples of corporate entrepreneurship in the airline industry that we will present through our thesis.

4.5 Strategic Position

Linking with entrepreneurship and deregulation, organizations had to come with innovative strategies to survive in the high competitive environment brought by deregulation. In this last chapter of theory will focus in specific models and strategies of individual organizations. We will present the SWOT analysis that will help us to identify strengths, weaknesses, opportunities and threats that changed with the introduction of deregulation. Then we present Porters’ competitive strategies of cost leadership, differentiation and focus, as well as other strategic possibilities a firm has according to the strategic clock.

4.5.1 - The SWOT analysis

*Ryanair’s weakness in the early days was that it didn’t know what it wanted to be.* Tony Ryan, in How a Small Irish Airline Conquered Europe” by Siobhán Creaton

Johnson, G., Sholes, K. and Whittington, R. define the SWOT analysis as “it summarizes the key issues from the business environment and the strategic capability of an organization that are most likely to impact on strategy development”. In other words, the goal of this analysis is to identify the strengths and weaknesses which are internal of the company and the opportunities and threats which occur on the external level. On one hand, the external factors deal with the environmental models of competitive advantage, on the other hand, the internal factors are related to the core competencies and capabilities of the company and may influence the future strategic orientation.

As for the PESTEL analysis on the macro-environment, the external and internal factors may be interdependent and can be represented by the following chart:

![Figure 10 - The interdependency of internal and external factors of the SWOT analysis](image-url)

To summarize the SWOT analysis, we can say that it help to focus on the strengths of organizations, nevertheless it highlights in the same time the weaknesses. In the same time, it

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Chapter 4

The Airline Industry and Theoretical Framework

reveals organizations opportunities in their environment but also the threats that organizations have to be aware of. Therefore, the SWOT analysis helps and supports companies in the early process of taken measures and setting strategies.

However, it is a simple model and has limits. Indeed, it is difficult to define whether certain factors are an opportunity or strength or rather a threat or a weakness. What are the boundaries? Furthermore, it is capital that managers who elaborate the SWOT analysis stays objective when applying the model in order not to influence it.

Finally, the SWOT analysis is really useful and has the maximum utility when you do a comparative study with your competitors also in term of strengths, weaknesses, opportunities and threats. For instance, SAS elaborates a SWOT analysis on its competitors (Ryanair, Air France…) and then compare in order to highlights its internal and external factors.

4.5.2. Competitive Strategies

“Ryanair snuck up on us. We didn’t realize it had redefined its strategy. It took a lot of adjusting to.”

Aer Lingus source in “How a Small Irish Airline Conquered Europe” by Siobhán Creaton

According to Porter, competitive strategy is “the search for a favorable competitive position in an industry” which aims to “establish a profitable and sustainable position against the forces that determine industry competition”. The firm, through its competitive strategy relates itself to its environment in order to give a better response to changes in it and to shape the environment in its favor. Thus, setting a competitive strategy is the following step of the firm after analyzing the forces of its industry.

In order to achieve a performance above average in an industry, a firm should develop a sustainable position in the long run, which means to have a sustainable competitive advantage. Low cost (cost advantage) and differentiation are the two basic types of competitive advantage a firm can have which in turn originate from industry structure. Porter presents three generic strategic approaches to outperform other firms in industries and create a sustainable position in the long run: overall cost leadership, differentiation and focus (which in turn has two variants – cost focus and differentiation costs). These three generic strategies are presented in the following figure:

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We will briefly explain each one of these three strategies:

Cost Leadership:

“It seemed blindingly obvious that if we couldn’t out-service Aer Lingus with better business class and better service, we could certainly offer better fares.”

By Michael O’Leary in “How a Small Irish Airline Conquered Europe” by Siobhán Creaton

In the first strategy, a firm tries to achieve the low-cost producer in the industry. This requires efficient-scale facilities, cost reductions in all the areas of the firm and in its value chain, tight control over costs. To achieve this, a firm must pursue low positions in the learning curve and to exploit all sources of cost advantage. As a result, firms who choose this strategy often sell a standard or no-frills product. Apart from these basic requirements, a firm should also have a high relative market share or other kind of advantage like easy access to sources of supply. In turn this may require having a wide range of related products in order to spread the costs, heavy capital investment in equipment, aggressive pricing and start-up losses. When the firm achieves this goal, the high margins obtained can be used to reinvest in modern equipment and facilities in order to maintain the low cost base and thus a low-cost leadership. This position will give the firm a defensive position against industry rivals, buyers, suppliers, new entrants and substitutes.

Summing up what has been explained above, citing Porter’s words, “a firm has a cost advantage if its cumulative cost of performing all activities is lower than competitors’ costs.” This cost advantage, in turn, is based on two major ways: control cost drivers (value of activities that have a high proportion in the total costs) and reconfigure the value chain (different and efficient processes like producing, distributing, marketing).

This low cost leadership is the strategy that Ryanair brought from the American company Southwest Airlines to Europe in the beginning of the 90’s, and constitutes the introduction of a new business model in a different context, an example entrepreneurial behavior.

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237 Ibid, p. 12
242 Ibid, p. 99
Differentiation:

“We know it’s the standard of service we provide that distinguishes Singapore Airlines from our competitors.”


In this second strategy a firm seeks to offer a different product or service in the industry, with the aim of creating something that is perceived as unique in the industry and highly valued by the buyers. To do this, the firm should focus in one or more attributes that are perceived as valuable and important by the buyers. There are several approaches to differentiating like design, brand image, technology, features, customer service, etc, but often firms who pursue this strategy differentiates themselves in several dimensions.

Porter specially reinforces the role of value chain to contribute to this uniqueness. According to him, “any value activity is a potential source of uniqueness”, and thus the firm procurement of inputs, support activities, technology development activities, operation activities can all create uniqueness. A firm can also differentiate itself through its competitive scope or allow differentiation come from downstream, specially channels that can be a source of uniqueness and strength its reputation, service, etc.

In order to achieve a sustainable differentiation and to have an above-average performance in its industry, the firm should not only focus in one or more of those areas we just mentioned - its price premium also exceed the extra costs incurred for being unique so the firm can achieve superior performance. That is, a firm pursuing this strategy should not ignore its cost position with the prejudice of its premium prices being annulled. To do that the firm should reduce costs in all areas that do not affect differentiation. This strategy will also provide a defensive position against the players in the industry.

Focus:

“I think the future for Ryanair is for a limited niche airline operating out of Ireland primarily to London.”

By PJ McGoldrick (former Ryanair’s CEO) in How a Small Irish Airline Conquered Europe” by Siobhán Creaton

This strategy implies that the firm chooses a specific segment of the industry to focus its strategy exclusively. The targeted segment can be a particular buyer group, a segment of the product line, or a geographical market. According to Porter, this strategy is based on the assumption that “the firm is thus able to serve its narrow strategic target more effectively or efficiently than competitors who are competing more broadly”. This implies the firm achieves a competitive advantage through differentiation focus (when the firm achieves differentiation in its target segment through the exploitation of the special needs of the customers in the specific segment) or through a

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247 Ibid, p. 14
cost focus (when the firm achieves cost advantage in its target segment through the exploitation of differences in cost behaviors of the specific segment)\textsuperscript{250}.

Other generic strategies:

More recently, some authors like Bowman and Faulker developed some intermediary strategies between Porter’s generic strategies (and that go in line with his theory) based on the principle that competitive advantage can be achieved if organizations provide customers with products or services that satisfy their necessities (needs and wants) in a way better and more effectively than its competitors\textsuperscript{251}. They developed a strategy clock aimed to briefly describe different competitive strategy options. Each position represent a different generic strategy and also different positions the firm can assume in the market, focusing on customer’s two types of requirements - perceived product/service benefits and price. In the following figure we present the strategy clock:

![Strategy Clock](image)

Figure 12 - The Strategy Clock: competitive strategy options\textsuperscript{252}

Positions 1 and 2 are price-based strategies (corresponding more or less to Porter’s cost leadership), position 4 is a differentiation strategy (similar to Porter’s differentiation), position 5 is a focused differentiation (that corresponds to Porter’s focused differentiation), position 3 is an intermediary position between cost and differentiation, and positions 6, 7 and 8 are failure strategies.

Chapter 5  Empirical Data Presentation

5 Empirical Data Presentation

In the chapter five, we will present our empirical data of the thesis. Since case study theorists argue about the importance of collecting multiple sources and types of evidence to achieve validity, we decided to hold data from different sources and tried to get the most variety of data. We start with a short presentation of the airline industry and by in introducing the largest European airline companies as well as the major variations in the airline industry’s development. Then we will continue by presenting SAS’ and Ryanair’s company data.

“*The airline industry will be going through dramatic changes in the years to come*”

by Gustafsson A., Ekdahl F., Edvardsson Bo

5.1. The European Airline Industry

It is impossible to explain all the characteristics of European Airline Industry in this thesis therefore we will describe the most significant characteristics and evolutions over the last two decades that are relevant for our topic. Besides presenting the gradual deregulation of air transportation in Europe, we also present the future trends of the industry, the three main alliances (Star Alliance, Oneworld and SkyTeam) and present the types of carriers that exist now in Europe

5.1.1 Evolution of air transport regulation in Europe

The European airline industry has inherit historical and political legacies that can be traced back far as the Chicago Convention of 1944. Within this meeting, nations gathered together to define the structure of air transportation in the post-Second World War period. However, most members wanted to protect their national airlines that were seen important vehicles to expand nation’s prestige and commerce, that is, airlines existence was based in benefits other than commercial viability. This protectionist regulation can be inserted in the public interest theory which is most of the times followed by the Governments when they regulate public utilities. The reasons to regulate are to correct the market failures, adjusting the distributional effects that arise from market power, asymmetric information and externalities. Sinha and Button agree that the public interest was the main logic countries adopted to regulate the air transportation market after the Second World War. However, even if the Government intentions seem to be the best ones, this kind of regulation introduces distortions in the market and a need to review economic regulation regularly. Barrett shows how the benefits Irish Government thought its flag carrier, Aer Lingus, would bring became a negative factor in air transportation in Ireland. That is, the

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public interest theory had failed to achieve its main goal – to satisfy the public interest, and instead brought benefits to the flag carrier. We will now explain how and why it failed.

Despite of public interest theory had failed to achieve its ultimate goal (to bring public benefits) some actors were benefited with this failure. The benefited ones were the flag carriers. In Europe, states had their own international airline (flag carriers), which was public owned and thus it had great amount of market power\textsuperscript{261}. For instance, in Ireland market, Barrett shows Aer Lingus achieved regulatory capture\textsuperscript{262} and in Scandinavian, Kjell Wilsberg says Before deregulation (Norway) On the domestic market, the Ministry of Transport granted concessions to SAS and Braathens for 5 years periods. This meant traffic rights but also obligations, to operate the routes granted and the Ministry's approval of schedule/frequencies and capacity, prices, discounts etc\textsuperscript{263}. During years, these flag carriers were heavy subsidized and dominated airline industry\textsuperscript{264}. When only a small group of society is able to achieve the benefits of regulation we say that small group achieved capture of regulation. This small group is benefited because its interests are in line with the interests of the legislative body, in this case, the national governments\textsuperscript{265}. Sinha, citing Stigler's notion of regulatory capture, argues that economic regulation is not always created with the public interest in mind, and even if it was, it can suddenly stop to focus on it. The main reason for this, he explains, is that regulators can be captured by the regulated\textsuperscript{266}. In turn this happens since the two groups see that cooperating with each other they can satisfy their own interests and maximize their own utility\textsuperscript{267}. In early 80s O'Leary commented the fact flag-carriers were against deregulation and pointed the benefits of a future change in the regulatory framework: Deregulation is a world that appears offensive to most national airlines. Nevertheless, in the long term deregulation combined with competition is the only method by which the traveling public will enjoy low fares\textsuperscript{268}.

Even though this may seem a theory of conspiracy, this was what happened between flag carriers and governments who brought benefits to each other through strict market regulation that apparently was bound to serve the public interest. During years, many airlines have played a role of ambassadors for the nations that own them and its public ownership makes them preserve their nationalistic character that restraints their strategies\textsuperscript{269}. Stigler four categories of benefits (direct subsidy of money, control over entry by new rivals, policies affecting substitutes and complements, and price-fixing\textsuperscript{270}) were enjoyed by flag carriers during years. Until the deregulation in EU, the industry suffered from over-capacity\textsuperscript{271}, almost non-existent price competition, capacity in various routes was agreed between airlines and pooling revenues was practiced\textsuperscript{272}. Bob Ayling (ex-CEO of British Airways) argued: Nation states believed that to be a nation you needed a flag, a national


\textsuperscript{263} Interview with Kjell Wilsberg, p. 2

\textsuperscript{264} Huettinger, M. (2006), Air Baltic and SAS – a case study in the European airline industry, Baltic Journal of Management Vol.1 No 2, p229


\textsuperscript{267} Ibid, p. 85


anthem and an airline. The first two come cheap but the third is extremely expensive. These reasons explain how Chicago Convention fail to create a freer international market and arrangements had to be solved within bilateral agreements. In turn, the fact that bilateral agreements are made by governments has led air liberalization to progress slowly and accounts for why this industry is so different from others and has not developed at a comparable way and pace as other industries.

These bilateral agreements in more than 40 European countries built a complex system with different authorities regulating their own air space and a diversity of institutional designs that airlines had to obey. Scott and Meyer argue that when there are more than one independent sources of authority that promulgate rules or that exercise control over the actors, this will create complex and administrative structures within the organizations that operate under the umbrella of those authorities. This was what was happening to Europe which, in opposition to USA, had a bigger disparity of situations. Regarding the situation before the Single European Market Herb Kelleher (CEO of Southwest Airlines) made the following comment: it was much more difficult because you were dealing with so many different airports, so many different nationalities and cultures, separate air traffic control systems. I think it was a harder job in a sense because you had so much disparity and diversity.

From the early days of European construction, there were some attempts to change this regulation that benefited the flag carriers in prejudice of European consumers and entrepreneurs. In 1954 the Council established the European Civil Aviation Community which in 1956 deregulated the charter airlines and in 1967 created a multilateral agreement regulating scheduled services. 12 years later, in 1979, further progress was made with the Commission’s Civil Aviation Memorandum No.1 which represented a step towards the creation of a competitive market by suggesting the Council to remove the barriers to entry. In 1984, after a its first failed attempt, Commission wrote a second version of its early proposal, the Civil Aviation Memorandum No.2 and introduced the concept of zones of flexibility into fare setting, which would give airlines more freedom to set fares, to be included in bilateral agreements. In 1985 the judgment by the ECJ in Nouvelles Frontières case (which involved preventing a French travel agent to sell air tickets below price) forced the Council two years later two give the first concrete step towards deregulation, through a gradual process.

Since the 80s air transportation in Europe has been following the liberalization trends that occurred in US in 1978. Market liberalization has occurred within many European countries that in early 80’s first unilaterally liberalized their domestic markets. This was the case of UK which had a national regulatory agency more liberal than in other European countries and thus was more liberal in the allocation of licenses and acceptance of fare flexibility zones. These liberalization was accomplished with privatization of airports (in UK BAA was privatized in 1987), gradual selling of flag carriers (like happened in Germany and the Netherlands) or complete privatization of flag carrier (BA was privatized in 1987).

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Liberalization also occurred in pairs of countries, which were liberalized their bilateral agreements. For instance, in 1984 UK and the Netherlands bilateral agreement loosed the rules covering traffic between them and a double disapproval system in 1985, two years than in other EU countries. After 1984, other countries made agreements between themselves, with different degrees of liberalization\(^{279}\). However a common liberal agreement among EU countries was still needed.

The intra-European market started to imitate the US deregulatory market in 1987 when the European Council introduced the First Aviation Package to come into force in 1\(^{st}\) January of the following year\(^{280}\). This first deregulation gave for the first time power to the Commission to apply EU competition rules, however with some limitations. This package also adopted suggestions from the Second Civil Aviation Memorandum regarding zones of flexibility. The Second Aviation Package came into force in 1\(^{st}\) November 1990 basically loosed the restrictions that were still present in the previous package and members agreed to introduce deeper freedoms in January 1993 with the implementation of the Third Aviation Package that would come with the introduction of the Single European Market. The last restrictions were abolished in 1\(^{st}\) April 1997 when full cabotage became available, national ownership rules were abolished (which meant EU airline industry could experience mergers subject only to competition rules) and all controls on fare levels and restrictions on non-scheduled services were removed\(^{281}\). It is important to bear in mind that implementation of full cabotage does not mean that the market is full deregulated – far from that. It means that economic regulation (concerning controls over prices and capacity) has been removed\(^{282}\). The details of these three packages can be seen in the table presented next page.

We argue that the first package of deregulation represented the first successful measure of European Union to introduce coherent public interest policies. As we have explained before, national governments had failed to implement these policies in their own countries. The progressive loosening of restrictions in capacity and price setting, the removal of barriers to entry, the introduction of competition rules and the opening of routes in the European territory to all EU airlines, are policies coherent with the spirit of public interest theory: correct malfunctions of market (like concentrations of power which were provoked by flag carriers in their own countries) and higher levels of efficiency and greater individual choice (which were achieved with the entry of LCC)\(^{283}\). In order to attain these goals, European Commission created constraints and enforcement policies that are according to North, the necessary tools to actors correct their models of action (in which they act with incomplete information), and so they can reduce transaction costs\(^{284}\). Those constraints and enforcement powers were delegated to European Commission by the European Council through Council Regulations and by the power of Treaty of Rome.

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\(^{280}\) Ibid, p.25


<table>
<thead>
<tr>
<th>Package</th>
<th>From 1st January 1988</th>
<th>From 1st November 1990</th>
<th>From 1st January 1993</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>International scheduled passenger transport</strong></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td><strong>Fares</strong></td>
<td>Percent of fares approved: ‘Discount’ 66%-90%, ‘Deep Discount 45%-65%, automatically, and all others subject to double approval.</td>
<td>Percent of fares approved: ‘Fully flexible’ 106% unless double disapproval, ‘Normal Economy’ 95-105% automatically, ‘Discount’ 80%-94% automatically, ‘Deep Discount’ 30%-79% automatically, and all others subject to double approval.</td>
<td>Provisions made for the States and/or the Commission to intervene against excessive basic fares (in relation to long term fully allocated costs) and sustained downward development of fares.</td>
</tr>
<tr>
<td><strong>Designation</strong></td>
<td>Multiple designations by a State allowed if: 250,000 pass (1st year after integration), 200,000 pass or 1,200 rt flights (2nd year), and 180,000 pass or 1,000 rt flights (3rd year).</td>
<td>Multiple designations by a State allowed if: 140,000 passengers or 800 route flights (from January 1991) and 100,000 passengers or 600 route flights (from January 1992)</td>
<td>No longer applicable.</td>
</tr>
<tr>
<td><strong>Capacity</strong></td>
<td>Capacity shares between states: 45/55% from January 1988 and 40/60% from October 1989.</td>
<td>Capacity shares of a State of up to 60%, and capacity can be increased by 7.5% points per year.</td>
<td>Unrestricted</td>
</tr>
<tr>
<td><strong>Route Access</strong></td>
<td>3rd/4th freedom region to hub routes permitted, 5th freedom traffic allowed up to 30% of capacity, additional 5th rights for Irish and Portuguese, combination of points allowed, and some exemptions.</td>
<td>3rd/4th freedom between all airports, 5th freedom traffic allowed up to 50% of capacity, public service obligations and certain protection for new regional routes, a 3rd/4th freedom service can be matched by an airline from the other State, and scope for traffic distribution rules and restrictions related to congestion and environmental protection.</td>
<td>Full access to international and domestic routes within the EU (exemptions for Greek islands and Azores), cabotage unrestricted from April 1997 with restricted cabotage allowed for up to 50% of capacity until then, reformed public service obligations and some protection for new thin regional routes, and more scope for traffic distribution rules and restrictions related to congestion and environmental protection.</td>
</tr>
<tr>
<td><strong>Competition rules</strong></td>
<td>Ground exemption regarding some capacity coordination, tariff consultation, slot allocation, common computer reservation systems, ground handling of aircraft, freight, passenger, and in-flight catering, and some sharing of pool revenues.</td>
<td>Ground exemption regarding: some capacity coordination, tariff consultation, slot allocation, common computer reservation systems, and round handling of aircraft, freight, and passenger and in-flight catering.</td>
<td>Ground exemption regarding; some capacity coordination, tariff consultation, slot allocation, common computer reservation systems, and joint operation of new thin routes.</td>
</tr>
<tr>
<td><strong>Licensing of Air Carriers</strong></td>
<td>Not provided for in 1st and 2nd Packages</td>
<td>Uniform conditions across EU; notion of EU ownership and control with small carriers subject to looser regulatory requirements.</td>
<td></td>
</tr>
</tbody>
</table>

Table 5 - The EU Air Transportation Packages

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56
5.1.2 Consequences of deregulation for the airline industry

Dan Lundvall argues that from 1993 deregulatory effects had more significance in market that started to change and airlines had to change their strategies\textsuperscript{286}. Stelios, founder and CEO of easyJet confirmed the opportunities provided by the open European market: \textit{We think the market in Europe is immense: there’s absolutely no reason at why a low-cost airline has to start stamping on the patch of an existing one. There’s a big sandpit here and plenty of space}\textsuperscript{287}. These opportunities seemed to have been taken by the new comers, as the following table shows:

\begin{table}[h]
\centering
\begin{tabular}{lccc}
\hline
 & \textbf{Domestic routes} & & \textbf{International routes} \\
\hline
Austria & 0 & 0 & 12 & 12 \\
Denmark & 0 & 4 & 8 & 11 \\
Finland & 9 & 9 & 7 & 0 \\
France & 10 & 9 & 26 & 35 \\
Germany & 36 & 40 & 10 & 15 \\
Greece & 0 & 0 & 0 & 16 \\
Ireland & 0 & 0 & 36 & 46 \\
Italy & 28 & 26 & 7 & 15 \\
The Netherlands & 0 & 0 & 20 & 18 \\
Norway & 27 & 38 & 0 & 9 \\
Portugal & 47 & 35 & 14 & 37 \\
Spain & 0 & 60 & 14 & 20 \\
Sweden & 47 & 47 & 12 & 12 \\
UK & 43 & 56 & 40 & 45 \\
\textbf{Total} & 26 & 36 & 19\textsuperscript{a} & 25\textsuperscript{a} \\
\hline
\end{tabular}
\caption{Changes in competition on selected EU scheduled routes\textsuperscript{288}}
\end{table}

As we can see, before and after the implementation of the Third Aviation Package in 1993, in both domestic and international routes the proportion of round trip flights with two or more competitors increased 10% and 6% respectively. This suggests this last package brought more competition to the industry. Apart from this increase of competition, deregulation also diminished the market power of the old monopolistic flag carriers, giving more space to competitors like regional carriers, as it is shown in the next table.

\textsuperscript{286} Interview with Dan Lundvall, p.3
Table 7 - Capacity of Air System (number of seats available in '000) on scheduled return flights within the EU

<table>
<thead>
<tr>
<th></th>
<th>December 1992</th>
<th>December 1997</th>
</tr>
</thead>
<tbody>
<tr>
<td>All carriers</td>
<td>12,232</td>
<td>16,893</td>
</tr>
<tr>
<td>Flag carriers</td>
<td>9929</td>
<td>11,355</td>
</tr>
<tr>
<td>Regional carriers</td>
<td>2303</td>
<td>5538</td>
</tr>
<tr>
<td>Share of flag carriers (%)</td>
<td>81</td>
<td>67</td>
</tr>
</tbody>
</table>

Table 7 - Capacity of Air System (number of seats available in '000) on scheduled return flights within the EU

Button argues EU followed the US experience concerning entry of new carriers and expansion of previous operators, which in the European case were mostly flag carriers. He argues after a massive entry of new airlines and expansion of activities of old operators, a period of consolidation is followed. The next table provides information regarding entry of carriers in different EU members and the survival rates of existing carriers. Among the differences between countries, Finland, Sweden, UK and Italy register the highest number of withdrawals. Despite of the high number of withdrawals, which demonstrates the effects of aggressive competition in the market, more than 50 airlines that entered in 1993 were still flying in 2001 (year which the paper was writing).

Table 8 - Airlines serving the EU market

<table>
<thead>
<tr>
<th>Operating in January 1993</th>
<th>Start-up since January 1993</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Still flying</td>
</tr>
<tr>
<td>Austria</td>
<td>4</td>
</tr>
<tr>
<td>Belgium</td>
<td>1</td>
</tr>
<tr>
<td>Denmark</td>
<td>4</td>
</tr>
<tr>
<td>Finland</td>
<td>9</td>
</tr>
<tr>
<td>France</td>
<td>2</td>
</tr>
<tr>
<td>Germany</td>
<td>11</td>
</tr>
<tr>
<td>Greece</td>
<td>1</td>
</tr>
<tr>
<td>Ireland</td>
<td>3</td>
</tr>
<tr>
<td>Italy</td>
<td>6</td>
</tr>
<tr>
<td>Luxembourg</td>
<td>1</td>
</tr>
<tr>
<td>The Netherlands</td>
<td>6</td>
</tr>
<tr>
<td>Portugal</td>
<td>3</td>
</tr>
<tr>
<td>Spain</td>
<td>1</td>
</tr>
<tr>
<td>Sweden</td>
<td>6</td>
</tr>
<tr>
<td>UK</td>
<td>11</td>
</tr>
<tr>
<td>Total</td>
<td>69</td>
</tr>
</tbody>
</table>

Table 8 - Airlines serving the EU market

290 Ibid, p. 262
291 Ibid, p. 265
Chapter 5  Empirical Data Presentation

5.1.3 Types of airlines in Europe

Prior to the implementation of the last package of deregulation in Europe, the market was full integrated due to the diverse type of services offered by flag carriers plus the seasonal leisure travel provided by charter carriers and the local and regional services provided by regional airlines. Button argues, after deregulation the market became much more segmented, reflecting the diversity of consumer preferences. We will now present the three main categories of airlines based on their business model: full services carriers (where are the flag carriers), no-frills carriers and non-scheduled carriers (charter airlines).

Full services carriers (FSC)

FSC include the flag carriers which in the last years have lost of its political tight through gradual privatization and pressures of a more competitive environment. These airlines have their network centralized in a single airport hub (the country capital), providing different services – business, leisure, domestic, intra-European, Intercontinental – that entails them to operate different types of aircraft. They often discriminate prices through an efficient and complex system of yield management bound to generate high revenues to sustain their structure. FSC make use of their hub-and-spoke network so they can maximize economies of scope and density. However, these incumbent airlines still benefit from grandfather rights, which grant them the right to renew all slots that had a degree of utilization above 80% in previous periods. Most of their revenues come from the business market which they target through different services like lounges, special cabins, flexible tickets, global connections, hubs in major centers of commerce, etc. This dependence on business travelers along with the dependence on revenues from the totality of spokes they serve and the low margins of this model are the main weaknesses of FSCs.

Throughout the last years, the structure of these FSC has followed some trends: first, the congested airports and constraints in air traffic control, along with the legacy effect has divided the market two types of hub service providers - the ones based in big hubs such as Heathrow (BA), Frankfurt (Lufthansa), Charles de Gaulle (Air France) and Schipol (KLM) and smaller hubs such as Madrid (Iberia), Stockholm (SAS) and Rome (Alitalia); second, they saw a decline revenues in shorter haul markets due to an increase competition and thus had to shift resources to long haul markets; third, these hub carriers have gone through a consolidation process strengthening their global strategic alliances merging with other carriers (such as Air France in KLM in 2003); fourth because of higher competitive environment, FSC have counter-attacked no-frills carriers through a modification of their fare structure (fares became cheaper and more flexible) in European short-haul flights.

No Frills

“"They were opportunistic companies [Ryanair and Easyjet]. These guys thought they had a possibility to set another type of air travel – an air travel that looked like a bus transport.”

By Dan Lundvall

293 Fridstrøm, L. et al, Towards a More Vigorous Competition Policy in Relation to the Aviation Market, Journal of Air Transport Management, 10, p. 74
The no-frills model was brought to Europe by Ryanair in the early 90’s from Southwest Airlines and this model have mushroomed since the Single European Market in 1993. Like the original concept created by Kelleher (CEO of Southwest Airlines) this models is based on short point-to-point routes, scheduled flights at a low cost, secondary airports close to final destinations, 25 minutes turnaround, single type of aircraft, only economy class and no assigned seats. As the time went by, other innovations were included in the model such as booking reservations through internet and yield management (although in a different way than established carriers). Kjell Wilsberg argues this new distribution system plays a main role in the LCC cost structure: Internet sale has an enormous impact on sales and distribution and is a key element of the Low Cost airlines success.

To achieve a low cost structure and efficient operations, these carriers take various measures like, removing elements of service, bargaining for inputs (favorable landing fees for airports and cheaper aircraft), pressuring their workforce (more working hours and lower remuneration than scheduled carriers), making an extensive use of resources (maximizing their flying time with short turnarounds in under-utilized airports close to big cities), receiving state aids, using one single class, achieving a better occupation rate, no services on board, reservations via internet and no refund policy. These characteristics can differ slightly from LCC to LCC. For instance, Easyjet offer services to hub airports and not to secondary or regional airports like Ryanair, GO (that was bought by Easyjet) offered higher quality service and was flying to big airports, mainly because it was a subsidiary of BA. Burton makes worth notice that no-frills carriers are a heterogeneous group and thus it is difficult to generalize this business model and the markets in which they operate. For instance, some of them compete with charters in leisure routes like bmibaby (however charters have a advantage in the cost structure as we already mentioned), others like Ryanair and Easyjet compete mostly with full service carriers (in some routes they compete also with charters) and others offer regional services with limited coverage like BA CityExpress and Wideroe’s.

Non-Scheduled Carriers

Charters have enjoyed a freer regime than scheduled airlines since Chicago Convention in 1944 excluded non-scheduled flights from international agreements and since 1967 charters have enjoyed freedom in the European market. After the third package, the distinction between scheduled and charter services was abolished, which mean they can designate their flights as they were scheduled flights.

Charter airlines main function is to provide leisure based services, normally included in a tour package, to sunny destinations in south European countries like Spain, Italy, Portugal or Greece or to ski resorts in France, Switzerland, Austria and Germany. Nowadays, most of European charter airlines are part of vertically integrated firms that include a tour operator, a travel agency, an airline and in some cases hotels and resorts. These airlines are able to achieve a cost base even

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296 Ibid, pp. 56-66
297 Interview with Kjell Wilsberg, p.1
300 Ibid, pp. 60-64
301 Chicago Convention Agreement, 1944, 5º article – Right of Non-Scheduled Flight
lower than low-cost no-frills carriers due to bigger aircraft (Boeing 321 and Airbus 757, both more than 220 seats), higher distance in their flights (more than 200km), high load factors (often more than 90%), higher aircraft utilization (however with a high seasonal variation) due to no constrains in operations times (schedules are often constrained between 7 a.m. and 22 p.m.), higher labor productivity (outsource of activities), higher labor productivity and non-existent distribution costs (undertaken by the tour operator)\(^{303}\). Despite of these advantages charters have always operated with low margins and are highly vulnerable to shifts in economic and market forces\(^{304}\).

**Full Service Carriers vs. No-Frills Carriers**

Now we will present comparison between the two types of services – no-frills model (represented by ELFAA) and the full service model (represented by AEA):

<table>
<thead>
<tr>
<th></th>
<th>ELFAA</th>
<th>AEA</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Members</strong></td>
<td>11</td>
<td>30</td>
</tr>
<tr>
<td><strong>Fleet</strong></td>
<td>402</td>
<td>2.400</td>
</tr>
<tr>
<td><strong>Daily Flights</strong></td>
<td>2.331</td>
<td>10.720</td>
</tr>
<tr>
<td><strong>Passengers (millions)</strong></td>
<td>106</td>
<td>320</td>
</tr>
<tr>
<td><strong>Employees</strong></td>
<td>14.000</td>
<td>378.000</td>
</tr>
<tr>
<td><strong>Employee Productivity (Passengers per employee)</strong></td>
<td>7.571</td>
<td>847</td>
</tr>
<tr>
<td><strong>Average Load Factor</strong></td>
<td>83%</td>
<td>n/a</td>
</tr>
<tr>
<td><strong>Aircraft Productivity (Passengers per aircraft)</strong></td>
<td>263.681</td>
<td>133.333</td>
</tr>
<tr>
<td><strong>Daily flights per aircraft</strong></td>
<td>5.79</td>
<td>4.46</td>
</tr>
</tbody>
</table>

Table 9 - ELFAA vs. AEA, authors’ creation with available data collected\(^{305}\)

The data we collected and calculated show that no-frills carriers are far ahead from the old scheduled services in terms of productivity (both from aircraft and from employee). For instance, no-frills carriers’ employees are almost nine times more productive than scheduled flight carriers’ employees. The same happen with the aircraft, where ELFAA members fly one more time per day and each year ELFAA aircraft are able to carry the double of passengers than AEA aircraft. This shows the maximization of no-frills fleet to achieve efficiency.

In the next page we will show the main differences between these two business models:

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\(^{305}\) Data collected from ELFAA member’s statistics JAN-DEC 2006 and AEA 2006 Yearbook
<table>
<thead>
<tr>
<th>Traditional carriers</th>
<th>Low-cost carriers</th>
</tr>
</thead>
<tbody>
<tr>
<td>Product/service concept</td>
<td>Product/service concept</td>
</tr>
<tr>
<td>- Three transport classes for customers</td>
<td>- Single class</td>
</tr>
<tr>
<td>- Seat assignment</td>
<td>- Limited number of daily flights</td>
</tr>
<tr>
<td>- Free baggage transfer</td>
<td>- Focused on point to point service</td>
</tr>
<tr>
<td>-_primary_airports</td>
<td>- Landing and take-off in secondary airports (mostly)</td>
</tr>
<tr>
<td>- Various distribution channels (Online, direct and travel agencies)</td>
<td>- Catering (in the economy class) against payment</td>
</tr>
<tr>
<td>- Loyalty program</td>
<td>- No special service</td>
</tr>
<tr>
<td>- Focus on business and leisure passengers</td>
<td>- Appealing to price-sensitive passengers</td>
</tr>
<tr>
<td>- Various types of aircraft</td>
<td>- High frequency</td>
</tr>
<tr>
<td>- Code share, global alliances</td>
<td>- High-density seating with smaller seats in order to have more ones.</td>
</tr>
<tr>
<td>- Generous pitch, seat assignment</td>
<td>- No seat assignment</td>
</tr>
<tr>
<td>- Customer service (full service, offers reliability)</td>
<td>- Customer service (generally under performs)</td>
</tr>
<tr>
<td></td>
<td>- No frequent flyer programs</td>
</tr>
<tr>
<td></td>
<td>- Short ticket-sales channels (Online and direct booking)</td>
</tr>
<tr>
<td></td>
<td>- Single type of aircraft (less maintenance costs, crew pool and savings in training and qualification)</td>
</tr>
<tr>
<td></td>
<td>- Few physical tickets</td>
</tr>
<tr>
<td>Communication concept</td>
<td>Communication concept</td>
</tr>
<tr>
<td>- Expensive commercials on television, radio, newspapers, magazines…</td>
<td>- Selective advertising only in relevant geographical markets</td>
</tr>
<tr>
<td></td>
<td>- Emphasizing communication on prices</td>
</tr>
<tr>
<td></td>
<td>- Focus on IT marketing</td>
</tr>
<tr>
<td></td>
<td>- Advertising on specific targets (teenagers…)</td>
</tr>
<tr>
<td>Revenue concepts</td>
<td>Revenue concepts</td>
</tr>
<tr>
<td>- Complicated fare system with a higher number of fares at a time + yield management</td>
<td>- Price differentiation by time of booking and strength of demand</td>
</tr>
<tr>
<td>- Ticket sales as biggest source of return</td>
<td>- One way pricing, simplified fare structure</td>
</tr>
<tr>
<td>- Medium to high utilization of aircraft</td>
<td>- Increasing revenues by focusing on volumes</td>
</tr>
<tr>
<td></td>
<td>- On board sales of some service amenities</td>
</tr>
<tr>
<td></td>
<td>- High number of flight hours by plane (+3 hours)</td>
</tr>
<tr>
<td></td>
<td>- Subsidies claimed to regions</td>
</tr>
<tr>
<td></td>
<td>- Some airports have eliminated landing fees for LCC</td>
</tr>
<tr>
<td>Growth concepts</td>
<td>Growth concepts</td>
</tr>
<tr>
<td></td>
<td>- Growth as long as it is efficient</td>
</tr>
<tr>
<td>Competence configuration</td>
<td>Competence configuration</td>
</tr>
<tr>
<td>- Product quality as a national carrier</td>
<td>- Underlining of low price reputation</td>
</tr>
<tr>
<td></td>
<td>- Increase of efficiency where possible</td>
</tr>
<tr>
<td>Organizational form</td>
<td>Organizational form</td>
</tr>
<tr>
<td>- Low turnaround</td>
<td>- Organization is focused around flight operations (core activity = flying)</td>
</tr>
<tr>
<td>- Many activities (extension: e.g. maintenance, cargo…)</td>
<td>- Outsourcing as a part of the policy</td>
</tr>
<tr>
<td></td>
<td>- Leadership without hierarchies</td>
</tr>
<tr>
<td></td>
<td>- Value addicted to efficiency</td>
</tr>
<tr>
<td></td>
<td>- “Just-in-time management” = 25mn turnarounds</td>
</tr>
<tr>
<td></td>
<td>- Pilots and flight attendants have to fly more</td>
</tr>
<tr>
<td>Cooperation concept</td>
<td>Cooperation concept</td>
</tr>
<tr>
<td>- Cooperation in order to cover regional flight offering</td>
<td>Vertical cooperation to generate marketing provisions</td>
</tr>
</tbody>
</table>

Table 10 – Differences between LCC and FSC, authors’ creation with available data collected.\(^{306}\)

5.1.4 The largest European Airlines

We would like to introduce you the largest European Airlines, especially before applying theories to two case studies on two different airlines in term of strategies, revenues etc: SAS Airline and Ryanair. We think that it is essential to rank these two companies among their competitors in Europe in order to see their importance. We could have ranked the European airlines according different criteria: the turnover, the profit, the number of passengers, the fleet size etc. We would have had different rankings but we decided to rank the five largest airlines according the number of passengers carried in 2006 (see table hereunder).

The largest European airline is Air France. It was founded in 1933 and is today one of the world’s leading airlines. Currently thanks to its merger with KLM (Dutch airline company), the Air France Group is the third largest international passenger transport, fourth largest freight carrier and second for the aircraft maintenance. Air France is present in more than 85 countries, has 200 destinations and 1,700 daily flights.

The second largest airline is Lufthansa (Germany). It was founded in 1926. In addition to its passenger activity, Lufthansa has other business units, such as logistics, catering (food), leisure travel (charter) and IT-service. Lufthansa is present in more than 85 countries, has 200 destinations and 1,700 daily flights.

The third airline is Ryanair (Ireland). It was founded in 1985 but in the beginning it was a normal scheduled private airline. In 1990, Ryanair became a real low-cost and a no-frills airline. In March 2007 Ryanair has 436 routes in 24 countries and 18 bases.

The fourth largest airline is the SAS Group (Scandinavia). SAS Airline was founded in 1946 as a flag-carrier but is currently a private airline as its competitors. In 2007, the SAS Group operates around 1,515 daily departures all over the world and has 164 routes.

The fifth airline is British Airways (United Kingdom). It is the UK's largest international scheduled airline; it operates around 550 destinations. The airline also carried 877,000 tones of cargo in 2006. British Airways was officially founded in 1972 but since 1924 the airline has existed (under the name of Imperial Airways). In 1972, BOAC (British Overseas Airways Corporation) and BEA (British European Airways) merged and from now on is famous under the name of British Airways. BA and Air France were the only two airlines which operated the supersonic aircraft: Concorde.

<table>
<thead>
<tr>
<th>Rank</th>
<th>Airlines</th>
<th>Passengers Carried (Millions)</th>
<th>Fleet size</th>
<th>Turnover (Billions €)</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>Air France/KLM</td>
<td>70</td>
<td>378</td>
<td>21.4</td>
</tr>
<tr>
<td>2</td>
<td>Lufthansa</td>
<td>53.4</td>
<td>534</td>
<td>19.85</td>
</tr>
<tr>
<td>3</td>
<td>Ryanair</td>
<td>42.5</td>
<td>120</td>
<td>1.693</td>
</tr>
<tr>
<td>4</td>
<td>SAS Group</td>
<td>38.6</td>
<td>301</td>
<td>6.6</td>
</tr>
<tr>
<td>5</td>
<td>British Airways</td>
<td>35.6</td>
<td>289</td>
<td>12.46</td>
</tr>
</tbody>
</table>

Table 11 - Total scheduled passengers carried in 2006, authors’ creation with available data collected.

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307 www.airfrance.com  
308 www.lufthansa.com  
309 www.ryanair.com  
310 www.scandinavian.net  
311 www.britishairways.com  
312 Annual Reports of Air France Group, Lufthansa, Ryanair, SAS Group, British Airways.
5.1.5 Strategic trends after deregulation

After EU deregulation it was clear that changes in strategy had to take place, like Kjell Wilsberg points: *The deregulations made it clear that a structural change in the business had to take place.* This implied that airlines had to make adaptations in order to face the new competitive environment: *The problems of the airline industry were structural. The traditional airlines had high cost level and low productivity – thus they had a big challenge to adapt to a deregulated industry*. European scheduled carriers copied strategies that were employed by USA airlines when the market was deregulated. One of these strategies to defend from an increase in competitors in the market was the restructuring of linear route systems (point-to-point and hub-to-hub) to hub-and-spoke systems, which was already a strategy implemented in EU. In the old continent, flag carriers had their routes centered in one only hub which was their capital. The dominance of their hubs was assured by market entry barriers that existed before deregulation. However, after deregulation flag carriers saw this protection removed and had to come with new strategies, which are still being implemented nowadays.

The first strategies airlines implemented were defensive moves to assure its dominance in its own territory. Examples of strategies preventing foreign carriers to buy airlines based on one’s home country can be found in UK where BA managed to buy Birmingham Executive Airlines through Maersk, in order to keep SAS far from UK. Other defensive strategies were bound to strengthen flag carrier’s dominance in its hub. This was done through acquiring other carriers or making them being dependent on them, like operating feeder services (to and from the hub) and regional routes (with small aircraft) or buying stakes of smaller airlines. Examples of this lock-in and marginalization strategy can be found in Air France which contracted TAT and Brit Air to operate services on its behalf.

Expansionist strategies include cross-border acquisitions within EU and USA and joining or creating alliances. The first one was possible after the third-package and constituted a quick way to enter in foreign markets. BA acquisition of Delta Air (a German regional carrier later on named Deutsche BA), and its acquirement of a 25% shareholding in USAir were movements to enter in the German and American domestic markets. The second example is aimed to access to global markets via cooperation. Examples of global alliances are the creation of Star Alliance in 1997 and Skyteam and Oneworld in 1999. Later on in this chapter we will explain more these alliances. However, these mergers pose challenges to the companies, like Dan Lundvall argues: *Airlines own other airlines but they keep part of the structure intact because of the local differences in business culture. If you look at other companies you have a local base. The goal is to have the best synergy possible.*

Airlines also created strategies aimed to get a competitive advantage. As we’ve already explained in the end of the previous chapter, these strategies include cost slashing and differentiation. Cost slashing, has been one of the most popular strategies airlines have been implementing to stay competitive. For instance, the Irish flag carrier Aer Lingus had to reformulate its strategy due to an increase in competition in its market (especially because of Ryanair) and

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313 Interview with Kjell Wilsberg, p.1
315 Ibid, pp. 500-501
316 Ibid, pp. 501-502
317 Interview with Dan Lundvall, p. 12
became a low cost carrier\textsuperscript{318}. BA started cutting massively its costs since 9/11 and its business plan for the next years has included cost control and cost savings\textsuperscript{319}. Differentiation strategy in airlines can be seen notably in their high-quality service focus. For instance, BA business plan for next years includes a focus on its long haul premium classes and customer service\textsuperscript{320}.

Flag carriers in Europe tried to shield attacks from LCC and created subsidiaries. For instance, BA created Go, KLM created Buzz, SAS created Snowflake. However, as Moutinho points, “DNA from mother company flowed inevitably to these new companies, hindering their strategic independence and new management”\textsuperscript{321}. However these plans failed in these three subsidiaries were bought by LCC (GO was bought by Easyjet and Buzz by Ryanair) or were abandoned by the mother company (like SAS with Snowflake). Since 1993, with the beginning of the European Single Market, airline franchisors and franchisees in Europe has grown. For instance, BA has several franchisees like (British Mediterranean, CityFlyer Express, Maersk Air UK), Air France (Brit Air, CityJet), Lufthansa (Cimber Air, Augsburg Airlines), Iberia (Air Nostrum), etc. Franchising is a strategy that benefits both franchisors and franchisees and the consumers. However in smaller European markets franchising can discourage new entry since routes are not big enough to sustain many competitors\textsuperscript{322}. All of these behaviors are examples of corporate entrepreneurship, specifically the creation of organization inside an organization.

Smaller airlines and also low cost carriers have, in the recent years, joined already global alliances or created associations to protect their interests. For instance, the European Regions Airline Association (ERAA) founded in 1980, is constituted by 70 airlines that in total transport around 70 million passengers per year\textsuperscript{323}. Low cost companies established in 2003 The European Low Fares Airline Association to represent the low fare sector in legislative decisions, to protect their interests and of their customers\textsuperscript{324}.

5.1.6 The three main Alliances

Airline alliances, another clear example of corporate entrepreneurship, are more and more ‘trendy’ nowadays and try to regroup airline all around the world. The objectives of these alliances are quite the same, to reduce costs and to increase customers’ satisfaction. In 2007, 75% of all airlines belong to one alliance. It could be either Star Alliance, SkyTeam or Oneworld.

Star Alliance

Star Alliance is the biggest airline alliance in the world. Its motto is: “An alliance for all the right reasons”\textsuperscript{325}. It was created on May 14th 1997 after the agreement of five major international airlines which are Air Canada, Lufthansa, SAS, Thai Airways and United Airlines. Since 1992, agreement had always been set between airlines geographically close like Air Canada and United Airlines.

\textsuperscript{318} Barrett, S. (2006) \textit{Commercialising a National Airline – the Aer Lingus Case Study}, Journal of Air Transport Management, 12, pp. 165-167
\textsuperscript{319} British Airways 2005/2006 Annual Report and Accounts, p.10
\textsuperscript{320} Ibid
\textsuperscript{322} Denton, N. & Dennis, N. (2000) \textit{Airline Franchising in Europe: Benefits and Discounts to Airlines and Consumers}, Journal of Air Transport Management, 6, pp. 179-190
\textsuperscript{323} http://www.eraa.org/inside-era/aboutera/whatwedo.php#
\textsuperscript{324} http://www.elfaa.com/background.htm
\textsuperscript{325} http://www.staralliance.com/en/meta/star_alliance/index.html
This alliance enables airlines to share their networks, lounges at airports, check-in desks etc. Star Alliance wants to improve its customers’ satisfaction. In 2007, Star Alliance is composed by 17 members and 3 smaller regional members. Furthermore, two other Chinese members have planned to join the Alliance within 2007.

Star Alliance’s arguments to attract new airlines are:

- They offer a large network of carriers
- Star Alliance members can fly to more destinations than the other alliances with faster connections
- To offer the travel experience smoother for customers
- They gather members within the airport, coordinate schedules

<table>
<thead>
<tr>
<th>Members</th>
<th>Date of entry</th>
</tr>
</thead>
<tbody>
<tr>
<td>Air Canada</td>
<td>May 1997</td>
</tr>
<tr>
<td>Lufthansa</td>
<td>May 1997</td>
</tr>
<tr>
<td>SAS</td>
<td>May 1997</td>
</tr>
<tr>
<td>Thai Airways</td>
<td>May 1997</td>
</tr>
<tr>
<td>United Airlines</td>
<td>May 1997</td>
</tr>
<tr>
<td>Australian Airlines</td>
<td>March 1999</td>
</tr>
<tr>
<td>Air New Zealand</td>
<td>March 1999</td>
</tr>
<tr>
<td>ANA</td>
<td>October 1999</td>
</tr>
<tr>
<td>Singapore Airlines</td>
<td>April 2000</td>
</tr>
<tr>
<td>British Midland</td>
<td>June 2000</td>
</tr>
<tr>
<td>Asiana Airlines</td>
<td>March 2003</td>
</tr>
<tr>
<td>Spanair</td>
<td>April 2003</td>
</tr>
<tr>
<td>LOT Polish Airlines</td>
<td>October 2003</td>
</tr>
<tr>
<td>US Airways</td>
<td>May 2004</td>
</tr>
<tr>
<td>TAP</td>
<td>March 2005</td>
</tr>
<tr>
<td>Swiss</td>
<td>April 2006</td>
</tr>
<tr>
<td>SAA</td>
<td>2006</td>
</tr>
</tbody>
</table>

Table 12 - Members of Star Alliance

Thanks to the Star Alliance network, passengers are offered more than 16,000 daily flights to 855 destinations in 155 countries.

Sky Team

The second biggest airline alliance is SkyTeam. Its motto is: “Caring more about you”. SkyTeam was created in June 22nd 1999 after the agreement of two major international carriers, Air France and Delta Airlines, on long-term strategic developments. Once again, like Star Alliance, it provides more flexibility to passengers around the world.

Sky Team’s arguments to attract new airlines are:

328 http://www.skyteam.com/skyteam
You can earn more miles
There are more lounges
You are more guaranteed reservations
There are more flights
The range of fares is wider
There are easier connections
There is an easier and enhancer check-in
The quality is high
The reservation network is large

<table>
<thead>
<tr>
<th>Members</th>
</tr>
</thead>
<tbody>
<tr>
<td>Aeroflot</td>
</tr>
<tr>
<td>Aeromexico</td>
</tr>
<tr>
<td>Air France/KLM</td>
</tr>
<tr>
<td>Alitalia</td>
</tr>
<tr>
<td>Continental Airlines</td>
</tr>
<tr>
<td>Czech Airlines</td>
</tr>
<tr>
<td>Delta</td>
</tr>
<tr>
<td>Korean Air</td>
</tr>
<tr>
<td>Norwest Airlines</td>
</tr>
</tbody>
</table>

Thanks to the SkyTeam network, passengers are offered 14,615 daily flights to 728 destinations in 149 countries.

Oneworld

The third biggest airline alliance is Oneworld. Its motto is: “Oneworld revolves around you”. Oneworld was created in February 1st 1999 after the willingness of international carriers, American Airlines, British Airways, Cathay Pacific, Canadian Airlines and Quantas. But since 1998, these airlines had the idea to gather in an alliance.

Oneworld’s arguments to attract new airlines are:

- There are more people to support you
- You can get greater Rewards if you are frequent flyers
- Your transfers are smoother
- Oneworld has more value
- You have access to many lounges

<table>
<thead>
<tr>
<th>Members</th>
</tr>
</thead>
<tbody>
<tr>
<td>American Airlines</td>
</tr>
<tr>
<td>British Airways</td>
</tr>
<tr>
<td>Cathay Pacific</td>
</tr>
<tr>
<td>Finnair</td>
</tr>
<tr>
<td>Iberia</td>
</tr>
<tr>
<td>Japan Airlines</td>
</tr>
<tr>
<td>LAN</td>
</tr>
</tbody>
</table>

330 http://www.oneworld.com/ow/FFP-oneworld-benefits
Chapter 5  
Empirical Data Presentation

| Malévé | Qantas | Royal Jordanian |

The Oneworld network employs 265,000 people in 150 countries in almost 700 destinations around the world.

To summarize this part concerning the airlines alliances, we can say that there is a fierce competition between the three alliances. All of them want to offer the best service to their passengers in order to make easier their travels and connections. They all existed before the events of New-York in 2001 and chances are that many airlines would not have gone bankrupt if they had been gathered in Alliance. Alliances enable airlines to be stronger in order to face economic downturns; they reduce costs and increase customers’ satisfaction to be more competitive.

5.1.7 Future and Challenges of European Airline Industry

Consolidation in the market and the consequent emergence of three or four major carriers seems to be the trend in European airline industry. Academics, airline managers and people inside the industry agree upon this. Kjell Wilsberg, regarding airline ownership argues there will be less state ownership, more international ownership and airline as an investment object for shorter or longer periods and there will be mergers. Button points the regulatory changes as the main responsible for consolidation (as mergers and alliances), mainly amongst the full services airlines. Further mergers will also depend on legal frameworks outside EU. Dan Lundvall has a similar argument and says EU policies to strengthen Europe position in the world will have a future impact on mergers: I think there’s a political driving within the Commission which is trying to get European actors that are not ethnic based. For instance, Air France is a company for French to travel abroad, SAS is a company for Scandinavian to travel abroad. If you go outside the country no one knows about your national airline. They have no market presence. Besides legal and political driving forces, Dan Lundvall points an economic driving force that will shape the European airline industry: Creating strong economic airlines will lower the overall cost because they are cost synergies for large airlines, especially on the overhead side. And they will be financially very strong. However he argues the consumers, at this point, do not have still an important role in shaping the future of the industry: I think the consumers know very little about airline. (…)But I don’t think the consumers are not bound for certain airlines. It’s like shopping cars - some people buy different brands others buy the same car along their life. Airline it’s a commodity product nowadays. (…) I don’t think there’s a consumer drive to have a market fragmentation. They like to have strong companies that give them a good value for money. Also Kjell Wilsberg agrees with Dan Lundvall that airlines have become a community product, special on certain routes: Air transport on short and middle distances has become a commodity.

Regarding strong airlines, Button says the process of consolidation will be based around the largest carriers – Lufthansa, Air France/KLM and British Airways. Michael O’Leary agrees in

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331 Interview with Kjell Wilsberg, p.3  
333 Interview with Dan Lundvall, pp.11-12  
334 Ibid, p.12  
335 Ibid  
336 Interview with Kjell Wilsberg, p. 1  
part with this view and puts Ryanair in the top of the industry: *The industry in Europe is moving in the direction of three large connecting airlines: the BA family, the Air France family and the Lufthansa family and there will be one large successful low-fares and that’s Ryanair. In a couple of years’ time we will be by any calculation the largest airline in Europe*.\(^{338}\). Dan Lundvall is not sure about BA leadership in the future: *There are opportunities to do things because at the end of the day there will be only two big airlines to become major airlines and that’s Air France and Lufthansa. BA is an island airline and they tried so many times to go through and they failed all the time*\(^{339}\).

However airline industry in Europe will not be constituted only with big flag carriers. There will be more new comers in the airline industry as Tim Jeans (managing director of Monarch): *It’s a very easy business to get into. So will there be new entrants? Yes. Will there be room for them? Yes. Will there be causalities? Inevitably, because that’s what happens in a deregulated market. It will be interesting to see which of the new entrants stay the course*\(^{340}\). The low barriers to entry and to exit are also, according to Dan Lundvall, a reason for states not to own airlines: *You can start an airline tomorrow, but the barriers to entry and exit are really low. Aircraft are already available, they are international, so there’re no reasons for states to own airlines today. If a state loses its airline today and decides it wants to secure airline transportation they can only set up easily an airline tomorrow*\(^{341}\). This fact along with the airline privatization trends that are going in Europe (as we’ve already mentioned) shows that airlines can get rid of their political tight and historical legacies and become fully market-oriented. IATA points a need to be more efficient in the future: *The key factor for a successful strategic response is for a firm to recognize where its competitive advantage lies and to focus on it. Liberalization provides opportunities for expanding into new markets as well as threats to existing markets. There will be winners and losers from liberalization. However, experience from the other industries has shown that firms who are efficient, flexible and responsive to customer needs – regardless of their size – are best placed to benefit*\(^{342}\).

Despite of seeking to be more effective, there are some anticompetitive issues EU regulation should solve in order to promote an effective liberal competitive environment, opportunities for entrepreneurs that want to create their own airlines and destroy the previous equilibrium in the market. Fridstrøm, L. et al point some issues EU should take into account in order to attain a more vigorous competitive policy in the aviation market: treat alliances and mergers with the same rigor, increase contestability to constrain abuse of dominant position, control predatory pricing, remove grandfather rights and create an open market for slots through blind bidding in periodic auctions, multilateral restrictions on the use of FFPs, limit corporate discount schemes, close control with the way CRS are used, have e-ticketing based on open standards, control anti-competitive travel agent agreements that favor some airlines, control state aid, make sure ground handling firms ensure the minimum standards and have non-discriminatory taxation system\(^{343}\). Kjell Wilsberg argues new trends of airline regulation will concern consumer rights since they have become a main political target within EU and consumer rights as a result of irregularities result in higher compensation than ticket value in many cases\(^{344}\).

**Button points some concerns with the ability of European airline industry to generate enough revenues to attract long-term investment. Since air transport industry is approaching a level**

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\(^{339}\) Interview with Dan Lundvall, p.15


\(^{341}\) Interview with Dan Lundvall, p.12

\(^{342}\) IATA Economics Briefing Nº7 (April 2007) - Airline Liberalization, p.34

\(^{343}\) Fridstrøm, L. et al, *Towards a More Vigorous Competition Policy in Relation to the Aviation Market*, Journal of Air Transport Management, 10, p. 73-77

\(^{344}\) Interview with Kjell Wilsberg, p.3
of maturity, he argues, this will pose problems for airlines to obtain investments. To achieve this, it will be important to be sustainable, which implies to solve the cost recovery problem through the correction of the value chain and the full recovering of costs\textsuperscript{345}. Kjell Wilsberg is also aware of the challenge of cost reduction: The challenge for the network airlines is to reduce the cost gap as much as possible, keep the advantages of the hub/spoke system and still serve the passenger segments that are willing to pay for extra service, and give value for money\textsuperscript{346}.

The success of these measures will depend from future regulation policies from EU and from national governments to correct market failures in the value chain, to remove the legal factors inherited from previous public ownership, to solve the problem of lack of slots in hubs (which is according to Mats Valinger the main hindering factor of the deregulation)\textsuperscript{347} and also to promote further liberalization with other continents. Giovanni Bisignani, CEO of IATA, points a need for further liberalization in order to achieve sustainability in the industry: Further liberalization of international air transport is essential. Airlines facilitate global travel but are among the last companies to benefit from globalization. Greater commercial freedom for airlines is vital for the long-term health of the industry and for the global economy\textsuperscript{348}.

Apart from challenges, there are also opportunities. Airlines can see in those challenges opportunities for institutional entrepreneurship action – that is moved by their new interests (reach efficiency and maximizing profits) they can change the previous institutional design inherited from public ownership and break the remain regulatory barriers in EU. For instance, Dan Lundvall points new airlines are given advantages when they start new routes, that is an entrepreneurial behavior (introduction of a new service and opening of a new market): The only exception [to price discrimination in airport taxes and fees] is if you start a route that is not flown by anybody else you are allowed to be given incentives for a limited number of years\textsuperscript{349}. Those programs can last 5 years where we give discount in a number of fees when they introduce a new route. Also entrepreneurial and innovative behavior are needed so airlines can overcome the new market pressures that push fares down to marginal costs (and thus give them low margins) and to make sure their value chain generates revenues to attract investment. Also the trend towards liberalization expect that in the near future all bilateral agreements done by EU members will be replaced by a common set of community agreements, which will provide non-discriminatory open skies agreements with non-EU states\textsuperscript{350}. This trends, will provide entrepreneurs with opportunities to create new services (new routes between EU and non-EU countries), introduce new methods of production (exporting the no-frills concept), opening new markets (targeting business and young people from non-EU countries to business and economic classes respectively), conquest new sources of supply (dominate regional and secondary airports in non-EU countries) and carrying the industry in other way (opportunities to consolidation through mergers with non-EU carriers).

### 5.2 The SAS Group (Scandinavian Airline System)

Now we will introduce our empirical data on the SAS Group. We will start by presenting the entire SAS Group and then we will continue with only data on the SAS Airline in order to compare it with Ryanair.

\begin{itemize}
  \item \textsuperscript{346} Interview with Kjell Wilsberg, p.3
  \item \textsuperscript{347} Interview with Mats Valinger, p.2
  \item \textsuperscript{348} IATA Economics Briefing Nº7 (April 2007) - Airline Liberalization, p.3
  \item \textsuperscript{349} Interview with Dan Lundvall, p. 8
  \item \textsuperscript{350} Fridstrøm, L. et al, Towards a More Vigorous Competition Policy in Relation to the Aviation Market, Journal of Air Transport Management, 10, p. 73
\end{itemize}
5.2.1 Introduction of the SAS Group and history of SAS Airline

The SAS Group gathers different airlines such as the largest airline in the group, SAS, which was founded in 1946 as a consortium gathering three national airlines: DDL a Danish airline company founded in 1918; ABA a Swedish airline company founded in 1924 and DNL a Norwegian airline company.

On August 1st 1946, these three airlines founded SAS in order to form a partnership to handle intercontinental flights to Scandinavia. Per A. Norlin was the first entrepreneurial CEO of SAS. Today SAS is still one of the only multinational airlines (MNCs) in the whole airline industry. It is owned by the Swedish (21.4%), by the Norwegian (14.3%) and by the Danish (14.3%) States. These States own 50% of SAS, the other 50% of the ownership are divided between insurance and investments companies but also banks.

The SAS Group own different companies, however SAS Airline still remains the biggest airline of the group which represents approximately 60% of the total turnover. Moreover, the SAS Group has different subsidiaries and affiliated airlines which represent 25% of the total turnover and it is also present in the freight (cargo) with around 12% of the total turnover and its remaining activities represent the rest of the turnover.

<table>
<thead>
<tr>
<th>Shareholder</th>
<th>Ownership</th>
</tr>
</thead>
<tbody>
<tr>
<td>The Swedish Gov.</td>
<td>21.4%</td>
</tr>
<tr>
<td>The Danish Gov.</td>
<td>14.3%</td>
</tr>
<tr>
<td>The Norwegian Gov.</td>
<td>14.3%</td>
</tr>
<tr>
<td>Wallenberg Foundations</td>
<td>7.4%</td>
</tr>
<tr>
<td>SEB Founder</td>
<td>2.2%</td>
</tr>
<tr>
<td>National Bank of Denmark</td>
<td>1.4%</td>
</tr>
<tr>
<td>Handelsbankenfunds</td>
<td>1.1%</td>
</tr>
<tr>
<td>State of New Jersey</td>
<td>0.9%</td>
</tr>
<tr>
<td>Första AP-fonden</td>
<td>0.9%</td>
</tr>
<tr>
<td>Robur</td>
<td>0.8%</td>
</tr>
<tr>
<td>Folksam</td>
<td>0.8%</td>
</tr>
<tr>
<td>Others</td>
<td>34.7%</td>
</tr>
</tbody>
</table>

Figure 14 - Composition of SAS' shares

Figure 13 - Focus on the SAS Group 2007 Report and Summary

352 SAS Group Annual Report
353 Ibid
354 Ibid
In 2007, the SAS Group operates around 1,515 daily departures all over the world and has 164 routes and transported 38.6 millions passengers in 2006 with a turnover of 6.6 billions euros. Furthermore, the Group owns 301 aircraft and is the fourth largest airline group in Europe.

The SAS Group is, as you can see hereunder, divided into five different business areas: SAS Airline, Subsidiary, such as the charter airline Spanair, and Affiliated Airlines, Airline Support Businesses, Airline Related Businesses and Hotels.

Figure 15 - The SAS Group's airlines

Figure 16 - The SAS Group structure and its business areas

355 Focus on the SAS Group 2007 Report and Summary
356 www.scandinavian.net
357 Ibid
5.2.2 The SAS Group’s business concept, vision and values

The business concept of the SAS Group is to “serve Europe with air travel” with a hub in Northern Europe. According to the SAS Annual Report 2006 the vision of SAS is to be “the preferred choice”. Concerning its values, SAS Group’s goals are to achieve:

- Consideration: they care about their customers and employees and want to respect their social and environmental responsibilities.
- Reliability: they want to be considered as a safe, trustworthy and consistent airline company.
- Value creation: they want to a professional businesslike approach with innovation
- Openness: they want to be open and have an honest management for their stakeholders.

5.2.3 The SAS Group’s objectives and strategies

Over the last decade, the airline industry has faced three ‘packages’ of deregulation, which have helped but also weaken the industry. One of SAS Group’s objectives is to remain stable and to face as well as it can its evolving market, especially after September 11th 2001 and the oil crises. SAS wants to increase its market capitalization thanks to a strong and regular growth and high profitability. SAS Group’s targets for 2007 are currently being set at the top level of SAS, however in 2006 they were:

- Profitability: to reach a CFROI (Cash Flow Return On Investment) of at least 20% over a business cycle.
- Products: make easier the purchase its products with a good perceived value and to meet customer’s expectations.
- Market position: its goal is to be one of the leading airline groups within Europe (it is fourth largest airline Group currently).
- Financial stability: its target is to main a good equity/assets ratio with low debts.
- Flight safety: to improve safety thanks to technical improvements

Concerning the strategies they want to implement, the SAS Group focuses on four main strategies which could be summarized like this:

- Commercial excellence
- Continued cost improvement
- Optimization of production
- Development of organization

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358 The SAS Group Report and Summary 2007, p.4
359 SAS Annual Report, 2006, p. 8
360 Ibid
361 Ibid
362 The SAS Group Report and Summary 2007, p.6
Moreover, the SAS Group aims to build up long-term developments, such as a strategic agreement between SAS Airline and the other airlines within the SAS Group. In the summary of the SAS Group published in 2002, this strategy was already fundamental in order to survive in “the present deep crises in the industry”\(^{363}\). SAS Group has, since 2002, been aware of the importance of internal cooperation or strategic alliances to cope with the fluctuation in the airline industry.

The SAS Group has also a sustainable policy concerning its development, financial growth, environmental improvements and social responsibility.

5.2.4 The SAS Group’s routes

The SAS Group has its headquarters is Scandinavia; however the company develops its routes on the European market as well. Currently, the SAS Group’s turnover comes from approximately 85.4% of non-intercontinental flights. Among these 85.4%, 41% were achieved with flights to European countries, 30.1% thanks to domestic (e.g. Stockholm-Umeå) and 14.3 % with Intra-Scandinavian flights (e.g. Stockholm-Copenhagen). Finally, 14.6 % of the passenger revenue is realized on pure intercontinental flights (e.g. Stockholm-New York).

The SAS Group is the leader on the Scandinavian with 90% market shares. Concerning the domestic markets in Sweden, Norway and Denmark, it reaches market shares of 80 %, 97 % and 89 % respectively. In spite of its leadership in Scandinavian, the SAS Group has to deal with a tough competition or well-positioned competitors like Flynnordic or Malmö Aviation\(^{364}\). (Appendix 1)

Hereunder, you can see the market share of the SAS Group within or outside Europe.

![Figure 17 - The Market Share of the SAS Group\(^{365}\)](http://www.scandinavian.net/12208/Pressmeeting_Hamburg2002.pdf)

5.2.5 SAS Airline (Scandinavian Airline System)

After having introduced the SAS Group, we would like to introduce our empirical data on SAS Airline before comparing it with Ryanair. As we have previously evoked in chapter 5.2.1, SAS Airline was founded in 1946 as a consortium gathering three national airlines: DDL a Danish airline company founded in 1918; ABA a Swedish airline company founded in 1924 and DNL a Norwegian airline company. It is impossible to explain and present the whole history of SAS Airline; however we want to give the major events of its development since 1992, three years before the period when Ryanair became the first LCC in Europe.

\(^{363}\) SAS Group in Summary 2001/2002, p. 6  
\(^{364}\) Interview with Mr. Mats Valinger, Vice President Corporate Development from the SAS Group  
\(^{365}\) www.scandinavian.net/12208/Pressmeeting_Hamburg2002.pdf
In 1992, SAS Airlines decided to grab many market shares in Europe and changed partly the normal fares way and introduced a specific fares called “Jackpot” and the EuroBonus program which still enables frequent flyers to earn points (miles). 1992 was also the year of the last deregulation in Sweden. The history and the strategies of SAS were totally modified by the new changes but we will talk about that in the following parts (Chapter 5.2.8).

On May 1997, SAS airline became a member of the Star Alliance which helped it to develop drastically its destinations but also improved the service offered for its passengers (Chapter 5.1.6).

In 2001, SAS Airline was on the ‘good track’ and continued its expansion and foresaw to reach a passenger volume of 35 million by 2005. In the same time, SAS’ board of directors wanted to increase by 50% the size of the airline by a recruitment policy, which consisted in hiring five thousand new employees. The year 2001 started very well until the events in September of this year. All over the world airline revenues shrank like ‘butter in the sun’ and SAS Airline as well. The scenario got even worse on October 8th when a SAS aircraft crashed into another aircraft during taking off in Milan (Italy). It has been the worst tragedy in SAS’ history. In 2001, SAS had experienced its most difficult period since its creation. There was only one solution to solve this problem; to make severe cost reductions. SAS wanted to become larger but the opposite happened, the airline had to lay off many employees and SAS had to think about a new organizational structure. Despite these difficult moments, it had to cope with the situation and had the objective to reduce the impact on its customers; SAS innovated and launched internet check-in and electronic tickets.

In 2003, SAS Airline continued its cost reductions to improve its efficiency and was divided into three regional bases: Denmark, Norway and Sweden. The competition became harder and harder, so in March 2003, SAS launched its own low-fare concept: Snowflake (Chapter 5.3.2)

On March 2005, SAS Airline launched its new concept within Sweden: one-way fares and flexible tickets. In autumn 2005 and seeing that this concept was a success, it decided to spread the concept on European routes.

These new concepts were very beneficial to SAS and it was in a better commercial situation than three years earlier. It was also the first airline which introduced ‘wireless high-speed internet’ on its intercontinental fleet. You can continue working while flying…

### 5.2.6 Figures of SAS Airline

<table>
<thead>
<tr>
<th>Number of aircraft</th>
<th>191</th>
</tr>
</thead>
<tbody>
<tr>
<td>Aircraft types</td>
<td>B767-300ER, B737-600/700/800, A340-400, A321-300, MD81/82/83/87/90, SAAB 2000, Q400, Fokker 50</td>
</tr>
<tr>
<td>Hubs</td>
<td>Copenhagen, Oslo, Stockholm</td>
</tr>
<tr>
<td>Number of employees</td>
<td>8,242</td>
</tr>
<tr>
<td>Passengers per year</td>
<td>23.8 million</td>
</tr>
<tr>
<td>Sales revenue</td>
<td>US$ 4.86 billion</td>
</tr>
<tr>
<td>Frequent flyer program</td>
<td>SAS EuroBonus (Gold, Silver, Blue)</td>
</tr>
<tr>
<td>Number of destinations</td>
<td>109</td>
</tr>
<tr>
<td></td>
<td>More than 750 daily flights covering</td>
</tr>
</tbody>
</table>

5.2.7 Objectives of SAS Airline

The main target of the SAS Airline is to become the leader airline in Scandinavia on three major traffic flows: to Scandinavia, from Scandinavia and within Scandinavia. In other words, it means to have the biggest market share on the domestic market, on local markets and with the rest of the world.

In the same time, SAS’ objectives are the same as ones of the SAS Group. They consist on the frequent renewal of its fleet in order to keep on offering the best comfort and silence to its passengers; a financial stability, quality, human resource and environmental targets.

The SAS Group has invested a lot from 1998 and 2004 for its investment program to renew its aircraft fleet, especially for SAS Airline with a total amount of 36 billion SEK. Among these investments, SAS Airline placed orders for both Boeing and Airbus aircraft (Boeing 737s, Airbus A340 & 330-300s and Airbus A 321). SAS Airline knows no purchasing pressure when it chooses its aircraft like it used to happen with flag-carriers when they had to purchase aircraft from their country or region (e.g. Boeing for American airlines and Airbus for French or European airlines). Aircraft are chosen according the route, their fuel efficiencies, their comfort…

Currently, the SAS Airlines’ capital expenditures are fewer because it is a period of low investments but the expenses are mainly due to spare parts and other operational investments.

Concerning its financial targets, SAS Airline’s objective is to increase its operating revenue by an average of 5% per year and hopes to achieve a minimum CFROI of 17% over the years to come. In order to achieve its CFROI target, SAS Airline wants to reduce its production costs. It will be achieved by:

- A better utilization of aircraft and capacity (on improving the average seat load factor)
- Increasing hours for pilots from 7.5 to 9 hours
- Rising working hours from 490 to 600 hours for pilots on an annual basis
- Rising working hours from 540 to 600 hours for cabin crew staff
- Decreasing in aircraft and crew overnight stays
- A new aircraft configuration with more seats
- A reduction in ground service
- Improvements in aircraft rotation by improved point to point rotation from 40 to 90 %

SAS Airline focuses also on meeting its customer expectations; it has created and is using a CSI (Customer Satisfaction Index). This index does not only reflect the level of satisfaction of its passengers but it also shows the rank of SAS in relation to the best airline. The airline had an

Table 13 - Key figures of SAS Airline

| Network strengths | Scandinavia and Finland, the Baltic, Europe including central and eastern Europe, Russia, Asia and USA |

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368 The SAS Group Report and Summary 2007, p.28
369 Ibid
average of 75 points over the last years. It is harder and harder to meet customer expectations in the airline industry and an example of the outcome of the index was to improve the service on board or the frequent flyer card (Eurobonus). According the SAS Group Annual Report, the key factors for increasing customer satisfaction are “image, customer treatment, timetable/route network and punctuality”.

Punctuality and regularity are also objectives of SAS. The airline wants to be the “Europe’s most punctual airline”. Punctuality for a take-off and a landing within 15 minutes reached 78.1%; nevertheless the target of SAS for punctuality has to reach an average of 90%.

SAS Airline has also an objective on the environment. The aim is to be ranked “among the airline industry leaders in adapting its operations to the environment and to make environmental management an integral part of the business management process”.

5.2.8 Strategies of SAS Airline

SAS Airline follows its own strategic direction, however belonging by the SAS Group, the airline has to set strategies which are coherent with the ones of SAS Group. So fare, it has set, before radical changes, these following strategies:

- Flight safety
- Punctuality
- Service

SAS Airline wants to offer the highest quality to its customers. This quality could be partly achieved by flight safety. The airline invests a lot of money on aircraft maintenance and different points where safety could be always improved to reduce for example incidents that occurred in 2006. SAS Airline improves also its quality by adjusting staffs according the size of the airport. For the punctuality, SAS Airline sets targets and aims to become in the years to come the most punctual airline in Europe, to increase its service level as well, such as the e-ticket, the lounges at the airport, frequent flyer card...

As we said previously, SAS Airline has its own strategies but it also takes advantages of the SAS Group, so it has a partnership. The goal is to improve the efficiency of its flights through benefits that it would not have if it had been alone.

In addition, as we have explained in chapter 5.1.6, SAS Airline was one of the founding members of Star Alliance in 1997 and this strategic alliance continues to be a ‘pillar’ of SAS strategies. Why not taking as many advantages as possible of this membership? SAS, thanks to the alliance, increased drastically the number of its passengers and consequently its turnover.

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371 www.scandinavian.net
372 The SAS Group Report and Summary 2007, p.34
373 Ibid
374 Ibid, p.35
375 Interview with Mats Valinger, p.2
376 The SAS Group Report and Summary 2007, p.18
377 Ibid
378 www.staralliance.com
Apart from this alliance, SAS Airline is Lufthansa’s most important partner in Europe, after that the European Commission approved a joint venture agreement between Scandinavia and Germany. They both are members of Star Alliance.

SAS Airline has also other airline partners in Europe, such as Iceland Air, Maersk Air or Estonian Air. SAS has a code sharing agreement with these airlines.

In addition, SAS Airline has a strategic interest in the Baltic airline market, so it has partnerships with a couple of regional airlines in Scandinavia. This strategy enables SAS to extent its regional route in Scandinavia, Finland and other Baltic countries. These partnerships are essential for SAS because the airline can propose these routes to its customers without using its own aircraft because they are not profitable enough. These partners are for instance AirBaltic, Cimber Air, Skyways Holding, Air Botnia and Widerøe's Flyveselskab. Thanks to them, fifty destinations in Scandinavia are not operated by SAS Airline but by its partners.

SAS Airline focuses on its distribution strategy as well. The airline wants to increase its competitiveness. SAS has to provide a service available at any time and from any place for its passengers. Moreover, the flight ticket sold on Internet (e-tickets) has known a ‘boom’. Passengers can, from now on, take tickets twenty four hours a day, seven days per week. The new electronic way to book your flight is quicker, makes easier the process and reduces distribution costs. However, does it strengthen customer relations? When you have a booking problem on Internet anybody is there to help you…We think that SAS has adopted a good method because it proposes various solutions:

- Electronic travel agencies or SAS retail stores: SAS Airline works with a number of electronic travel agencies, to reduce distribution costs and to raise revenues. SAS has around 400 retails stores in Scandinavia.

- SAS Direct (Call Centers): the objective is to provide a customer service support, whether for a booking or for any other questions.

- SAS’ website (www.scandinavian.net): the website offers customers self-service solutions (bookings, schedule, frequent flyer program, information on SAS…). It is likely and obvious that this distribution channel will know a strong growth in the future according the 2005’s and 2006’s figures.

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379 SAS Annual Report, 2001
381 The SAS Group Report and Summary 2007, p16
382 Ibid, p35
Another strategy of SAS Airline was to launch its own low-cost carriers on March 30th 2003. Its name was Snowflake. Eva-Karin Dahl, Director of Business and Concept Development, with responsibility for snowflake said that: “We have succeeded in combining the product’s simplicity with corresponding simplicity in production, which is a requirement for the low prices we offer.

We will go more in details concerning Snowflake in the SAS case study part 5.3.2 (Entrepreneurship and Innovation).

5.3 Ryanair Story

“Ryanair is more than an airline - is a phenomena.”

By Dan Lundvall

The second Irish airline is born – Ryanair from 1985-1990

“It was a bit like giving a license to an electricity supplier just to supply power to the city of Dublin or a postal service. It was picking the most profitable part of the Aer Lingus network.”

By David Kennedy (ex-CEO of Aer Lingus) commenting when the Department of Transport gave a license to Ryanair to operate in Dublin-London route, in “Ryanair – How a Small Irish Airline Conquered Europe” by Siobhán Creaton

Ryanair today could be called Irelandia if in 1980 Tony Ryan’s plans to create a no-frills, low fares scheduled transatlantic carrier had been accepted by the Irish Government. The experience he had from being working in the industry since the mid-60s, the dual Memoranda of European Commission on air transport liberalization in 1979 and 1984, the public dissatisfaction in Ireland with the performance of air transportation along with the failed attempt of Ryan’s start up airline led him to state prophetically that in the long, deregulation combined with competition is the only method by which the traveling public will enjoy low fares. Foreseeing possible changes in EU regulation within the next years, Ryan negotiated other proposals with the Irish Government.

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383 Ibid
386 Ibid, p. 8
until the Department of Transport accepted to give him the license for Ireland-UK routes. Ryanair was born in 28 November 1985 and its initial strategy was to design a low-cost base and no-frills outfit. Other innovative strategies for the time were that Ryanair had no booking restrictions like no need to make advance bookings, or to stay a Saturday night or no penalties for cancellations. In 1985 Ryanair began to operate charter flights to business and leisure travel groups between Waterford (close to Dublin) and Gatwick with a 15 seat airplane. Further success would come in May 1986 when the Department of Transport granted Ryanair a license to fly to London Luton, although with a restriction to operate with a maximum of a 44 aircraft seat on the route from Dublin, in order to protect Aer Lingus premier route. At this point a tough competition between Ryanair and Aer Lingus began. The price duel was the most evident battle between the two Irish carriers. On its first flight Ryanair set a fare of £99 on Dublin-London Luton route which was half of the £200 charged by Aer Lingus and BA. Aer Lingus immediately slashed its fares as low as £95 and Ryanair responded with a £94.99 fare. The opening of the route to the new entrant would start the first fare war in Europe that still prevails today. Along with the price war, the two Irish airlines began an advertising war to try to get customers.

During this start-up phase Ryanair was far from having a bright future. First, Ryanair strategy was not clear since Tony Ryan wanted to create a low cost and no frills airline but some of the policies practiced by the airline (like business class service, frequent flyer club, four different types of aircraft, serving drinks and selling duty-free during flights) present some contradictions. Second, it was operating in a broad network of unsustainable routes. Third, the battle against Aer Lingus and BA (on the route to London) was like David versus Goliath, not only for the size of both flag carriers but also because they were state-owned companies (BA was privatized in 1987) and thus they benefited from special advantages like regulatory capture. Fourth, there were its cheap and slow airplanes took the double of the time to go from Dublin to London than Aer Lingus and BA airplanes, technical problems caused flights to be suddenly cancelled, the reservation system was not working properly (furthermore it belong to BA), trade unions from Aer Lingus were lobbying the Government to deny any further routes to Ryanair. Fifth, there were political-legislative restrictions that led to some route modifications, like the route from Cork to Luton that had to include a further stop in Dublin. Due to these five factors, in 1989 Ryanair abandoned its business class, closed the Frequent Flyer Program and had large debts to Aer Riana, the owner of Dublin Airport. During the first four years it lost £20 million and by 1990 the airline was having negative results of £7 million a year. This situation is described by Michael O’Leary pessimism (that had been hired in 1988 as a financial director) as the follow: It will never make

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390 Ibid, pp. 19-20  
391 Ibid, pp. 23-24  
392 Ibid, pp. 20-21  
393 Ibid, p. 22  
394 Ibid, pp. 25-26  
395 Ibid, pp. 26-27  
396 Ibid, pp. 23-27  
400 Ibid, p. 31  
money. It will always lose money. It’s an airline. Forget it. However, better days were about to come.

Coming back to life – Ryanair from 1989 to 1992

“After O’Leary took control, gratitude played no part in Ryanair’s corporate policy. There was no level of support that would ever satisfy Ryanair.”

By An Aer Rianta source in “Ryanair – How a Small Irish Airline Conquered Europe” by Siobhán Creaton

By 1989 Ryanair was about to be shut, however Ryan persistence led the Minister of Transportation in September to grant his request to take routes from Aer Lingus and to give them to Ryanair. The Minister was convinced that Ireland should have two airlines policy. From this year, Ryanair was granted exclusive rights to fly from Ireland to London Stansted and London Luton, received rights to offer direct flights from Irish regional airports to the rest of Europe and got Aer Lingus rights to fly to Munich and Liverpool for three years. This decision was in line with the first package of EU Air Transportation deregulation. Another helping hand came from Aer Rianta who forgave the debt that Ryanair had, and allowed it to renegotiate deals in some airports, providing advantageous conditions for the airline.

By this time O’Leary was in command of the airline and began his cutting cost policy with negotiations with the Stansted airport (which in 1991 would become Ryanair main base). Like Terry Morgan, the director of the airport describes: Ryanair was given and still has a deal where it is given a discount off the full tariff mainly related to the volume of traffic it brings through. The fees were a sixth of the normal ones and were an incentive to open up new routes. During this time, similar advantageous arrangements were arranged in other airports. This cost cutting policy in other areas: workers saw pay cuts, flights were cancelled if the loads were low, flights were diverted to other Irish airports to pick up passengers bound to London, huge amount of money was saved for cash reserves and its route network was shaved back from 19 to 6.

In 1990 Ryan family put near £20 million into the airline and O’Leary went to USA to learn with Kelleher (CEO of Southwest Airlines) the low-cost model followed by Southwest Airlines: short point-to-point routes, scheduled flights at a low cost, secondary airports close to final destinations, 25 minutes turnaround, single type of aircraft, only economy class and no assigned seats. Back to Ireland, O’Leary decided Ryanair would follow Southwest model and to have a price-based competition: We decided to follow the kind of low-fares formula that Southwest Airlines had pioneered in the US. It seemed blindingly obvious that if we couldn’t out-service Aer Lingus with better business class and service, we could certainly offer better fares. But Ryanair would not only low their fares but would also try to achieve a cost leadership in the market like O’Leary was determined to do: Once we saw what Southwest was doing we though this could be the way forward: selling at the lowest possible price to the maximum number of people.

406 Ibid, pp. 44-47
407 Ibid, p. 49
408 Ibid, p. 53
409 Ibid
413 Ibid, pp. 56-66
414 Ibid, p. 89
The price war began again and the low-fares proved to be so successful that in 1992 Aer Lingus financial situation forced the airline to withdraw from routes in Ireland and to increase their fares, while for the first time British Airways had to move off a route as a result of direct competition.416 Besides the low fare and no frill service, Ryanair copied other characteristics of Southwest model: the airline bought used Boeing 737-200 (that would become Ryanair standard fleet), didn’t use air bridges, not offered interlining and not had lounges at airports.417 Michael O’Leary briefly describes this strategy: Our strategy is low fares, high capacity at busy times and flexible tickets418.

From 1989 to 1992 the number of passengers increased from 644,000 to 945,000, a 46.7% growth, and in 1991, despite of the harsh economic conditions due to the Gulf War, Ryanair made a profit for the first time419. However, the entire European airline industry was about to face a deep change with the open skies policy of the European Union Single Market that would come into force in 1993.

Flying in open skies: Ryanair from 1993 to 1996

“When the restrictions on airlines are lifted, short-haul, cost-efficient, point-to-point airlines will sprout up throughout Europe. They will in a short space of time, change the face of European air travel.”

By Michael O’Leary in “Ryanair – How a Small Irish Airline Conquered Europe” by Siobhán Creaton

The Single European Market (SEM) gave a handful of freedoms to airlines that were not possible (or that were restrained by regulation) until now. The access to all routes within EC (except of cabotage), freedom to set own fares, freedom to have unlimited number of flights and transporting a no-restricted number of passengers, are some of the examples of strategies that deregulation provided. Apart from this, European Commission (EC) introduced competition rules that benefited new entrants in the market, hindering the big airlines to perform predatory pricing and regulating the terms of state aid.420

Aer Lingus suffered the effects of competition rules when European Commission blocked its plans to set up Aer Lingus Express.421 Later on, O’Leary took advantage of competition rules to lodge complains to EC accusing Aer Lingus to abuse from its dominant position by practicing below-cost pricing and seat dumping to drive Ryanair off some routes. These complain led Aer Lingus to lose money and to change their strategies.422 However in November 1995 was Ryanair’s turn to face the effects of the airline regulatory framework when it was about to launch its first route within the UK between Stansted and Glasgow. Its British competitors invoked the anti-cabotage rule which implied that if Ryanair wanted to operate between two points in UK it had to set a separate British company, to apply for an airline operator’s certificate to operate and to have UK registered planes. However Glasgow airport managers pressured the UK Ministry of Transport and

419 http://www.ryanair.com/site/EN/about.php?page=About&sec=story
422 Ibid, p. 101
after days of negotiations Ryanair got a special dispensation however with restrictions in capacity.\textsuperscript{423}

Meanwhile, O’Leary continued its cost cutting policy, eliminating suppliers of on board service or making pressure to reduce costs and seeking discounts and advantageous conditions in Irish and British Airports.\textsuperscript{424} Ryanair was now a successful airline in Europe: it had become the first low fares airline to operate a domestic route in the UK and its number of passengers rose grew from 1.120.000 in 1993 to 2.950.000 in 1996, an impressive 260% growth in three years.\textsuperscript{425} The last step of deregulation was close and that would provide European airlines opportunities to establish new routes. To take advantage of this investment would be needed. This happened when in August 1996 Ryanair arranged a deal with David Bonderman (founder of Texas Pacific Group) to bring the airline to trade on the international markets.\textsuperscript{426}

Conquering Europe: Ryanair from 1996 to 2001

“Real new opportunities didn’t arrive before the end of last century. It was from 1996/1997 when the market started to change and new airlines tried to find new ways of working.” By Dan Lundvall, Marketing Director of LFV

In May 1997 Ryanair Holdings is established, buys Ryanair for £56.7 million and had successful flotation on the Dublin and NASDAQ Stock Exchanges.\textsuperscript{427} This enabled Ryanair in the following years to increase its fleet of Boeing 737-800 that, as O’Leary argued, will allow Ryanair to compete head-on and beat any low cost competition from Europe’s major airlines.\textsuperscript{429} The attractiveness of the European market was recognized by O’Leary: Continental Europe is a market with over 300 million people, most of whom are now paying outrageously high air fares. I assure you that this is a market that Ryanair cannot ignore.\textsuperscript{430} This expansion would be based on Southwest Airlines model which meant that Ryanair would attract passengers to fly to secondary airports close to major cities, offering low fares at the same time. This strategy would be complemented with special limited deals and promotions to its European destinations with the aim, as described by O’Leary, to re-emphasize Ryanair’s position as Europe’s low-fares carrier.\textsuperscript{431} O’Leary cleared stated: We don’t look upon ourselves as an Irish airline anymore. We look upon ourselves as a European airline.\textsuperscript{432}

Ryanair launches its first European routes from Dublin to Paris Beauvais and to Brussels Charleroi and from London Stansted to Oslo Torp and to Stockholm Skavsta.\textsuperscript{433} Later on, it launched more flights to other destinations in Italy, Belgium, France, Germany and Scandinavia, but this time only from Stansted due to the high fees charged by Dublin airport.\textsuperscript{434} The duel with Aer Rianta and the Irish Government to charge lower fares and to obtain a permission to build its own terminal went through several years, without success for the Irish company.\textsuperscript{435} The fact that Ryanair could not build its own terminal it’s a proof that the airport business was not a completely

\textsuperscript{423} Ibid, pp. 106-109
\textsuperscript{424} Ibid, pp. 98-102
\textsuperscript{425} http://www.ryanair.com/site/EN/about.php?page=About
\textsuperscript{427} Ibid
\textsuperscript{428} http://www.ryanair.com/site/EN/about.php?page=About
\textsuperscript{430} Ibid, p. 104
\textsuperscript{433} http://www.ryanair.com/site/EN/about.php?page=About
\textsuperscript{435} Ibid, pp. 190-193
deregulated business. In 2000 Ryanair opens a new base in Glasgow Prestwick and in 2001 it set up its first continental Europe base in Charleroi airport, a small airport that when Ryanair arrived was receiving 20,000 passengers per year.

O’Leary continued to pursue its low cost based policy and found new opportunities to do it in the reservation system and travel agents that by that time had an impressive power over the airlines (75% of Ryanair seats were sold by travel agents who booked them through CRS and in turn Ryanair was charged to use these systems and had to pay a fee to travel agents for every ticket they sold). Ryanair created Ryanair Direct (a call centre) to encourage customers to book their seats directly with the airline. Using again EC competition rules to complain about the travel agents which refused to sell Ryanair tickets, the airline was able to reduce the commission from 9% to 7.5%. The role of travel agents diminished even more when in August 1999 the airline created its website that allowed online booking. Besides enabling a save in the costs, the website was also used to sell travel insurance, accommodation and car hire.

Despite of this success, the application of the no-frills concept went too far and this generated a growing number of complaints simply because O’Leary had his own interpretation of Southwest Airlines model and ignored the concerns for customers. However, for O’Leary complaints regarding refund made no sense: We guarantee to give you the lowest airfare. You get a safe flight, You get a normally on-time flight. That’s the package. We don’t and won’t give you anything more on top of that. We care for our customers in the most fundamental way possible: we don’t screw them every time we fly them. Ryanair lost this battle and the airline was forced to say in which situations the refunds were available. However there were also complains regarding misleading information that was given by Ryanair on its advertisements: first, the company did not show how many flights were sold at the advertised price and how many seats were available for a specific fare on a specific flight; second Ryanair did not mention the exact final destination of their flights – some airports Ryanair was flying were 2 hours far from the announced destination, like the flights to Paris, Frankfurt and Stockholm which landed in Beauvais, Hahn and Nyköping. The complains rose but the number of passengers was still growing exponentially: in 1997, 3,730,000 passengers are a bit higher than an half of the 7,002,000 passengers carried three years after.

The low-cost empire: Ryanair from 2001 to 2006

“We are a small Irish company, out there stuffing it to the biggest airlines all over Europe, and of course that feels good.”

By Michael O’Leary in “Ryanair – How a Small Irish Airline Conquered Europe” by Siobhán Creaton

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436 Interview with Dan Lundvall, p. 9
437 http://www.ryanair.com/site/EN/about.php?page=About
440 Ibid, p. 182
441 Ibid, p. 184
442 Ibid, pp. 162-174
443 Ibid, p. 106
444 Ibid, p. 162
445 Ibid, p. 189
In the 2001 GO, a BA low-cost subsidiary that had been flying in some Ryanair routes from Ireland to UK had no other choice but to retreat due to Ryanair aggressive price war. When everything was over, Cassiani (GO CEO) told: We learned another crucial lesson about discounting. You can’t take on someone lower costs because they dig deeper than you to lower their prices and still make money while you’re bleeding. One year later, GO would be taken off by Easy Jet, the main Ryanair low cost rival.

After the tragedy of 9/11, the whole air transportation industry suffered a drawback and airline companies had to modify their strategies in order to adapt to the new situation that led to an increase in oil prices and a downturn in traffic. Ryanair, instead of cancelling thousands of flights, O’Leary said the company would adapt the opposite strategy: Other companies are grounding flights, laying off staff... We are going to fly our way out of this crisis. Our solution is to get back in the air with more passengers and lower fares. With thousands of flights cancelled and flag carriers like Swissair and Sabena in bankruptcy, the company took advantage of empty slots in the airports, which were until the date, according to Dan Lundvall, were the biggest constraint in European airports. In 2002 Ryanair opened a base in Hahn and ordered 80 airplanes from Boeing with options for more, taking advantage of a manufacturing industry that suddenly didn’t have any orders. Like O’ Leary said: the time to buy is when everybody else is selling and the time to sell is when everyone else is buying. By this year Ryanair copied the Southwest idea to advertise images in its aircraft to generate extra profits. Money also came from the Irish Government, which constitutes a contradiction for a company that had complained to national governments and to EC about the state aids that were being given to flag carriers like BA and Sabena. With money and its pocket and dozens of aircrafts on the way, Ryanair invaded the German market.

During the initial years in the German market, Lufthansa made several complains to the courts against Ryanair fares and advertisement but with no success. By this time, Ryanair had a 40% increase in its profits, a 26% profit margin and just needed to fill half of the seats on each flights to break even. In 2002 the company had its own terminal in Stansted that by the time was becoming too small to accommodate Ryanair expansion plans, like the airport CEO Terry Morgan noticed: Ryanair had a fleet acquisition plan which meant that it was going to be receiving aircraft knowing that only a limited number of them could be based here and that more would have to be based elsewhere in Europe. Apart from this restriction, in 2003 Ryanair continues its expansion plans taking over Buzz, a low-cost subsidiary from KLM that had start competing in some Ryanair routes in Scotland and was losing money. The main reason to acquire the company was the slots it had in some airports which Ryanair had interest.

In 2004 EU investigated the agreements in Charleroi airport and said it they gave Ryanair an advantage over its competitors and thus the company had to repay the money because the special

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449 Ibid, p. 204
450 Interview with Dan Lundvall, p. 3
452 Interview with Dan Lundvall, p.4
454 Ibid
455 Ibid, pp. 206-207
456 Ibid, pp. 208-209
457 Ibid, p. 213
459 Ibid, p. 222
460 Ibid, pp. 229-234, 244
conditions and the financial grants were declared incompatible with the EU Treaty. Flag carriers from Spain, France and Denmark made complaints about similar situations in their territories but there were no consequences for the airline. In the same year, Ryanair had to impose a wheelchair levy on every ticket due to the court action won by a group of disabled people and its shares fell down in Dublin stock market. In 2005 an EU new legislation that guarantees compensation to customer came into force (EU regulation 261/2004). There were down days and O’Leary admitted a defeat: we had been saying fares and margins would fall, what we didn’t foresee was that they would come down this bloody quickly. (...) It was inevitable that at some point in our history profits would stop accelerating. Apart from this, from 2001 to 2006 Ryanair passengers’ number rose from 9.355.000 to 42.500.000 and the company saw a growth in its profits.

From 2007 towards the future

“"The lowest-cost airline will always win, and that will always be Ryanair.””

By Michael O’Leary in “No Frills – The Truth behind the Low Cost Revolution in the Skies”, by Simon Calder

In three or five years time there will be one or two large low cost carriers in Europe. Ryanair will be one. The statement above was made by O’Leary in early 1998 and when looking at today’s situation, the Irishman prophetic words were correct. In March 2007 Ryanair was operating 134 aircraft (Boeing 737), has 436 routes in 24 countries and 18 bases. Bonderman (ex-Ryanair chairman) has a similar opinion about Ryanair bright future: There will be always minor players here or there because the nature of this business is that anyone with new airplanes can start a carrier and there are always surplus airplanes. But there will probably be two, maybe Ryanair and one other, that will survive as successful low-cost guys. O’Leary is sure about Easyjet success: Easyjet is fundamentally a good operation, except it’s not a low-fare operation. But it’s still very competitive with British Airways, Air France and Lufthansa, and I think they’ll do very well.

Despite of this optimism, Stelios, CEO of Easyjet (Ryanair main low-cost opponent), points a challenge for Ryanair business model: Flying from London to nowhere can work but flying from nowhere to nowhere is a challenge, particularly with large aircraft. Cassiani, ex-CEO of GO, points a weakness in Ryanair: Ryanair’s profitable, but they don’t have a good relationship with their people and they don’t have a good relationship with their customers. Other challenges came from the subsidies policy. Some of Ryanair’s competitors say that is not profitable to fly to remote airports without receiving state aid. The fact is not completely true - some these routes are not so profitable (or not profitable at all) and Ryanair uses its UK-Ireland routes to subsidize European

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462 Ibid, pp. 244-246
463 Ibid, pp. 235-236
464 Ibid, p. 237
465 Ibid, p. 247
466 Ibid p. 238
467 http://www.ryanair.com/site/EN/about.php?page=About
routes (UK-Ireland routes in 2003 and 2004 counted for around a third of total revenues\textsuperscript{474}). Despite Ryanair’s capacity to subsidize itself, we can not state that financial grants from governments are a helpful hand to the airline. For instance, in 2004 the French newspaper La Tribune said that in Ryanair’s 2002-2003 financial years the company benefited from 168 million euros, which corresponded to 70\% of its net annual profit\textsuperscript{475}. Regarding the advantageous conditions in airport charges provided by airports, Lundvall warns that this could come to an end: \textit{In the future if EU is successful in implementing its airport charges directive then all the airports would become price regulated and then would not be any difference if you are a private or a public airport}\textsuperscript{476}.

Apart from customers complaints, interrogations concerning state subsidies, O’Leary already has ambitious plans for the future: \textit{we’ll go to half-a-dozen new destinations each year, two new bases every five years, unless we do something stupid like have a crash or join an alliance}\textsuperscript{477}. To meet these plans, Ryanair has orders for more 117 aircraft to be delivered in the next 5 years. Apparently these plans will also follow the trend of airline consolidation in Europe, since Ryanair in November 2006 increased its Aer Lingus stake to 25.2\%, that it’s still waiting for EU Commission approval despite of Ryanair optimism\textsuperscript{478}. Ryanair pioneered an important change in air travel and made air travel affordable for everyone, which didn’t happen before when air travel was only accessible to an elite\textsuperscript{479}. Now the situation is different and O’Leary proudly says that \textit{Even the unemployed can afford to fly Ryanair} as he announces that in the future more seats will be offered for free\textsuperscript{480}. O’Leary is convinced of Ryanair success: \textit{We’re running the biggest, fastest-growing low-fares airline in Europe, revolutionizing air travel. (…) I am absolutely convinced that nothing will stop us, unless we screw it up ourselves through self-inflicted stupidity or arrogance}\textsuperscript{481}.

\begin{footnotesize}
\begin{enumerate}
\item Ibid, p. 257
\item Dobruszkes, F. (2006) \textit{An Analysis of European Low-Cost Airlines and Their Networks}, Journal of Transport Geography 14, p. 251
\item Interview with Dan Lundvall, p. 9
\item Interview with Dan Lundvall, p. 4
\end{enumerate}
\end{footnotesize}
6 Empirical Data Analysis

Chapter six will be the empirical Data Analysis on SAS and Ryanair. Afterwards, we will compare both business models.

“There are three kinds of companies, those that simply ask customers what they want and end up as perpetual followers; those that succeed – for a time – in pushing customers in directions they do not want to go; and those that lead customers where they want to go before customers know it themselves.”

By Hamel, G. and Prahalad, C.K.

6.1 SAS Analysis

6.1.1 Context and Industry Analysis

The airline industry in which SAS Airline evolves is much more fragmented than any another industry (telecom, electricity…). It is a large industry with a mass market where quite all services provided used to be standardized. Over the last years, all airlines companies were almost the same, there was few differences. They did not really care about competitors and did not develop strategies like differentiation. But these days are over and currently the airline industry is booming and changing rapidly, especially after the deregulation which has created entrepreneurial opportunities and changed in the environmental context.

The economic development of SAS Airline has always been more or less flourishing before the deregulation, in spite of some crisis (oil crises, incidents…). But since the events on September 2001 there have been an economic downturn with a worldwide recession. The number of passengers fell and many companies disappeared. The environmental context was highly fluctuating and was rather bad for the airline industry. Years were needed to come in again into the market. The deregulation, changes in the environmental context and new discoveries of entrepreneurial opportunities helped SAS Airline to become, today, one of the major, most respectful and prestigious airline in Europe.

Customers’ satisfaction

As we said in the part 5.1 (the European airline industry), services are mostly standardized the airline business. We are in a mass market. However, airlines have to find a ‘trick’ in order to differentiate themselves because “many companies have lost track of true needs of their passengers…” SAS Airline aims to meet their customers’ needs, which would lead to entrepreneurial opportunities recognitions, so the airlines has investigated into the concerns of their passengers and it has even monitor them to gather important information: observations. Why is it so important to provide the best service as possible? It is quite simple, having a high service quality enables to attract new customers and to keep them loyal and pleased. These new or actual passengers may become really profitable customers, so your service quality must be immaculate at

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484 Ibid
any time. Sometimes, it is essential to involve your customers in the opportunities recognition process in order to be sure that you are applying strategies or services that suit them.

SAS Airline used observations as a primary source of information concerning their passengers and especially when they were at the gate lounges in airports. The airline wondered what kind of new entrepreneurial opportunities they could provide. Lounges in airports are a quite good place to ‘dissect’ your passengers’ gestures and advices and especially the ‘wealthiest’ of them because lounges are only accessible by passengers having business or first class tickets or with a high level of frequent flyer card. This separation enables you to analyze your premium passengers and discover their needs, from the time they arrive at the airport and check-in until the time they leave your aircraft. SAS Airline tries to provide largest number of service variations than its competitors. The goal is to provide tailored-services to the passengers and SAS is highly determined to be the first mover on its market and to be a competitive airline in years to come.

To go further, SAS Airline has developed its own model to fulfill customers’ needs:

![SAS' model to understand how to fulfill its customers' basic needs](image)

Firstly in the first part, it is important for SAS Airline to fulfill the fundamentals needs of its customers; normally all airlines should behave in the same way, there is no new opportunities discovered. Then, the higher to go in the pyramid, the more opportunities you will find; for the activity support, opportunities offered to you are huge in order to fulfill customers’ needs. SAS Airline wants to help and support its passengers from the check-in until the landing (check-in, lounge, gate, onboard service and baggage claim). The top of the pyramid consists of the ‘tailored’ service or product support. Even here, SAS Airline is present to enable passengers to fly in the best comfort thanks to high quality services (first class tickets, Gold SAS EuroBonus…).

Concerning the changes and influences in the environmental context, we can give the example of the rules on February 2001 by the Swedish Market Court. It asked SAS to modify its frequent flyer program and stop giving points (miles) to its passengers flying within Sweden. It judged that it gave a leading position to SAS, which is an abuse of process. This new regulation must be applied within Sweden for SAS but also for regional agreement, where SAS is in competition with other airlines.

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486 Fridström, L. et al, *Towards a More Vigorous Competition Policy in Relation to the Aviation Market*, Journal of Air Transport Management, 10, p. 76
One year before, SAS experienced the same sanction but in Norway this time, by the Norwegian Competition Authority, on all domestic routes. Kjell Wilsberg (Director of Government Relations of SAS Braathens) regarding this argues this hinders company’s strategies: “This is negative for SAS Norge only, in the company’s competitive position towards foreign network carriers which are allowed to use their frequent flyer programs unrestricted both in their home market and on their service to/from Norway”.\footnote{Interview with Kjell Wilsberg, p. 1}

The consequence of this endorsement had a big influence because one month after, a new competitor arrived on the market and opened twelve domestic and five international routes\footnote{Fridstrøm, L. et al, Towards a More Vigorous Competition Policy in Relation to the Aviation Market, Journal of Air Transport Management, 10, p. 76}.\footnote{http://www.airbaltic.com/public/26557.html}

Air Baltic Corporation

In 1995, SAS had a great opportunity thanks to the change in the environmental context. After the independence of countries such as Lithuania, Latvia or Estonia, former countries of the Soviet Union did not have their own airline company. The inhabitants from these countries are often described as “people with a Slavonic heart and a Scandinavian head.” Scandinavians are the biggest investors in this region and SAS had, in the mid of the 90’s, tried to develop the Baltic air transport market on launching with the Government a new airline named Air Baltic, which is today the most successful Baltic airline\footnote{Huettinger, M. (2006), Air Baltic and SAS – a case study in the European airline industry, Baltic Journal of Management Vol.1 No 2, p.227} (the major shareholder is the Latvian state, with 52.6% of shares and SAS AB in the other shareholder with 47.2% of shares\footnote{Ibid, p.233}). It was a great opportunity for SAS. It took advantage of the new independence of Latvia and by the fact that the country did not have a state-owned airline.

In the beginning of Air Baltic, the company was run like a normal flag-carrier with the “Traditional Airline Model”\footnote{Ibid, p.228}, which is characterized by a state-owned airline, landing in big airports and with only round trip tickets.

But in 2001, the board of the company and especially SAS felt that to be more competitive, to grab more market shares, to have the first mover advantage, Air Baltic had to change its features. So, Air Baltic turned into a semi low-cost carrier. In other words, the airline became a low-cost carrier providing flag-carrier advantages. It was almost privatized with had now a single-ticket strategy, a no-frills strategy but the same time it kept the characteristics of a traditional flag carrier\footnote{Nimmp, B. (2004), Hailing the revolution, The Baltic Times, available at www.baltictimes.com}. The results were so good that Air Baltic has now a second hub in Vilnius after the one in Riga.

To summarize, SAS saw a huge opportunity by being the second biggest shareholder of Air Baltic, especially when you know that the Baltic market is experiencing a strong economical growth with the arrival of many foreign businesses and a booming in the number of tourists\footnote{Nimmp, B. (2004), Hailing the revolution, The Baltic Times, available at www.baltictimes.com}. The market
cannot be better for LCC\textsuperscript{495}. In 2005, Air Baltic carried 1.04 million passengers and has a fleet of eighteen aircraft. Moreover, the Baltic region belonging to the European Union, it has the same ‘rules’ as the ones for SAS, which facilitate co-operation and code-sharing agreements.

The Pestel framework and especially its Political and Legal frameworks can change drastically the environmental context of an airline. In the case of SAS Airline, these two frameworks had big consequences. Already in 1988, the European Commission decided to deregulate the airline industry and to welcome new comers by modifying the legislation\textsuperscript{496}. Successively through the three ‘packages’, the barriers to entry were lower, new airlines grew like ‘mushrooms’ such as low-cost carriers, fares of flag-carriers collapsed to be closer to low-cost ones, slots were not allocated like before and the European market became a domestic market.

SAS Airline had to modify its strategies; the Political and Legal frameworks, which were so favorable, became suddenly hostile. Because of the arrival of LCC, SAS Airlines had to reduce its fares and its operational costs in the same time. In 1996, SAS tried to make an alliance with the German airline Lufthansa in order to be stronger in Scandinavia and Germany\textsuperscript{497}, after that SAS had lost its monopoly following the third ‘package’ of deregulation in 1993\textsuperscript{498}.

When the airline industry was still regulated, before 1988, SAS Airline was assigned by the Scandinavian governments as the national carrier of Denmark, Norway and Sweden and was therefore granted traffic rights on domestic routes and international (subject to bilateral agreements with the national carrier at the other end)\textsuperscript{500}. That is, the company achieved regulatory capture, obtaining special rights that were not given to other carriers. Therefore, SAS like any other European flag carrier, operated on monopoly or duopoly routes. There was hardly any price competition as prices and products were regulated through IATA.

The environmental context was totally modified the European airline industry in the early stage of the 90’s. Deregulation in Europe has been a gradual process over 10-15 years. Concerning the domestic markets in Scandinavia, there were fully deregulated in the early 90’s, leading to competition on most domestic routes. Then, in the mid/late 90’s, “open skies” was agreed between the Scandinavian countries and the US. Deregulation within Europe was introduced in steps during the 90’s (a little bit later then in Scandinavia) and completed by the end of that decade. To compare, other markets in the world, like Russia and Asia, are still regulated. Future will tell us if they will follow the same change as in Europe.

\textsuperscript{495} The Economist (13.04.2004), Spreading wings
\textsuperscript{497} Balfour, J. (2003), EC competition law and airline alliances, Journal of Air Transport Management 10, p81-85
\textsuperscript{498} Randoy, T., Pettersen Strandenes S. (1997), The effect pf public ownership and deregulation in the Scandinavian airline industry, Journal of Air Transport Management Vol 3, No 4, p211
\textsuperscript{499} Ibid, p.212
\textsuperscript{500} Interview with Kjell Wilsberg, p.2
The deregulation gave SAS Airline a larger freedom to develop their products and prices but, as they already had the right to fly to most European destinations; the airline did get new network opportunities\textsuperscript{501}. The characteristics of these opportunities that were created with the deregulation present characteristics of Schumpeterian opportunities:

<table>
<thead>
<tr>
<th>Characteristic of Schumpeterian Opportunities</th>
<th>Example</th>
</tr>
</thead>
<tbody>
<tr>
<td>Disequilibrating</td>
<td>SAS has provoked disequilibrium when it launched Snowflake on the market. The Swedish market suffered from over-capacity and too low prices. Certain routes became unprofitable\textsuperscript{502}.</td>
</tr>
<tr>
<td>Requires new information</td>
<td>The change between the packages provided entrepreneurs with new information about how they could operate\textsuperscript{503}.</td>
</tr>
<tr>
<td>Very innovative</td>
<td>SAS had to innovate a lot after deregulation to maintain a high service quality (lounges, distribution channel, frequent flyer card…\textsuperscript{504}).</td>
</tr>
<tr>
<td>Rare</td>
<td>After deregulation it became rare for SAS to operate on regional routes\textsuperscript{505}.</td>
</tr>
<tr>
<td>Involves creation</td>
<td>The opportunities were possible because of the creation of deregulation packages\textsuperscript{506}.</td>
</tr>
</tbody>
</table>

Table 14- Schumpeterian Opportunities and SAS Airline, authors’ creation

6.1.2 Entrepreneurship and Innovation

Deregulation has enabled a fierce competition within Europe and particularly from low-cost carriers. SAS Airline had to react and take drastic measures in order to keep its market shares. We will give you now some innovations and entrepreneurial behaviors of SAS Airline.

One good example of the innovation introduced by SAS Airline was in 1996; they wanted to innovate as much as possible, so they proposed to their passengers “the gate café”: SAS’ passengers could choose their food and drink just before boarding when they were still in the airport\textsuperscript{507}. According Schumpeter, it is a good entrepreneurial behavior because an entrepreneur is someone who “gets new things done”\textsuperscript{508}. SAS Airline introduced of a new quality of a service. In the same

\textsuperscript{501} Interview with Mr. Mats Valinger, Vice President Corporate Development from the SAS Group  
\textsuperscript{502} Interview with Mr. Dan Lundvall, Marketing Director of the LFV Group  
\textsuperscript{505} Ibid, p. 343  
time, we can say that it is, for Drucker, the introduction of innovation. Drucker said “innovation is the specific instrument of entrepreneurship” and “innovation creates resource”\textsuperscript{509}. SAS Airline is a perfect example of the perfect relation between entrepreneurship and innovation. Being an entrepreneur means taking risks to move on. Passengers did not ask for this new quality of service, nevertheless SAS airline wanted to test it, although it would be costly. It was right because the service was well perceived.

**Innovative behavior**

As we already explained before in the theoretical framework, creative destruction is related with innovation. According to Drucker, innovation implies a change and this change is possible through a constant analysis of opportunities changes might offer\textsuperscript{510}. This constant analysis of opportunities was what had been happening with SAS Airline. This allowed SAS to take advantage of the sources of innovation that were created after the change in deregulation. We will now present the sources of innovation presented by Drucker\textsuperscript{511} and link them to the empirical data we have from SAS:

<table>
<thead>
<tr>
<th>Source</th>
<th>Example</th>
</tr>
</thead>
<tbody>
<tr>
<td>The unexpected (success)</td>
<td>SAS introduced firstly one-way tickets within Sweden but has rapidly extended the concept to European routes\textsuperscript{512}</td>
</tr>
<tr>
<td>The incongruity</td>
<td>SAS incongruity between perceived and actual customer values about air service\textsuperscript{513}</td>
</tr>
<tr>
<td>Innovation based on process needed</td>
<td>Low fares take advantage of economies of density\textsuperscript{514} (Snowflake)</td>
</tr>
<tr>
<td>Changes in industry structure or market structure</td>
<td>EU Air Transport Deregulation</td>
</tr>
<tr>
<td>Demographics</td>
<td>It is easier and cheaper to commute in Scandinavia but also in Europe\textsuperscript{515}</td>
</tr>
<tr>
<td>Changes in perception mood and learning</td>
<td>SAS is now perceived differently from its customers. It is a more affordable and flexible airline\textsuperscript{516}.</td>
</tr>
<tr>
<td>New knowledge</td>
<td>Air Baltic is an ‘hybrid’ airline mixing the features of a flag-carrier and of a LCC\textsuperscript{517}.</td>
</tr>
</tbody>
</table>

Table 15 - SAS and sources of innovation, authors’ creation

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\textsuperscript{511} Ibid, pp. 30-35
\textsuperscript{513} http://nweb.waymaker.se/bitonline/2003/03/19/20030318BIT00670/wkr0002.pdf (www.scandinavian.net), Press release, 2003-03-19
\textsuperscript{515} www.scandinavian.net; press release from August 29, 2002
\textsuperscript{516} SAS Annual Report, 2006, p. 8
SAS already existed before the three ‘packages’ of deregulation but it did not really have an entrepreneurial behavior. After the first package, SAS had to exploit those opportunities in order to keep their leadership in Scandinavia, carrying out new combinations of resources and innovating. We will now give examples of how deregulation allowed SAS to allocate resources in the five different types that are presented by Schumpeter:

<table>
<thead>
<tr>
<th>SCHUMPETER’s combination of new means of production that cause development</th>
<th>Examples</th>
</tr>
</thead>
<tbody>
<tr>
<td>The introduction of a new good or of a new quality of good or service</td>
<td>Introduction of Snowflake[^519]</td>
</tr>
<tr>
<td>The introduction of a new method of production</td>
<td>No frills concept in Sweden[^520]</td>
</tr>
<tr>
<td>The opening of a new market</td>
<td>Snowflake was launched to meet customers’ demand for cheap flights[^521]</td>
</tr>
<tr>
<td>The conquest of a new source of supply</td>
<td>Many new agreements with regional airlines to extent SAS’ market[^522]</td>
</tr>
<tr>
<td>The carrying out of the new organization of an industry</td>
<td>Trying to become the leader in the Baltic Market by purchasing AirBaltic[^523]</td>
</tr>
</tbody>
</table>

Table 16 – Examples of SAS’ new combination resources (according to Schumpeter theory) industry, authors’ creation

SAS Airline innovated also when it launched the SAS kiosk. “It is an interactive information system that assists customers to personally take of ticketing, seating and other similar procedural activities.”[^524] It enables customers to be in touch with the world thanks to e-mail or telephone (e.g. searching information about your destination). Moreover they can select the level of service they expect from SAS and SAS tries to meet their expectations. So, SAS knows in which areas it has to take care of its passengers. SAS kiosk is available on Internet but also from the in-flight entertainment (the screen in front of you when you are seated), in lounges, at ticket offices, in some hotels or by phone. All that you need to take advantage of the innovation is to have a EuroBonus card. It is in the same time a good strategy because you urge people to take that card, so in other terms, to be loyal to SAS. Furthermore, in addition to the EuroBonus card, the use of a credit card makes possible the passenger to ‘tailor’ the service he is expecting from SAS and to book the flight. All this information about passengers is scrupulously saved by SAS in databases for the futures journeys.

[^520]: Ibid
[^521]: Ibid
[^523]: Ibid
In 2005, SAS decided to innovate in reaction to the heavy competition of LCC. SAS was the first flag-carrier airline (first mover strategy) in Europe which introduced one-way flights for all its flights inside Europe; a low-cost carrier strategy\(^{525}\). It turned its economy class into a ‘downgraded’ economy class. The service onboard is, from now on, the same as on a no-frills carrier: no free services any more, no possibility to change your ticket...However, passengers who want to ‘go back’ to the former economy class with free refreshments and a dinner/lunch tray, SAS launched in the same time its ‘economy-flex’ class at a higher price. The Business Class has not changed and is mainly for business travelers.

SAS went even further in its willingness to be the one which wants to ‘revolutionize’ standstill flag-carriers and reduce the threats of low-cost carriers by launching Snowflake. Johnson, G., Sholes, K. and Whittington, R. define threats as a part of the SWOT analysis, “it summarizes the key issues from the business environment and the strategic capability of an organization that are most likely to impact on strategy development.”\(^{526}\).

**Snowflake**

SAS turned this threat into an opportunity and on March 30\(^{th}\) 2003, SAS launched its ‘own’ low-cost carrier called: Snowflake. SAS had sold tickets before flights were operational. More than 90 000 tickets were pre-sold. According to SAS, Snowflake was created for leisure travelers who want to travel at a cheap price and easily inside Sweden, within Scandinavia or through Europe.

Snowflake was launched to meet customers’ demand for cheap flights\(^{527}\). Eva-Karin Dahl, Director of Business and Concept Development of Snowflake, said that it had many characteristics of SAS Airline in term of safety or customer care. Moreover, pilots and cabin crews come from SAS Airline as well. SAS chose the name Snowflake to show that it was another business unit with its own fleet.

The first prices for tickets were around 600 SEK, including airport taxes and fees. It was possible to book flights directly on the website (www.flysnowflake.com), through travel agencies or by phoning their call-centers.

Snowflake tickets were like all the other LCC, either one-way tickets or with a return ticket: (e.g. only Umeå-Stockholm or Umeå-Stockholm/Stockholm-Umeå). Snowflake was apart from SAS. It had its own check-in automats in airports and flight attendants wore a specific uniform.

The airline operated at its launch stage four B737-800s, which could welcome 150 passengers. The aircraft had yellow tails with the snowflake website (www.flysnowflake.com) painted on the white fuselage.

Concerning the routes, we can give for instance the flights from Stockholm to Istanbul and from Copenhagen to Bologna; however Snowflake had also routes from Stockholm to Alicante, Athens, Barcelona, Bologna, Budapest, Dublin, Istanbul, Malaga, Nice, Prague and Rome but also from Copenhagen to Alicante, Athens, Bologna, Lisbon, Malaga, Palma de Mallorca, Pristina and Sarajevo.

\(^{525}\) Ibid, p. 358


The service onboard was not free, like in other low-cost carriers, but you could get meals and beverages at affordable prices. As we said previously, Snowflake was a separate business unit; nevertheless it took the best of SAS Airline and in particularly it know-how to meet passengers’ needs. You could make your own meal, according your tastes. Snowflake, like other airlines, proposed duty-free and sales offers onboard.

What about the current situation of Snowflake? Mr. Lundvall told us “Snowflake is dead today but they still have painted planes with their colors. They are dead for the reason that they had never been a low cost. It was just a brand name.”

This example of corporate entrepreneurship was a way to experiment a new strategy in an economic downturn. SAS Airline had enough aircraft and the leisure market increased dramatically. SAS had no ‘tool’ to handle with leisure market, so it was a good opportunity to know what they would need to do to enter into the market.

Today, after the cessation of Snowflake, which was confirmed by Mr. Valinger from SAS, SAS Airline has changed its pricing philosophy based on the experience they had with its low-cost carrier. They have extended their price range downwards and let a number of seats in each plane at a low price in order to be still a player in the real low-cost market. The objective is not to compete head-to-head with Ryanair but rather to be an alternative to the low cost business. Mr. Lundvall concluded by saying that according to him, this new pricing strategy is a success.

According to Matt Valinger, Snowflake enabled to develop a new flexible pricing policy within SAS airline. With the fierce competition in Sweden (FlyNordic, Malmö Aviation…), SAS airline tries to attract customers who left for its competitors and especially the most profitable passengers, business travelers. To achieve its goal, the airline cuts down its fares by up to 30%. Nevertheless, passengers must be aware that they will receive less service on economic class. When you travel on business class you receive food and you are able to modify your ticket whenever you want, you are more flexible. SAS airline has also innovated because prices of tickets are not the same according the season you are flying (peak and non-peak season). Moreover, since August 2002 SAS airline has set special prices for students (under 25 years old) but only inside Sweden. Finally, all passengers can get reductions, if they choose online booking for domestic flights.

Once again the objective of these innovations is to attract new passengers but also to limit the supremacy of low-cost carriers.

We saw previously (Chapter 5.1.6) the biggest airlines alliances and we wanted to know if SAS took into account its partners from Star Alliance or other companies when it develops strategies. Matt Valinger answered that SAS airline followed the development of all types of airlines around the world but especially in Europe when formulating strategies in order to always offer the best for its customers. Benchmarking is a must in the airline industry to take the best of your competitors.

To conclude this part, we can say that the deregulation fostered innovation and entrepreneurship inside SAS. It could not ‘rest on its laurels’ that had to move on and to develop new strategies. It has implemented a more flexible price policy, diversified its products and markets, became a member of an alliance to be more competitive and set a profit-oriented approach.

528 Interview with Mr. Dan Lundvall, Marketing Director of the LFV Group
529 www.scandinavian.net; press release from August 29, 2002
6.1.3 Competitive Strategies

SAS airline has different strategic positions on prices, targets, fleet etc. We will divide them into two parts, the strategies of SAS and the ones of Snowflake.

Concerning SAS Airline, one of its strategies is differentiation. It seeks to offer a different service in the industry, with the aim of creating something that is perceived as unique and highly valued by its customers. Porter says that to do this, the firm should focus in one or more attributes that are perceived as valuable and important by the buyers. SAS applies exactly these several approaches by differentiating its brand image (SAS wants to be recognized as a safe, punctual and high service quality airline), its technology (SAS is use to having investment programs to renew its aircraft fleet with the most advanced aircraft), its customer service etc. SAS pursues its differentiation strategy on several dimensions.

It focuses a lot of offering the best service quality to its customers. In order to differentiate with its competitors in Europe, SAS Airline invests a lot of money on aircraft maintenance. SAS airline improves also its quality by adjusting staffs according the size of the airport.

According to Porter, competitive strategy is “the search for a favorable competitive position in an industry” which aims to “establish a profitable and sustainable position against the forces that determine industry competition”.

The new pricing policy of SAS airline was decided in order to develop a sustainable position in the long run, which means to have a sustainable competitive advantage. The new fares will attract people who used to travel by coach or train within Sweden or people who did not want to travel by plane because of the former expensive prices. Moreover, with the arrival of low-cost carriers in Sweden, SAS airline did not really have the choice and has to implement competitive strategies. Cost advantage and differentiation are besides the two basic types of competitive advantage a firm can have which in turn originate from industry structure.

Differentiation is also applied for its distribution strategy as well. The airline wants to increase its competitiveness. SAS Airline distribution strategy is to be present at any time and at any place for its passengers.

Concerning Snowflake, SAS applied a total different competitive strategy. Snowflake had a cost focus strategy. This strategy implies that the firm chooses a specific segment of the industry to focus its strategy exclusively. Snowflake was created for leisure travelers who want to travel at a cheap price and easily inside Sweden, within Scandinavia or through Europe. Snowflake was launched to meet customers’ demand for cheap flights. Porter says that this strategy is based on the assumption that “the firm is thus able to serve its narrow strategic target more effectively or

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533 Ibid, p. 15
534 Ibid, p. 14
efficiently than competitors who are competing more broadly". Snowflake proposed low fares for its customers but in the same time had the advantages of SAS. It was more than a single low-cost carrier.

Authors like Bowman and Faulker developed some intermediary strategies between Porter’s generic strategies based on the principle that competitive advantage can be achieved if organizations provide customers with products or services that satisfy their necessities (needs and wants) in a way better and more effectively than its competitors.

We can say that SAS, like almost all its flag-carriers competitors in Europe, has a differentiation strategy (No.4 on the figure 10) which is characterized by a high perceived product and service benefits with normal or high prices.

Snowflake on the opposite has a low price strategy, but not a ‘no frills’ strategy like Easyjet or Ryanair. Snowflake does not have all the features of a normal low-cost but it only focuses on low fares. Its strategy is characterized by medium perceived product and service benefits with low prices.

6.1.4 Future Deregulation and Opportunities for Entrepreneurship and Innovation

Button points the regulatory changes as the main responsible for consolidation (as mergers and alliances), mainly amongst the full services airlines. Further mergers will also depend on legal frameworks outside EU. SAS Airline could purchase other medium airlines in Europe or airlines which have severe financial problems, such as Alitalia. But, for the moment, SAS is not in a good financial condition to be a major actor on the European market. SAS could be rather purchase and owned by a major airline in Europe like Lufthansa, British Airways or Air France. Mr. Lundvall told us there are rumors saying that Lufthansa wants to buy SAS Airline.

Air France could become a partner of SAS Airline because it would provide it access to markets they do not have so far. Mr. Lundvall added that he thinks that SAS will be swallowed by someone because we are living in a very strange business today where a number of airlines are purchased although they do not have the same core values. “What are the synergies between Spanair and SAS?” Time will tell us…

Also the trend towards liberalization expect that in the near future all bilateral agreements done by EU members will be replaced by a common set of community agreements, which will provide non-discriminatory open skies agreements with non-EU states.

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540 Interview with Dan Lundvall, Marketing Director of LFV
541 Ibid
542 Fridstrøm, L. et al, Towards a More Vigorous Competition Policy in Relation to the Aviation Market, Journal of Air Transport Management, 10, p. 73
Chances are that future deregulation will bring threats to flag carriers like SAS but they will also bring huge entrepreneurial opportunities and innovation. SAS will have to be more competitive, find new innovation in order to cope with the everlasting fierce competition of LCC. We can wonder what will be the next step of LCC after the ticket for free. But in any case, SAS must have a step forward them not to lose market share within Europe.

6.2 Ryanair Analysis

6.2.1 Context and Industry Analysis

Ryanair had the specific particularity to have been created more or less one year before an important change in the airline industry environmental context – the implementation of the first deregulation package in 1987. This regulatory change can be considered an environmental jolt according to Meyer543. So, Ryanair was born in a very special time in the airline industry – the beginning of a great environmental jolt that brought important changes to the European airline industry. However, before the introduction of the first package of deregulation in 1987, a small jolt occurred in December 1985 when the deregulation Ireland-UK air services occurred544. That is, Ryanair was created before a small and a great jolt in the industry. Despite of this fact, we can argue the anticipatory phase of the company to this jolt was done before it was created, when Ryan was trying to start Irelandia545. Therefore, when Ryanair was created, it did not go through the reorientation of organization strategies that are typical when these jolts occur546, something that did not happen with Aer Lingus which was not prepared for the change547.

Until the implementation of cabotage in 1997 (which meant more freedom for the companies to implement their strategies and to be more innovative), Ryanair strategy and exploitation of opportunities were clearly influenced by the politic and regulatory factors, which are two factors the PESTEL framework argues that influence a firm strategy548. For instance, its first flight from Ireland to UK saw its capacity being restricted549, in 1987 the Department of Transportation took Ryanair’s right to fly to Gatwick and gave it to Aer Lingus550 and its flight from Cork to Luton had to include a previous stop in Dublin551 (this hindered the company to establish certain direct routes and thus it influenced the strategy). Even that the deregulation was more beneficial for the new entrants and small companies like Ryanair than for the established flag carriers, after the implementation of the three packages of deregulation, Ryanair strategy continued to be restricted by the European legislation. For instance, Ryanair first internal UK route was delayed due to its conflict with the anticabotage rules552. This last example shows that there was space for creation of opportunities in the UK market – internal routes were expensive and thus only targeted to customers with high yields. However, before the change in the context there were fewer

550 Ibid, p. 46-47
551 Ibid, p. 31
552 Ibid, pp. 106-109
opportunities for the airlines, and this also influenced the decisions of companies. This was the case of Ryanair whose strategy and exploitation of opportunities were influenced by the context where it was competing. This is not only in line with the PESTEL framework but also with Shane argument that argues people’s decisions are influenced by the context in which they operate.\(^{553}\)

### 6.2.2 Entrepreneurship and Innovation

**Entrepreneurial Opportunities**

Despite of the fact that Ryanair strategic moves were constrained by the specific regulatory context (especially until implementation of cabotage in 1997), when the deregulation packages came, they created opportunities for airline industry’s entrepreneurs that until there did not existed. For instance, the multi-designation allowed Ryanair to open routes from regional Irish airports to London.\(^{554}\) Before this, Ryanair was only operating in the Dublin-London Luton route, the only route that was deregulated due to the policy of Irish Government.\(^{555}\) After the application of cabotage in 1997, the influence of this regulatory change is more evident, as well as Ryanair exploitation of opportunities – for instance, in 2000 Ryanair established its first continental European base in Charleroi and started flying to airports all over Europe\(^{556}\) and nowadays Ryanair has 11 bases in continental Europe.\(^{557}\) This meant that Ryanair could introduce the low cost model in other countries (and thus targeting several segments of population), thus exploiting an opportunity created by the deregulation. This goes in line with Shane argument that argues that changes in regulatory context are a source of Schumpeterian opportunities\(^{558}\). We can also view this argument from another point of view: even if it is true that these changes created opportunities for entrepreneurs, some of these opportunities were not directed created (like the possibility to practice cabotage) but instead they were created because they were renounced to others (they were undirected created). For instance, the EU competition rules that came with the third package facilitated (and provided) Ryanair exploitation of opportunities by restricting Aer Lingus setting up of a new company that was considered to be against competition rules.\(^{559}\)

The characteristics of these opportunities that were created with the deregulation present characteristics of Schumpeterian opportunities:

<table>
<thead>
<tr>
<th>Characteristic of Schumpeterian Opportunities</th>
<th>Example</th>
</tr>
</thead>
<tbody>
<tr>
<td>Disequilibrating</td>
<td>Ryanair reduction on ticket price was a consequence of deregulation that provoked a disequilibrium in the market(^{560})</td>
</tr>
<tr>
<td>Requires new information</td>
<td>The change between the packages provided entrepreneurs with new information about how they could operate(^{561})</td>
</tr>
</tbody>
</table>

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\(^{556}\) http://www.ryanair.com/site/EN/about.php?page=About


Chapter 6  Empirical Data Analysis

<table>
<thead>
<tr>
<th>Very innovative</th>
<th>The license to operate in the UK-Ireland market was completely innovative for the time.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Rare</td>
<td>In the UK-Ireland market, Ryanair was the only airline that was granted exclusive rights in Luton and Stansted airports.</td>
</tr>
<tr>
<td>Involves creation</td>
<td>The opportunities were possible because of the creation of deregulation packages.</td>
</tr>
</tbody>
</table>

Table 17- Schumpeterian Opportunities and Ryanair, authors' creation

These opportunities analyzed through Sarasvathy et. al perspectives upon looking at opportunities, in the Ryanair case we can apply market as an allocative process (opportunity is recognized) and market as a discovery process (opportunity is discovered), taking into account the different contexts. For instance, the recognition of an opportunity happened when O’Leary saw that after the Single European market in 1993, Ryanair should take advantage of the 300 million people market. An example of discovering of opportunity was the implementation of the Southwest Airlines model could work in the deregulated European market (in this case, it is the potential of an opportunity that was discovered).

Entrepreneurial behavior

As we already explained, the deregulation provided entrepreneurs with opportunities that were not possible until arrival of deregulation. After the first package, entrepreneurs could exploit those opportunities, carrying out new combinations of resources and innovating. We will now give examples of how deregulation allowed Ryanair to allocate resources in the five different types that are presented by Schumpeter:

<table>
<thead>
<tr>
<th>SCHUMPETER’s combination of new means of production that cause development</th>
<th>Examples</th>
</tr>
</thead>
<tbody>
<tr>
<td>The introduction of a new good or of a new quality of good or service</td>
<td>Introducing of low cost flights</td>
</tr>
<tr>
<td>The introduction of a new method of production</td>
<td>No frills concept in Europe</td>
</tr>
<tr>
<td>Establishing several connections that were</td>
<td></td>
</tr>
</tbody>
</table>

567 Ibid, pp. 56-66
570 Ibid, p. 89
The opening of a new market | not possible before deregulation⁵⁷¹, first
time flyers (for income reasons)⁵⁷²  

The conquest of a new source of supply | Entering in previous non-used regional
airports⁵⁷³ or/and dominance of secondary
airports⁵⁷⁴  

The carrying out of the new organization of
an industry | Breaking exclusive routes⁵⁷⁵, obtaining
exclusive routes⁵⁷⁶  

Table 18 – Examples of Ryanair’s new combination of resources (according to Schumpeter theory), authors’
creation

Sometimes the carrying out of these combinations led to a disruption in the economic
equilibrium in the market, which is considered by Schumpeter as a process of creative
destruction⁵⁷⁷. For instance, the price war that followed the entry of Ryanair in previous exclusive
Ireland-UK routes destroyed the previous market equilibrium, leading the fares to fall and BA to
retreat (therefore, both the price and quantity were affected)⁵⁷⁸. Other example is how Ryanair
negotiating power led them to get special conditions in secondary airports in Denmark, France and
Spain, demonstrating its dominance over the suppliers and an alteration in market equilibrium due
to an increase in the supply⁵⁷⁹. These examples show how Ryanair behavior is characterized by a
creative destruction (which in turn was triggered by the creation of opportunities with the change in
regulation) and coherent with Schumpeter theories of entrepreneurship and the theories of creative
response in economic history⁵⁸⁰. In turn, these entrepreneurial behaviors that led to market
disequilibrium were fostered by deregulation that provided opportunities to combine resources in
other ways that were not possible until the date.

Innovative behavior

As we already explained before in the theoretical framework, creative destruction is related
with innovation. In turn, according to Drucker, innovation implies a change, and this change is
possible through a constant analysis of opportunities changes might offer⁵⁸¹. This constant analysis
of opportunities was what had been happening with Ryanair since the prophetic foreseen of the
effects of a close deregulation⁵⁸². This allowed Ryanair to take advantage of the sources of

innovation that were created after the change in deregulation. We will now present the sources of innovation presented by Drucker\textsuperscript{583} and link them to the empirical data we have from Ryanair:

<table>
<thead>
<tr>
<th>Source</th>
<th>Example</th>
</tr>
</thead>
<tbody>
<tr>
<td>The unexpected (success)</td>
<td>Ryanair success not expected by actors in the industry\textsuperscript{584}</td>
</tr>
<tr>
<td>The incongruity</td>
<td>Aer Lingus incongruity between perceived and actual customer values about air service\textsuperscript{585}</td>
</tr>
<tr>
<td>Innovation based on process needed</td>
<td>Low cost take advantage of economies of density\textsuperscript{586}</td>
</tr>
<tr>
<td>Changes in industry structure or market structure</td>
<td>EU Air Transport Deregulation</td>
</tr>
<tr>
<td>Demographics</td>
<td>Irish communities in Britain and Ryanair flights to UK\textsuperscript{587}</td>
</tr>
<tr>
<td>Changes in perception mood and learning</td>
<td>Ryanair change of perception about passenger’s values\textsuperscript{588}</td>
</tr>
<tr>
<td>New knowledge</td>
<td>New knowledge of LCC brought to Europe by Ryanair\textsuperscript{589}</td>
</tr>
</tbody>
</table>

Table 19 - Ryanair and sources of innovation, authors’ creation

Institutional entrepreneurship

Despite of taking advantage of sources of innovation and for taking entrepreneurial behavior, Ryanair also tried to bend the rules of the game in order to impose its own interests in a environment with hindering factors (the devastating price war with Aer Lingus and the regulatory framework). For instance, in 1989 Ryanair persuaded the Department of Transport of Irish Government to change Irish aviation policy so the airline could survive in the price war against Aer Lingus. Ryanair initiative was successful and as a consequence of the new “two airline policy” of the Government, the airline was granted exclusive rights to fly from Ireland to Stansted and Luton\textsuperscript{590}. This attempt to change the practices of the Irish airline industry and thus to shape the institutions is considered to be institutional entrepreneurship, according to the concept of Garud et al\textsuperscript{591}. However, an interesting fact of this success was that even in a distressful financial situation (the company was about to close\textsuperscript{592}) the company manage to alter government airline policy, that is, to change the previous institutional design. This goes against a detail presented in the definition of institutional entrepreneur presented by Beckert which argues that changes in the institutional design

\textsuperscript{585} Ibid, p. 33
\textsuperscript{589} Ibid, p. 77, 89-90
\textsuperscript{590} Ibid, p. 46-47
are only possible if an actor possess enough resources. This represents an examples that creative destruction behavior that destroys the “taken-for-granted” rules that are typical in institutional environments, are not dependent on the resources a firm possess, at least in the European airline industry.

Other example of institutional entrepreneurship in Ryanair was the practice of cabotage in UK in 1995, two years before the cabotage rules had come into force. Despite of British and European regulation, Ryanair could bend the institutional design (the airline got a special dispensation from the UK Transport Department) and operate in the routes (despite of capacity restriction). Invoking again Beckert’s definition of institutional entrepreneur we can ask ourselves whether Ryanair resources were determinant for this successful behavior of institutional entrepreneurship. By 1993 Ryanair financial situation was better than in 1988 – they were making profits since 1991 and they registered a 46.7% growth in the number of passengers between 1989 and 1992. However the company was smaller compared with its main rival, Aer Lingus who was carrying four times more passengers than Ryanair, therefore Ryanair situation was not so great they could use their resources to influence a change in institutions. Beckert was not clear in his article to explain what he meant by “resources”, so we can argue that resources are a broad definition that includes both tangible and intangible goods. Glasgow airport managers were also interested in having Ryanair in its facilities and so they were supporting Ryanair establishment of its UK internal routes. However this was the secondary airport of Glasgow, Prestwick, who did not have much resources (therefore they wanted and need Ryanair to fly there – which also leads us to define this as an interest-driven behavior). If neither one company nor another had many resources and they could promote a change in institutional design (UK Transport Department dispensation), it means that resources are not always important in institutional entrepreneurship like Beckert mentioned.

Even if both examples to not strictly follow Beckert explanation of the role of resources in institutional entrepreneurship, they follow the main argumentation of his article that says that institutional entrepreneurship changes positively with the degree of certainty that an entrepreneur has to face in their environment. In the first example, we can argue Ryanair had certainty regarding Ireland low competitive environment in airline industry due to the several records of Aer Lingus regulatory capture during its existence. The degree of certainty along with Ryanair’s financial situation and the introduction of 1st package of deregulation that promote more competition, led the Irish company to promote strategic agency aimed to change the environment. In the second case, the degree of certainty regarding competition in foreign domestic markets was assured in the 3rd package that postponed unrestricted cabotage until 1997 – those were the rules that airline companies should follow during the following years, and thus they were taken-for-granted by the airline companies. Thus, leaded by a willingness to fix the current situation in its environment that was hinder the company’s strategy, Ryanair challenged the isomorphism of Aer Lingus and British carriers, hindered these actors to benefit from the advantages in adhering to these

594 Ibid, p. 777
formal structures, destroyed the “taken-for-granted” rules of institutions in order to assure that its interests would prevail.

Apart from following this argument from Beckert, Ryanair institutional entrepreneurship also follows the Greenwood & Suddaby arguments that argue more peripherical organizations are the ones where entrepreneurship has more chances to arise from. As we already showed, in the European airline industry flag carriers benefited from economic regulation. As Aer Lingus benefited from regulatory capture, Ryanair was in disadvantage with the current agreements. The company had also a weak connection with institutions than Aer Lingus (which was state-owned) or BA (which was state-owned until 1987), therefore was not so aware of institutional expectations. These two facts were even more evident when the company entered in the UK domestic market and had to face the rules that benefited British established companies and UK government policy towards British companies. These facts prove that Ryanair was a peripherical organizational player that was less embedded in institutional design, and thus had more incentives to change the current institutions.

The two examples of institutional entrepreneurship were fostered by the deregulation. In both cases (1989 and in 1993) deregulation had already occurred when Ryanair changed institutional design. Institutional entrepreneur behavior in the first example was led by Ryanair perspective that viewed a clash between Irish airline policy (which in turn was against airline interests) and the 1st deregulation package. Therefore, deregulation had to occur so Ryanair could convince the Department of Transport to change Irish aviation policy and thus the institutional design where it operated. In the second case, institutional entrepreneurship was motivated by the announcement of unrestricted cabotage from April 1997 accorded in the 3rd deregulation package that came into force in 1993. Therefore, in 1995 Ryanair knew already cabotage would soon come into force, however because of its interest in expanding to UK domestic market, with the help of Glasgow airport they obtained a special license to operate in UK market that went against the institutional design of British airline market. So, the 3rd package had to come into force for Ryanair obtain the information about cabotage rules and thus to challenge the institutional design.

6.2.3 Strategic Position

“Ryanair has undergone a remarkable conversion from failing full-service carrier to the most cost-conscious - and profitable airline in Europe.”

By Simon Calder in “No Frills – The Truth behind the Low-Cost Revolution in the Skies”

The change in business environment influenced the strategy of Ryanair. As we already saw, deregulation provided strategic possibilities that weren’t possible before for the airline, like opening new markets or introducing a new service, and it also created sources of innovation like a change in market structure, which in advantages were taken from. These behaviors can be linked to Porter’s competitive strategy concepts in which the firm “relates itself to its environment in order to give a better response to changes in it and to shape the environment in its favor”. In order to compete in the environment and to attain a sustainable position in the long-run, the firm has to adopt strategies

bound to achieve competitive advantage. This was what happened to Ryanair that took advantage of the opportunities created by changes in its environment to create competitive strategies able to achieve a sustainable position. Its most well-known strategy is its low cost policy.

The low-cost policy developed by Ryanair that began in the beginning of the 90’s aimed to achieve a cost leadership strategy clearly fits with Porter’s cost leadership strategy, one of two ways to achieve competitive advantage in an industry. According to the author, a firm seeks to have the lowest cost base in the industry through efficiency in processes, reduction of costs in several areas, cost monitoring. We will present how Ryanair pursuits this strategy which enabled the company to achieve a cost advantage:

- **Economies of density**: Ryanair, as well as other LCC, are able to achieve economies of density putting their airplanes flying more time (2 hours more per day) than the airplanes of other companies. Using secondary and regional airports that are not congested allows the company to achieve a maximization of its flights and an on-time performance record. With these airports the company is able to have a 25 minute turnaround of aircraft, higher rates of time departures and fewer terminal delays. Furthermore, its frequent point-to-point flights on short-haul routes allow the company to offer a frequent service with an average of 1.2 hours, to operate 1.83 round trips per route per day, and to produce 300,000 passengers per aircraft per year. This strategy imported from Southwest is resumed by Kelleher: *Keep planes flying, because that is where they make money*.

- **Pressure on workforce**: Ryanair staff contracts is under Irish legislation, which allows the airline to give them a higher workload and shorter holidays than they would have if their contracts had been governed by domestic labor law. Furthermore, Ryanair does not recognize workers associations and unions, and as the company does not negotiate with them, its employees have no changes to obtain better salaries. Their employees also have worst work conditions than workers who are in other airlines.

- **High load factors**: in 2006 Ryanair assured an 82% load factor, which is ensured by its low prices. This gives the company a considerable profit margin in every airplane since it attains the break-even with half of the seats.

- **Standardized fleet**: Ryanair has a standardized fleet of Boeing 737 (that allows reducing costs with training staff, maintenance and purchase and store of spare parts) which is a cost-efficient aircraft.

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604 Ibid, p. 11
609 Interview with Dan Lundvall, p. 7
612 Ibid, p. 113
613 Ibid, p. 135
614 http://www.ryanair.com/site/EN/about.php?page=Invest&sec=traffic
Basic Service: Ryanair neither use air bridges or interlining nor has lounges at airports. It also does not offer frequent-flyer club or business class service on board.

Direct Sales: The development of the website and calling centre allowed Ryanair to eliminate travel agents commissions. Nowadays internet and telephone, account for 96% and 4% of the reservations, respectively.

Airport Special Conditions and Public Financing: through special agreements with airports, Ryanair can get special advantages such as low landing fees, like it happened in Stansted and other European Airports. Its public known that Ryanair obtained financial grants from Charleroi Airport that are still now being discussed in European Court of Justice. The company is also accused to have special anti-competitive agreements and financial grants in some Spanish, French and Danish airports.

Low customer service: despite of the new EU regulation that guarantees customer compensation under certain conditions, all Ryanair fares are non-refund except in case of flight cancellation or significant flight time change.

Ancillary services revenues: through its website Ryanair provides ancillary services that account for 15.3% of its operating revenues.

Most of these factors were copied from Southwest Airline Model that was brought to Europe in the beginning of 90s. Others, like having ancillary services, its low customer service and the non-unionized work force, were implemented first as a result of the tight competition with Aer Lingus and then with other European carriers. In turn, since the beginning of its existence, tight competition led Ryanair to introduce innovative strategies like no booking restrictions. All these innovative strategies bound to provide a cost leadership were a possible (and were a result) of a specific source – the change in the industry brought by EU air transport deregulation. They represent not only innovative behavior but also entrepreneurial behavior as we already saw – an introduction of a new service (low cost flights) and the introduction of a new method of production (no-frills concept).

This cost leadership strategy was implemented after Ryanair had unsuccessfully tried to compete with Aer Lingus with a focus differentiation strategy – two classes, frequent flyer program, on-board sales – with low fares at the same time. That is, Ryanair was stuck in the middle. When O’Leary realized the company could not compete with Aer Lingus on service, they changed their strategy and started compete on a price base. Analyzing this change of strategy using the strategic clock, Ryanair went from position 3 (Hybrid) to position 1 (no-frills). This implies to have less

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624 Ibid., p. 247
626 Ryanair Annual Report and Financial Statement 2006
service benefits and lower price. Once again, this change in strategy was a consequence of competition that was intensified after the deregulation. To O’Leary this new airline strategy makes sense and they will increasingly give away seats because they are no longer in the aviation business but in the deliver business. Dan Lundvall position is the same: They had totally different strategy because they were concentrated in one thing: selling tickets between two places. (...) They just cared about transporting people just like a simple bus company.

After the first package, airlines could introduce changes in capacity and fares. Due to Aer Lingus power (they were a state company which could obtain advantages that Ryanair could not obtain) Ryanair could not compete in the same base – for instance, when Ryanair low their fares, Aer Lingus was able to slash their fares to match ones from Ryanair. Therefore, Ryanair was forced to change its strategy to no-frills, which could succeed due to its successful institutional entrepreneurship behavior and due to the direct effects of deregulation, like we showed before. That is, institutional entrepreneurship that was successful during the deregulation period (decisions of Irish transport department followed the aims of the first package) along with the consequences of deregulation, allowed Ryanair to successful change its strategy from hybrid to no-frills, an innovative strategy that contained entrepreneurial behaviors like the introduction of a new service and the introduction of a new method of production.

6.2.4 Future Deregulation and Opportunities for Entrepreneurship and Innovation

As Ryanair grows, it merges more companies and acquires more market share, a movement that clashes with Article 81 from EC which restricts agreements that restrict or distort competition affecting trade inside EC and Article 82 from EC Treaty that prohibits abuse of dominant position. EC competition rules can restrain Ryanair entrepreneurial behavior in the opening of new markets, conquest of new sources of supply and above all, the carrying out of a new industry organization. This last one can be restrained in the future, as Ryanair plans to growth its 25.2% stake in Aer Lingus.

It would also be interesting to analyze whether Ryanair strategy would be successful in transatlantic routes that are regulated with bilateral and open-skies agreements. That is, if further deregulation (this time international regulation) would provide opportunities for innovation and entrepreneurial behavior (opening of new markets and conquest of new sources of supply). With a quarter of Aer Lingus, the most probable move is to buy the Irish flag carrier, which will allow Ryanair to enter in new markets. Dan Lundvall foresees this interesting movement: Computer Systems would be the same, maintenance and aircraft would be the same, administration would be the same, the only difference is that one aircraft would be blue and another green. The rest is the same, just like there’s no difference between a Peugeot and a Citroen. Only the shape is difference, the ownership is the same. Aer Lingus could produce Ryanair with the long haul carrier which they could use anywhere in the world.

630 Interview with Dan Lundvall, p. 4
632 Ibid
634 Ryanair Q3 2007 results
635 Interview with Dan Lundvall, p.15
For Ryanair, as well as for other LCC, their model is restricted during a 24 hours period, where they can take advantage of economies of density, as we already explained. With transatlantic flights they could only fly two legs within 24 hours, and this would limit the productivity of their aircraft and then they would lose the advantage of economies of density. Along with this disadvantage, since Ryanair does not have a business class, it would lose the highest profitable customers, which are important in transatlantic flights. Despite of these two disadvantages, their low cost base due to salaries, basic service, direct sales, standardized fleet could remain. Therefore, Ryanair could benefit from its model in Europe and take advantage of EU expansion to create routes that take advantage of the rules in the single market. However, when (and if) the transatlantic market becomes deregulated, Ryanair would need to have a creative response to these changes in the environment, aimed to destroy the market equilibrium with entrepreneurial and innovative behavior, like it did in Europe in the 90s.

6.3 Comparative analysis

After having gathered empirical data of SAS Airline and Ryanair, now we will make a comparative analysis to see if there are any similar or different characteristics. However, we must not forget that both do not have the same background; SAS Airline was a flag-carrier before being privatized and Ryanair has always been a private airline but since 1990 it has been a low-cost and no-frills airline. Deregulation has been a major driving force for both companies, both already existed before 1992 and both of them experienced drastic evolutions.

6.3.1 Context and Industry Analysis

In our case studies we have seen that the more competitive environment that arose with a deregulated market fostered entrepreneurial behavior led firms to innovate. It has been the case for Ryanair but also for SAS Airline. Thus, we found that it was mandatory to talk about competition within this industry and its competitive forces and explain how the deregulation affected them in different ways. We start analyzing the structural analysis of this industry by using Porter’s matrix of the Five Forces Framework. We will compare how the Five Forces changed after the deregulation and their impacts on SAS and Ryanair.

According the empirical data that we collected from both airlines, we decided to build these two following charts to explain the impacts of deregulation of the Five Forces.

636 Ibid, p. 11
As we could see from these two figures, deregulation affected the Five Forces in European airline industry. In turn, the change of these forces forced SAS and Ryanair to create innovative strategies and have entrepreneurial behavior in order to adapt to the change.
For instance, before deregulation it was difficult to create an airline and start operating in any country in Europe. That is, there were barriers to entry and thus there was less rivalry in the industry. When the deregulation came, barriers to entry diminished and plenty of entrepreneurs created their own airlines, and as a consequence, the competition became fierce. This was good for the consumers because since then they had more alternatives to travel, the ticket prices became cheaper and thus they can travel more often in airplanes instead of train, coaches and cars. That is, the entry of low cost airlines created demand through the “Southwest effect” as Rob Brown (marketing director of Southwest airlines) says: *when we go into a market fares go down and traffic goes up*\(^637\).

To explain how the deregulation affected both airlines, we used the PESTEL framework, more specifically, its Political and Legal frameworks. We will now explain how these factors influenced SAS and Ryanair in different ways.

Concerning SAS, these two frameworks had big consequences. Already in 1988, the European Commission decided to deregulate the airline industry and to welcome new comers by modifying the legislation\(^638\). Successively through the three ‘packages’, the barriers to entry were lower, new airlines grew like ‘mushrooms’ such as low-cost carriers, fares of flag-carriers collapsed to deal with the low-cost ones, slots were not allocated like before and the European market became a domestic market. As a consequence, SAS had to modify its strategies. However, these changes were not so accentuated like the ones Ryanair made. In spite of being already a low cost carrier, Ryanair was a “with-frills” charter airline and when the deregulation came they changed their business model completely\(^639\). Within SAS, the regulatory framework didn’t lead to a 180º change in its business model – they are still a flag carrier with frills and higher prices than low cost carriers.

Another important difference regarding the political and legal framework was that after deregulation, the environment became suddenly hostile for SAS but not for Ryanair which benefited from these changes. Because of the arrival of low-cost carriers, SAS had to reduce its fares and its operational costs in the same time. Therefore, SAS saw its profit margin being reduced from 39,1 billion SEK in 1993 to 35,1 in 1996\(^640\) and lost its monopoly after the third ‘package’ of deregulation in 1993\(^641\). For Ryanair this change brought opportunities to open new routes with unrestricted capacities and thus to increase its profits which were positive for the first time in 1993\(^642\). During this period of change, Ryanair was opening routes to Europe\(^643\) while SAS was closing down its unprofitable routes.

As we have seen, changes in the deregulatory framework provoked changes in both firm’s structures. Some of these changes were taken with the creation of opportunities that came with the new environment. That is, strategic decisions were caused by the change in the context, which follows Shane argument that argues people’s decisions are influenced by the context in which they operate\(^644\). For instance, for Ryanair the change in multi-designation rules allowed Ryanair to open

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\(^640\) SAS Annual Report 1997, p. 12
\(^641\) Randoy, T., Pettersen Strandenes S. (1997), The effect pf public ownership and deregulation in the Scandinavian airline industry, Journal of Air Transport Management Vol 3, No 4, p211
\(^642\) http://www.ryanair.com/site/EN/about.php?page=About&sec=story
\(^643\) http://www.ryanair.com/site/EN/about.php?page=About
routes from regional Irish airports to London\textsuperscript{645}. Before this, Ryanair was only operating in the Dublin-London Luton route, the only route that was deregulated due to the policy of Irish Government\textsuperscript{646}. For SAS, the deregulation brought differences concerning freedom to develop their products and prices but, as they already had the right to fly to most European destinations; the airline did get new network opportunities\textsuperscript{647}. In different ways, deregulation brought opportunities for both carriers. The characteristics of these opportunities that were created with the deregulation present characteristics of Schumpeterian opportunities:

<table>
<thead>
<tr>
<th>Characteristic of Schumpeterian Opportunities</th>
<th>Example</th>
</tr>
</thead>
<tbody>
<tr>
<td>Disequilibrating</td>
<td>Ryanair reduction on ticket price was a consequence of deregulation that provoked a disequilibrium in the market\textsuperscript{648}</td>
</tr>
<tr>
<td>Requires new information</td>
<td>The change between the packages provided entrepreneurs with new information about how they could operate\textsuperscript{649}</td>
</tr>
<tr>
<td>Very innovative</td>
<td>The license to operate in the UK-Ireland market was completely innovative for the time\textsuperscript{650}</td>
</tr>
<tr>
<td>Rare</td>
<td>In the UK-Ireland market, Ryanair was the only airline that was granted exclusive rights in Luton and Stansted airports\textsuperscript{651}</td>
</tr>
<tr>
<td>Involves creation</td>
<td>The opportunities were possible because of the creation of deregulation packages\textsuperscript{652}</td>
</tr>
</tbody>
</table>

Table 20- Schumpeterian Opportunities and Ryanair, authors’ creation

<table>
<thead>
<tr>
<th>Characteristic of Schumpeterian Opportunities</th>
<th>Example</th>
</tr>
</thead>
<tbody>
<tr>
<td>Disequilibrating</td>
<td>SAS has provoked disequilibrium when it launched Snowflake on the market. The Swedish market suffered from over-capacity and too low prices. Certain routes became unprofitable\textsuperscript{653}</td>
</tr>
<tr>
<td>Requires new information</td>
<td>The change between the packages provided entrepreneurs with new information about how they could operate\textsuperscript{654}</td>
</tr>
<tr>
<td>Very innovative</td>
<td>SAS had to innovate a lot after deregulation to maintain a high service quality (lounges, distribution</td>
</tr>
</tbody>
</table>


\textsuperscript{647} Interview with Mr. Mats Valinger, Vice President Corporate Development from the SAS Group


\textsuperscript{653} Interview with Mr. Dan Lundvall, Marketing Director of the LFV Group

Rare After deregulation it became rare for SAS to operate on regional routes.  

Involves creation The opportunities were possible because of the creation of deregulation packages.

Table 21- Schumpeterian Opportunities and SAS Airline, authors’ creation

The five characteristics that were present in the opportunities brought by deregulation can be comparable between the two airlines. However, as companies do not have the same targets and the same strategies, faced with a same change, they took opportunities in a different way.

6.3.2 Entrepreneurship and Innovation

Within this part we will present entrepreneurial and innovative behavior in SAS and Ryanair that came after the change in European Air Regulation. Regarding entrepreneurial behavior, both companies found ways to combine the resources in different ways and to fix the industry that was affected by different forces (like we have already explained in previous chapter regarding SWOT). We will now give examples how the two airlines took entrepreneurial behavior.

<table>
<thead>
<tr>
<th>SCHUMPETER’s combination of new means of production that cause development</th>
<th>Examples</th>
</tr>
</thead>
</table>
| The introduction of a new good or of a new quality of good or service | Introduction of Snowflake  
| The introduction of a new method of production | No frills concept in Sweden  
| The opening of a new market | Snowflake was launched to meet customers’ demand for cheap flights  
| The conquest of a new source of supply | Many new agreements with regional airlines to extent SAS’ market  
| The carrying out of the new organization of an industry | Trying to become the leader in the Baltic Market by purchasing AirBaltic  

Table 22 – Examples of SAS’ new combination resources (according to Schumpeter theory) industry, authors creation

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656 Ibid, p. 343


659 Ibid

660 Ibid


662 Ibid
Chapter 6    Empirical Data Analysis

<table>
<thead>
<tr>
<th>SCHUMPETER’s combination of new means of production that cause development</th>
<th>Examples</th>
</tr>
</thead>
<tbody>
<tr>
<td>The introduction of a new good or of a new quality of good or service</td>
<td>Introducing of low cost flights663</td>
</tr>
<tr>
<td>The introduction of a new method of production</td>
<td>No frills concept in Europe664</td>
</tr>
<tr>
<td>The opening of a new market</td>
<td>Establishing several connections that were not possible before deregulation665, first time flyers (for income reasons)666</td>
</tr>
<tr>
<td>The conquest of a new source of supply</td>
<td>Entering in previous non-used regional airports667 or/and dominance of secondary airports668</td>
</tr>
<tr>
<td>The carrying out of the new organization of an industry</td>
<td>Breaking exclusive routes669, obtaining exclusive routes670</td>
</tr>
</tbody>
</table>

Table 23 – Examples of Ryanair’s new combination of resources (according to Schumpeter theory), author’s creation

When analyzing these two tables, we can see some similarities: the introduction of a new service – introduction of low cost flights, the introduction of a new method of production – introduction of no-frills concepts, and the opening of new market that was created with deregulation – the demand for low-cost flights, mostly by young people segment671. These entrepreneurial behaviors occurred both in their home markets. Despite of Ryanair had been the first mover in the low-cost market (both in Ireland-UK and in Europe), SAS adopted the same strategy with the launch of Snowflake in order to face competition. In the next chapter we will see this strategy into more detail.

Regarding the conquest of the new source of supply, both companies extended their network to the periphery, that is, to the regional market. While SAS established cooperation with regional airlines like Air Botnia, and thus did not enter in the regional market directly (instead they made code-share agreements), Ryanair entered in the markets directly, establishing routes from less used regional and secondary airports in Europe.

Within the carrying out of a new organization of the industry, SAS and Ryanair achieved created market disequilibrium in different ways. Scandinavians had became in biggest investor in the Baltic market and SAS had, in the mid of the 90’s, tried to develop the Baltic air transport market, so it launched with the Government the new airlines named “Air Baltic” which is today the

664 Ibid, p. 89
669 Ibid
most successful Baltic airline\textsuperscript{672}. Thus, SAS created a monopoly in air transport within the Baltic region. While SAS was achieving dominance through creation of monopolies, Ryanair was destroying monopolies. For instance the price war that followed the entry of Ryanair in previous exclusive Ireland-UK routes destroyed the previous market equilibrium, leading the fares to fall and BA to retreat (therefore, both the price and quantity were affected)\textsuperscript{673}. Furthermore, Ryanair also destroyed the previous monopoly of Aer Lingus in the Irish market. The process of creative destruction and creative response that are characteristic of an entrepreneur is related with innovation\textsuperscript{674}.

This constant analysis of opportunities was what had been happening with SAS and Ryanair. This allowed both companies to take advantage of the sources of innovation that were created after the change in deregulation. We will now present the sources of innovation presented by Drucker\textsuperscript{675} and link them to the empirical data we have from SAS and Ryanair:

<table>
<thead>
<tr>
<th>Source</th>
<th>Example</th>
</tr>
</thead>
<tbody>
<tr>
<td>The unexpected (success)</td>
<td>Ryanair success not expected by actors in the industry\textsuperscript{676}</td>
</tr>
<tr>
<td>The incongruity</td>
<td>Aer Lingus incongruity between perceived and actual customer values about air service\textsuperscript{677}</td>
</tr>
<tr>
<td>Innovation based on process needed</td>
<td>Low cost take advantage of economies of density\textsuperscript{678}</td>
</tr>
<tr>
<td>Changes in industry structure or market structure</td>
<td>EU Air Transport Deregulation</td>
</tr>
<tr>
<td>Demographics</td>
<td>Irish communities in Britain and Ryanair flights to UK\textsuperscript{679}</td>
</tr>
<tr>
<td>Changes in perception mood and learning</td>
<td>Ryanair change of perception about passenger’s values\textsuperscript{680}</td>
</tr>
<tr>
<td>New knowledge</td>
<td>New knowledge of LCC brought to Europe by Ryanair\textsuperscript{681}</td>
</tr>
</tbody>
</table>

Table 24 – Ryanair and Innovation, author’s creation

\textsuperscript{672} Ibid, p.233
\textsuperscript{677} Ibid, p. 33
\textsuperscript{681} Ibid, p. 77, 89-90
Table 25 – SAS and Innovation, author’s creation

<table>
<thead>
<tr>
<th>Source</th>
<th>Example</th>
</tr>
</thead>
<tbody>
<tr>
<td>The unexpected (success)</td>
<td>SAS introduced firstly one-way tickets within Sweden but has rapidly extended the concept to European routes(^{682})</td>
</tr>
<tr>
<td>The incongruity</td>
<td>SAS incongruity between perceived and actual customer values about air service(^{683})</td>
</tr>
<tr>
<td>Innovation based on process needed</td>
<td>Low fares take advantage of economies of density(^{684}) (Snowflake)</td>
</tr>
<tr>
<td>Changes in industry structure or market structure</td>
<td>EU Air Transport Deregulation</td>
</tr>
<tr>
<td>Demographics</td>
<td>It is easier and cheaper to commute in Scandinavia but also in Europe(^{685})</td>
</tr>
<tr>
<td>Changes in perception mood and learning</td>
<td>SAS is now perceived differently from its customers. It is a more affordable and flexible airline(^{686}).</td>
</tr>
<tr>
<td>New knowledge</td>
<td>Air Baltic is an ‘hybrid’ airline mixing features of a flag-carrier and low-cost(^{687}).</td>
</tr>
</tbody>
</table>

Both SAS and Ryanair recognize the importance of low fares – that is why the sources of innovation after deregulation for both companies are related with the introduction of a cheaper and simpler service. For instance, Aer Lingus incongruity between perceived and actual customer values about air service led Ryanair to successfully innovate the price structure of airline industry, whereas SAS incongruity between perceived and actual customer values about air service led the Scandinavian company to recognize the importance to proceed to innovation bound to change the fare structure and service of its flights. Also both companies innovated taking advantage of economies of scale (SAS did this with Snowflake) and the change in industry structure due to deregulation. They both also introduced new knowledge of business models in the European market: Ryanair first introduced the no-frills and low cost concepts and then SAS mixed this new model with the old one and created a hybrid model which is being applied to Air Baltic.

The last common point in the field of entrepreneurship within these two companies was the corporate entrepreneurial behavior that was triggered by deregulation. As we have explained before, corporate entrepreneurship includes the creation of an organization inside an organization and renewal within the organization. The first can be applied to SAS when the Scandinavian firm created Snowflake as an answer to the threat of LCC and the second can be applied to Ryanair when in the early 90s they resolved to instigate a strategic renewal from a with-frills and low cost company to a no-frills and low cost airline in order to survive and to compete in the market.


\(^{685}\) www.scandinavian.net; press release from August 29, 2002

\(^{686}\) SAS Annual Report, 2006, p. 8

6.3.3 Strategic position

“Weather airports in Europe are monuments, masterpieces. Either they look like shit or they are monuments.”

By Dan Lundvall, Marketing Director of LFV

We already described that deregulation provided strategic possibilities that weren’t possible before for the airlines, like opening new markets or introducing a new service, and it also created sources of innovation like a change in market structure, which in advantages were taken from. These behaviors can be linked to Porter’s competitive strategy concepts in which the firm “relates itself to its environment in order to give a better response to changes in it and to shape the environment in its favor.” In order to compete in the environment and to attain a sustainable position in the long-run, firms has to adopt strategies bound to achieve competitive advantage. Both airlines took advantage of the opportunities created by changes in the environment and developed different strategies in order to achieve a sustainable competitive advantage in the long run.

While Ryanair is most well-known strategy is its low cost policy and SAS adopts a differentiation strategy, two strategies that are according to Porter the two basic types of competitive advantage a firm can have which in turn originate from industry structure. We will now present a table to compare the main characteristics of SAS and Ryanair strategies:

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689 Ibid, p. 11
690 Ibid
### SAS Airline

**Product/service concept**
- Three transport classes for customers (Economy, Economy Flex, Business)
- Seat assignment
- Free baggage transfer
- Primary airports (Hubs in Stockholm, Oslo and Copenhagen)
- Various distribution channels (Online, by phone and travel agencies)
- Loyalty program (EuroBonus card)
- Focus on business and leisure passengers
- Various types of aircraft (B767-300ER, B737-600/700/800, A340-A340, A321-300, MD81/82/83/87/90, SAAB 2000, Q400, Fokker 50)
- Code share, global alliances (Star Alliance + regional agreements)
- Generous pitch, seat assignment
- Customer service (full service, offers reliability)

**Communication concept**
Expensive commercials on television, radio, newspapers, magazines... (in 2006, in-flight magazine Scanorama, in 2007 magazine Seasons)

**Revenue concepts**
- Complicated fare system with a higher number of fares at a time + yield management (according the hour, the season and the demand)
- Ticket sales as biggest source of return
- Medium to high utilization of aircraft (Improvement in aircraft rotation by improved point to point rotation from 40 to 90%)

**Growth concepts**

**Competence configuration**
- Product quality as a national carrier (Focus on service quality)

**Organizational form**
- Low turnaround
- Many activities (Maintenance, cargo...)

### Ryanair

**Product/service concept**
- Single class
- Limited number of daily flights (1 or 2 flights per route)
- Focused on point to point service
- Landing and take-off in secondary airports (mostly) (Charleroi, Beauvais, Luton, Skavsta...)
- Catering (in the economy class) against payment (range of snacks, hot or cold beverages, beers, wines and spirits)
- No special service
- Appealing to price-sensitive passengers
- High frequency
- High-density seating with smaller seats in order to have more ones (economies of density, in 2006 ➔ 82% load factor)
- No seat assignment
- Customer service (generally under performs) (non-refund except in case of flight cancellation or significant flight time change)
- No frequent flyer programs
- Short ticket-sales channels (Online 96% and direct booking 4%)
- Single type of aircraft (less maintenance costs, crew pool and savings in training and qualification) (Boeing 737-800)
- Few physical tickets (printed Check N’Go boarding pass)

**Communication concept**
- Selective advertising only in relevant geographical markets (advertising onboard)
- Emphasizing communication on prices
- Focus on IT marketing
- Advertising on specific targets (teenagers...)

**Revenue concepts**
- Price differentiation by time of booking and strength of demand
- One way pricing, simplified fare structure
- Increasing revenues by focusing on volumes
- On board sales of some service amenities
- High number of flight hours by plane (+3hours)
- Subsidies claimed to regions
- Some airports have eliminated landing fees for LCC (low landing fees in Stansted and other European Airports, financial grants from Charleroi Airport)

**Growth concepts**

**Competence configuration**
- Underlining of low price reputation
- Increase of efficiency where possible

**Organizational form**
- Organization is focused around flight operations (core activity = flying)
- Outsourcing as a part of the policy
- Leadership without hierarchies
- Value addicted to efficiency
Table 26 – Differences between SAS and Ryanair, authors’ creation with available data collected\textsuperscript{691}

<table>
<thead>
<tr>
<th>Routes</th>
<th>Ryanair (Fares in SEK)</th>
<th>SAS Airline (Fares in SEK)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Stockholm- Paris</td>
<td>169</td>
<td>630</td>
</tr>
<tr>
<td>Stockholm- Riga</td>
<td>124</td>
<td>285</td>
</tr>
<tr>
<td>Stockholm- London</td>
<td>79</td>
<td>630</td>
</tr>
<tr>
<td>Stockholm- Frankfurt</td>
<td>199</td>
<td>1,245</td>
</tr>
<tr>
<td>Stockholm- Glasgow</td>
<td>149</td>
<td>630</td>
</tr>
</tbody>
</table>

Table 27 - Fares comparison between SAS & Ryanair on July 20\textsuperscript{th} 2007 (one-way ticket)\textsuperscript{692}

Ryanair low-cost no-frills policy began in the beginning of the 90’s and was aimed to achieve a cost leadership\textsuperscript{693}. However, before implementing this cost leadership strategy, in the beginning it strategy was not bound to slash its cost base – instead they practiced low fares with service, a stuck in the middle strategy that brought financial problems for the company\textsuperscript{694}. That is, the change in their strategy implied a diminishes focus on the service offered, which meant that Ryanair took away its differentiation from its “stuck in the middle” strategy, beginning to focus solely on cost leadership with the introduction of the third package of deregulation. The situation in SAS was the opposite. The Scandinavian airline first began with a fully differentiation strategy typical from flag carriers. However after the competition that was brought by the deregulation, it introduced an innovative mixed service on its flights offering high quality services for business class and lowered the quality in the economic class within short-flights (for Europe) in order to focusing more on the costs\textsuperscript{695}. If we look at that graphic below, SAS followed the strategy adopted by many European airlines, when around 1997 (introduced of cabotage of cabotage), they started adapting low cost business elements, mainly in the economic class fares and services.

When you compare the fares in table 28, you can see how Ryanair is cheaper than SAS. SAS could have also low prices but it depends on the date you book, if you are in a peak season or not and on the demand.

\textsuperscript{692} http://www.scandinavian.com, http://www.ryanair.com
\textsuperscript{695} The SAS Group Report and Summary 2007
SAS maintained their broad differentiation strategy, with a higher focus differentiation on business class who are the most profitable passengers, in order to attract them. While the fares remained the same for SAS business class, the fares went 30% down on economic class. This was made to compete with LCC in the economic class, the only class where they compete directly.

Looking at the figure below, some of SAS and Ryanair strategic movements fit in the three areas of potential innovation. Within the new technology area, for instance, SAS Airline distribution strategy is to be present at any time and at any place for its passengers. Passengers can, from now on, take tickets twenty four hours a day, seven days a week. The new electronic way to book your flight is quicker and makes easier the process and reduces distribution costs. SAS proposes three ways to book for flight: in electronic travel agencies or SAS retail stores, thanks to SAS Direct (Call Centers) or directly on SAS’ website. Ryanair also presents some innovations in the distribution channel. Ryanair created Ryanair Direct (a call centre) to encourage customers to book their seats directly with the airline. It was also able to take away the role of travel agents when in August 1999 the airline created its website that allowed online booking. Besides enabling a save in the costs, the website was also used to sell travel insurance, accommodation and car hire.

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697 www.scandinavian.net; press release from August 29, 2002
699 Ibid, p. 184
Within the new business model, SAS introduced a hybrid model – Air Baltic – and a low cost model – Snowflake, whereas Ryanair imported its low cost no-frills business model from Southwest Airlines. Therefore, both companies present a new business model focus on a reduced cost base. Regarding advanced segmentation, as we said before, SAS started focusing in high-yield business passengers, whereas Ryanair started focusing even more in low yield passengers, offering a high and growing number of fares for free.  

6.3.4 Future Deregulation and Opportunities for Entrepreneurship and Innovation

Deregulation in EU strengthened at the same time the rules for competition – Article 81 from EC which restricts agreements that restrict or distort competition affecting trade inside EC and Article 82 from EC Treaty that prohibits abuse of dominant position. Button notices that further mergers will depend on legal frameworks outside EU. Both SAS and Ryanair entrepreneurial behavior with the aim to organizing the industry in other way are dependent on these rules and the intentions of EU to have a global European carrier. For instance, Ryanair plans to growth its 25,2% stake in Aer Lingus, and SAS purchase of medium European airlines such as Alitalia, or having a partnership with Air France, or being bought by a European main carrier such as Lufthansa (which is according to Dan Lundvall a predictable movement) are restrained by these competition rules. However, these policies in the future will depend on the balance of powers between EU regulatory bodies and Commission, that is, the willingness to protect consumers (with the new laws about competition) and have a fragmented market and the willingness to have a European global carrier competing with the strong American carriers.

701 http://www.ryanair.com
703 Ryanair Q3 2007 results
704 Interview with Dan Lundvall, Marketing Director of LFV
Regarding the future of a common set of EU bilateral agreements\textsuperscript{705}, it would be interesting to see how these two carriers will compete. While SAS can maintain their differentiation strategy and retain high valuable business passengers, Ryanair would need to have a creative response to these changes like it did in Europe in the 90s. If Ryanair and other LCC are able to achieve a cost competitive advantage, SAS will have to be more competitive, find new innovation in order to cope with the everlasting fierce competition of LCC.

\textsuperscript{705} Fridstrøm, L. et al, \textit{Towards a More Vigorous Competition Policy in Relation to the Aviation Market}, Journal of Air Transport Management, 10, p. 73
Chapter 7

7 Conclusions

Chapter seven will be the conclusions of the Thesis where the problem statement, the objectives, the theoretical framework and empirical data will be combined and analyzed together. Conclusions will be organized like a conversation on the different previous chapters of the Thesis where opinions could be given.

7.1 Conclusions

We will bring back the research question in order to link it with the theory and our findings:

**How did the deregulation of air transportation in Europe foster entrepreneurial behavior and innovation in the European airline companies? The case of SAS and Ryanair.**

The main objective of this thesis was to know how the deregulation of air transportation in Europe fostered entrepreneurial behavior and innovation in the European airline industry. We started with the assumption that deregulation implies more entrepreneurship and innovation, like it was stated in the theories of Shane and Drucker. We presented the relevant theories, and used empirical data collected from primary sources (the three interviews we made) and from secondary sources (books and articles already written) to write the case studies. After the SAS and Ryanair case studies we presented a comparison between them, pointing the differences and similarities between them in the new context of deregulation, analyzed the opportunities this change brought and the entrepreneurial and innovative behavior that came afterwards.

We will now present a scheme that will summarize the results we achieved:

![Figure 24 – Interpretation of our research process, authors’ creation](image)

Figure 24 – Interpretation of our research process, authors’ creation
Deregulation, that can be considered an environmental jolt according to Greenwood and Suddaby\(^{706}\), provoked a major environmental change through the removal of barriers to entry in the industry (which allowed the entry of new players). According to Drucker, this change in industry structure is also a source of innovation\(^{707}\). Deregulation created entrepreneurial opportunities for existing actors and for new comers. These new opportunities, using Shane explanation regarding Schumpeterian opportunities\(^{708}\), were characterized for being rare (only three packages of deregulation came into force), for involving creation (creation of a new regulatory framework) and for provoking a disequilibrium (fostered more competition).

These new opportunities allowed entrepreneurs in airline industry to carry out new combinations of resources through five different combinations and to innovate. As we explained, these entrepreneurial and innovative behaviors were different in SAS and Ryanair, since both actors reallocated resources in different ways. Among these entrepreneurial behaviors, we specifically found examples of institutional entrepreneurship in Ryanair and corporate entrepreneurship in both companies. The sum of all entrepreneurial and innovative behaviors by the actors in the industry and in SAS and Ryanair domestic markets led to a higher rivalry in the industry. In turn, this implied that existent actors in the industry like SAS had to rethink their strategies and search for a favorable competitive position in the industry in order find sustainable position against the new competitive forces of the airline industry, that is according to Porter, the seek for a competitive advantage\(^{709}\). While SAS chose to develop a differentiation strategy along with a cost differentiation strategy through its subsidiaries, Ryanair follow the trail of cost leadership. These new strategies were fostered by a higher degree of competition and by the creation of new opportunities in the industry can be considered entrepreneurial and innovative behavior.

With the explanation of this model in mind, we can give an answer to the research question. First of all, our previous assumption that deregulation fostered entrepreneurial and innovative behavior was correct. Without deregulation, as we shown in the case studies, entrepreneurial and innovative behavior could not have been possible in both airlines. Deregulation fostered entrepreneurship and innovative behavior through changes in the competitive forces in the industry:

1. Removal of barriers to entry – this opened the door for several entrepreneurs to set their own airlines and to companies like SAS and Ryanair to enter in new markets with new products and services (two entrepreneurial behaviors)
2. Greater rivalry in the industry – the consequences of the removal of barriers to entry led to further entrepreneurial and innovative behavior such as more introductions of new qualities of goods and services and carrying out a new organization in the industry through innovative strategies.

Regarding future deregulation and entrepreneurship-innovation, the scheme will be also valid, however the opportunities deregulation will bring (if we take in mind the trend to have common set of bilateral agreements in EU) will be different since the changed regulatory context involves different actors from different contexts.

Concerning the three objectives that we had set in the beginning of our thesis, we can say that we fulfilled them:


Our first one was an explorative objective. We linked entrepreneurship with deregulation in the airline industry filling the existing gap in literature and theory that relates deregulation and entrepreneurship-innovation behavior in the European airline industry. This gap was explained in chapter 4.1. In order to help us to fill this gap, we took two major European airlines, SAS and Ryanair, as base for our study. Taking in mind the two different contexts where they operate, our exploratory objective was also achieved since there are also no studies relating entrepreneurial-innovative behavior in the airline industry after deregulation.

Our second was a descriptive objective. We have described two different situations – the story of SAS and Ryanair and how through the time they implemented entrepreneurial and innovative behavior in order to compete in the new deregulated context – and a process – the evolution of deregulation in European aviation industry in the last 20 years, and the adjustment of these two airlines to this evolution.

Our third was a predictive objective. We have based our analysis on the past events of deregulation and at the end of the case studies, bearing in mind the information that was given to us in the primary and secondary sources, we have anticipated and tried to explain what the future trends of the regulatory framework would be in the EU, as well as the next moves of SAS and Ryanair in this new context.

Thus, this thesis successfully answered to the problem statement, achieved the proposed objectives and filled a gap in current academic research.

7.2 Managerial Implications

Our study demonstrated how deregulation fostered entrepreneurship and innovation within the airline industry, specifically to Ryanair and SAS. This study can be useful for managers of European airlines as an example of successful strategies they can adopt in order to answer to changes within their environment. Above all, managers from Ryanair and SAS are the most benefited ones with this study, since these were the companies we chose to focus on. Thanks to our study managers from these two airlines are able to:

- Understand the how their strategies changed with changes in the regulatory environment and identify the strengths and weaknesses of these strategies along the years
- Identify opportunities and threats that can arise with further EU deregulation, and thus create a possible scenario of future strategies and competitive environment
- Identify the main strategic trends within the airline industry and thus have an idea how competitors are expected to behave in the future
- Understand how an important competitor (SAS or Ryanair, depending on the reader) adapted to changes in the regulatory environment

These are the main advantages our study provided for managers from both companies. Managers from other airlines in Europe can also gain with this study, since changes in regulatory environment and the need of a adequate response are two issues that affect their companies.
8 Further research

In chapter eight, we will propose future research that we have identified along our research process which could be interested to go deeper.

As we have already referred in chapter 4.1, several studies in the airline industry present at least a link between two of this issues: deregulation, institutions, entrepreneurship and innovation. Despite of our contribution to filling the gap in literature linking deregulation, institutions, entrepreneurship and innovation, there is much work that can be done. Our work was only centered in two airlines (SAS Airline and Ryanair) competing with two different business models, two different contexts. Taking into account the same context and the link we did between deregulation and entrepreneurship-innovation it would be interesting to:

- Have a deeper perspective in one of these contexts individually; analyzing the entrepreneurial and innovative behavior of all domestic companies (both the existent carriers and the new entrants). For that, empirical data from different airlines and from the governmental body present valuable sources to make the analysis;
- Have a broader perspective of the European airline industry, analyzing entrepreneurial and innovative behavior from several airlines in several countries, find a pattern or a common response for the European airlines (both established carriers and new entrants) and predict the trend.
- Redoing the same study we did, this time taking the airports instead of airlines. Since in Sweden are private and public airports, it could be interested to know what kind of entrepreneurial and innovative behavior came from the two different owned types of airports.
- Compare the entrepreneurial and innovative behavior of airlines in two different European countries, one belonging to EU where deregulation already happened and other outside from EU where deregulation has not happened yet.
- With the deregulation-entrepreneurship/innovation relation in mind, compare the entrepreneurial and innovative behavior between EU countries (or just one) and US, since there is already some studies concerning the effect of deregulation in US but not comparing with the EU experience.

As we can see there are several possibilities to investigation and to write an interesting study concerning deregulation and entrepreneurship-innovation. We strongly recommend future researchers in entrepreneurship to take the airline industry as a topic for their dissertations.

Good luck!!
9 Criteria for Evaluation

In chapter nine, we will explain and discuss about the components of trustworthiness, authenticity and transferability of our thesis.

Doing a qualitative research, we wanted to adopt the best criteria for evaluation in order to prove to the reader that our thesis is trustworthy, reliable and valid. So, we decided to apply the specific criteria proposed by Lincoln and Guba\textsuperscript{710} which suit better a qualitative research. We will use reliability and validity, but trustworthiness and authenticity.

9.1 Trustworthiness

The first main criterion is trustworthiness. Its goal is to prove to the reader that the study done by the researcher is valuable and was made on a scientific way\textsuperscript{711}.

This criterion is divided into four other criteria that we will explain now: credibility, transferability; dependability and confirmability.

9.1.1 Credibility

The criterion of credibility enables the reader to be sure that the research has been made according specific methods\textsuperscript{712}. To give credibility to our thesis, we asked different people at USBE to check that it was credible. First of all, thanks to our quasi-fortnightly meetings that we had with our supervisor, specialized in Entrepreneurship and other business areas, he made sure that we respected this criterion. Second of all, we analyzed our theories and methodology with other researchers and teachers from our School of Business in order to have another confirmation of the right credibility of our thesis. Third of all, when we had a specific question and that we did not find any answer in books and on Internet; we had contacted the professional from the airline industry that we had interviewed.

Moreover, after having transcribed the interviews, we sent them back to the interviewee to be sure that they were the exact words they had said.

Building from these verifications, we can say that our thesis has a high credibility, although it could have check by other scientists.

9.1.2 Transferability

In a qualitative research, researches focus on a small group of people who share the same features. Transferability is also called “thick description” in a qualitative research. On the contrary, a quantitative research focuses more on large features.\textsuperscript{713} Garu and Lincoln argue that: “a thick description provides others with what they refer to as a database for making judgments about the possible transferability of findings to other milieux”\textsuperscript{714}.

Transferability is also the ability to apply the study in practice. We believe that our thesis can be used in order to better understand the airline industry since the last decades. Moreover, our studies could be a good starting point for other studies where the relation between entrepreneurship and the airline industry must be shown. We also really think that entrepreneurial opportunities and innovation have been the immediate answers to the changes in the environment after the deregulation.

Finally, we believe that our thesis could be useful for new comers, new airlines which would like to discover the environment of the airline industry because we explain the strategies that must be used nowadays to grab new market shares or simply to go on surviving in a always more fierce competition.

9.1.3 Dependability and confirmability

On a qualitative research, we could analyze these two criteria in the same because they have the same goal: verify that the research is valid.

The concept of validity is linked with the incorporation of the results and conclusions of a thesis that are generated by the researcher. This criterion is one of the logical tests that is important to judge the quality of research design which is, as we have explained previously, is a set of logical links between the findings of a research and the conclusions that arose from the work. Therefore it is important to incorporate such criteria in order to make the work more coherent and to assure a minimum level of quality. Within validity, Yin presents three different tests to judge the quality of research designs: construct validity, internal validity and external validity.

Construct validity is aimed to provide an “operational set of measures” for the theoretical concepts and definitions that the investigator chose to use in his/her work.

Internal validity is related with the logical link between the variables and the conclusions of a study, in other words, with the cause-effect theory. This purpose of this test is to check whether the independent variables that researcher chose to work with are the cause of a change the dependent variable of the work, that is, if certain conditions are presented they will lead to other conditions.

External validity is linked with the generalizability of the study beyond the specific context where it was made. Some authors argue that generalizations can hardly be made since a specific time and context is always incorporated in phenomena. If not being context-free, a generalization can not be of value for the researcher since he/she is able to predict and control under other circumstances.
Given the fact that a study provides more use for the academic, scientific and society if it is possible to be generalized, within this thesis, even considering the fact we went through a retrospective study, we found important to produce some conclusions (also according to our research objectives) that could be applied in the future.

We have only conducted interviews with male interviewees but we truly think that if the interviewees would have been women instead of men, we think that we would have received the same answers with the same degree of quality.

Researchers always try to get valid knowledge, in other words it means that if you conduct the identical research in the future, you will find the same results. However, validity may be influenced by historical events, maturation and selection biases. Be to good, the same results should be obtained on making the same analyzing but of course on assuming that the context has not changed between the two tests.

If the Thesis, the researcher only uses secondary data, such as Annual Reports, we can assume that this kind of information only present a positive look which may bias results.

Concerning our secondary sources, we can say that they have a high internal validity by assuming that the results published on Annual Reports, books or articles were true and explained the real situation in the airline industry.

As we said previously, we interviewed three professionals on the airline industry, which is relevant for our study. Two of them worked directly inside a company (Mr. Valinger and Wilsberg) and the last one works in a group which controls almost all the public airports in Sweden. The information gathered from these interviews was really beneficial and were excellent primary sources.

Finally, we wanted to add that the analysis that we have done are not based on our personal interpretation but after having studied the real situation found in empirical data.

9.2 Authenticity

Regarding authenticity of a research, Lincoln and Guba divide it into five sub-criteria: fairness, ontological authenticity, educative authenticity, catalytic authenticity and tactical authenticity.

9.2.1 Fairness

If you want to fulfill the criterion of fairness, you must try to get different points of view inside the business you are studying. In order to analyze correctly the airline industry, we made sure that we had various professionals from this industry. For instance, to define properly the low-cost industry, we asked questions to Mr. Lundvall from LFV but also to Mr. Valinger from SAS.

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9.2.2 Ontological authenticity, educative authenticity, catalytic authenticity and tactical authenticity

We had also decided to join these four criteria together because they all solicit the researcher to have comments from people you have interviewed\(^\text{727}\).\(^\text{727}\)

To fulfill these criteria, we sent to our interviewees the whole thesis we have done. However, the period between the day when we sent it to everybody and the day we hope to receive a feedback is too close, so it has been impossible to respect these criteria. This could constitute a weakness for our research.

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10.4 Interviews

→ Interview with Dan Lundvall, Marketing Director of LFV
→ Interview with Kjell Wilsberg, Director Government Relations of SAS Braathens
→ Interview with Mats Valinger, Vice President Corporate
11 Appendixes

Appendix 1 - Key actors in the Northern European airline market

Figure 25 - Key actors in the Northern European airline market\textsuperscript{228}

Appendix 2 - Interview with Dan Lundvall, LFV’s Marketing Director

A: Gilles & Nuno
B: Mr. Lundvall

A: What are the main differences before and after the deregulation?
B: From these 3 perspectives, if you look at aircraft manufacturer… The airline business has grown up in the international world, is a true global business, although if you look at the companies, is a real fragmented industry. It’s a true global business based on international standards. And all this is the outcome of the Chicago Convention in 1944. Without it, we would have the same fragmentation as railways, where we can not take a train to Denmark because it is based on national standards. Airline industry is one of the few industries that is based on true international standards. As it is based on international standards, and this international standards in my opinion concern aircraft are such that any aircraft manufactured anywhere in the world can land anywhere in the world. This means that aircraft manufacturing has always been a deregulated true international business. And today we can see that if you take a look at the number of manufacturers in this business. We have two main jet manufacturers, Airbus and Boeing, and there are also two regional manufacturers Bombardier and Embraer and a couple of small manufacturers which markets are not very big at the moment. There have been other jet manufacturers but they have, just like in the car industry, fallen because their products have never been real competitive in the market – especially if you have a look at the British aircraft industry (Vickers) which had a important aircraft industry after the World War II, but it has never succeeded. They try to force British carriers to buy British aircraft but they never succeeded. BA never had a totally British aircraft fleet because it was not sustainable. So, from my perspective, the aircraft business has been always deregulated and has been a true global business with few but large players.

A: But as you said in BA, when they bought the Vickers jets, it was more for political reasons...
B: At that time these companies were state owned and they were forced to buy local manufactured. Like in other industries it last for very short period. And it never gave these companies a very broad international success by forcing them to buy British aircraft. They were not just effective as their American counterparts.

A: Did this situation happen in SAS?
B: In the beginning of the 50s there was a Saab manufacturing but it lasted for a very short time. I don’t think that SAS ever bought a Saab aircraft. It was bought by other companies, but I don’t think that SAS ever did that. But it last few years because it was during the Cold War and the production was used for military aircraft. When you look at Saab aircraft at modern times SAS does not own a single Saab aircraft. They once leased 5 aircraft (Saab 2000) for commuters. But they don’t own, just lease. I wouldn’t say that is the outcome of political pressure, although it might be an outcome of industrial pressure of the owners of Saab or the large private shareholders of SAS. And also if you look at Air France, they also buy Boeing aircraft like the B-777 and B-737. So the business, when it comes to buying aircraft, is free today from regulation and strong political influence.

A: Before the end of the 70s, when it still was an own stated company Air France had to buy Airbus aircraft (A300). But now they buy only the planes are more efficient for each route.
B: In the American market they only buy American aircraft for patriotic reasons. In America it’s very good example of a non-free market regarding aircraft purchase. But this is a very funny
country. But those are the things that can endanger the free market. Also in Lufthansa and Air France they buy by European feeling because there are hundred thousands of people that are dependent on aircraft construction. So of course there are political pressures on these airlines. But they keep themselves as free as possible from these pressures. And most European companies have aircrafts from both Airbus and Boeing, which is not the case for Continental Airlines, or American Airlines or Delta Airlines, which only have American made aircraft. So I think the aircraft manufacturing market is a free business.

A: And how did the deregulation affect airports?
B: The airport industry is both regulated and deregulated. But in some reasons the airports are deregulated monopolies. That is no doubt that airports are local monopolies - in very few countries you can find active competitive airports. UK is the most typical example where you have totally deregulated and competitive airports. In no other country you have a true deregulated airport. There are airports that are privatized but in very many cases these are just private monopolies. So from that point it’s not truly deregulated today. As airports are local monopolies in most European countries, you have a price regulation and airports are both considered companies and utilities and looks like the States they can not really settle themselves in how they want to look at airports. Because of the planning process is awkward, opposition against the construction of new airports is very strong, then it’s very hard to build competitive airports to compete with existent ones. So I would really say that is not a truly deregulated industry. It’s an industry with lots of private capital but still has a lot of monopolistic influences as far as I am concerned.

A: Are those rules set by national governments or by EU?
B: Airport industry is a national founded industry. It’s built part in the same type of international standards as the aircraft manufacturing. But it’s very national oriented industry. There are lots of small suppliers so it’s a very fragmented industry. And often, in spite of treating these as privatized regulated business, nations have very strong interests in airports and sustaining large airports. EU nations actively sough to introduce competition to the airport business.

A: We know that there are some private airports in Sweden like Skavsta…
B: There are two private airports in Sweden, Skavsta and Linköping.

A: Do they operate with different rules?
B: No, the rules which they operate are the same as any other airport. But the only thing that differs is the ownership – state owned or private owned. Apart from that you have municipal airports that are owned by the local municipality and the only thing that differs from them is the size of the airport and owner. All the rules and standards are the same.

A: Regarding the regulation about airlines that changed…
B: For the airline industry, you have a deregulated market in Europe but you have a regulated market for intercontinental flights. Any type of flights outside the internal market is regulated and most are nearly old bilateral agreements between all states that specify that you have to have a national ownership. And with 75% of the market deregulated and 25% regulated it’s very hard to produce global companies in such a market. This is one of the reasons we have this tremendous fragmented business despite of being a much globalized business. This means that when deregulation has come new airlines have only been able to operate within the deregulated market environment. This means that they have grown to become big within this market. It has never been any few active airlines have been created and gained strength on the intercontinental market. I only know one airline that has based its business strategy on intercontinental market as a sustainable strategy- it’s Virgin Atlantic. There’s no new big airline that has emerged since the deregulation of
the internal European market and that has grown in intercontinental field because of being very heavy regulated.

A: How does the deregulation of the airlines affect the development of the airport industry?
B: It means that based on the fact that the most growth of the airline business is the intercontinental business. And as the intercontinental business still can only be handled through national companies it means that national airlines and national airports hubs still dominate the business. Air France can not set up a hub in Germany and fly to China, which means that even if they might consider Germany a better market than France they can not do it because they would not get the license to operate. So there’s still a very strong connection between large European airlines and large airports. And they are basically interdependent from each other. Air France can not move itself to any other airport in France than Paris Charles de Gaulle, so they are basically sitting which means they are fully dependent. There’s no free supplier/buyer relationship between Charles de Gaulle and Air France, so it means that they can only be successful thanks to these relationships that are quite complex and not very business like.

A: In the domestic European market regional airports were very influenced by the deregulation. For instance low-cost can set hubs in other countries like Ryanair in Charleroi. Did the deregulation have any influence in small regional airports?
B: Yes it does. Deregulation didn’t mean any change for big airlines – they continue operating the way they have always done. If you look at the network before 1987 of the large airlines, the network is basically the same type. There’re very little differences. The effects of deregulation were the arrival to low cost airlines. I would say that deregulation all over the market was in 1993. Real new opportunities didn’t arrive before the end of last century. It was from 1996/1997 when the market started to change and new airlines tried to find new ways of working. The reason why I believe this new airline settled on secondary airports was the fact that before 9/11 there was no slot available at large airports. This was the biggest market entry constrain in the European airports until 9/11. With that, new companies didn’t have the possibility to enter in big airports and the big markets, so they were more or less forced to find ways of operating into smaller secondary airports that no one really bothered about and that were considered totally inefficient or inadequate for supplying air travel to large passengers business.

A: Are the attacks in New York the causes of the decreasing number of flights and thus the rising number slots? Do you think low cost took advantage of that?
B: That’s one of the reasons. The price of airline ticket was quite high – airline travel was a tool for the elite until the turn of last century. Prices were very high, air travel was not something that everybody did (mainly for business passengers and rich people). Ordinary people flew on charters flight. So the market was not oriented to service, frequency and frequent flyers programmes, which are more important than the price of the airline ticket. Because those who paid it didn’t really bother, most of the travel were done by people who didn’t pay their own tickets. And when they paid their tickets they still have enough money. That started changing by the end of the last century. The effects of 9/11 basically changed they whole way this industry operates. 9/11 connected with the economic downturn in Euro for the first time ever produced a reduction in air travel. In all countries air travel was reduced to quite a large extent. And compared to what happened in 1991 with the Gulf War the market did not bounced back – everyone believed that the market would immediately bounce back but did not for some reason. It continued to decline in some countries or to remain stable at a lower level. As airline business has really low margins, very many companies found themselves in very severe financial distress. You have two bankruptcies in the beginning of first year after 9/11 – Sabena and Swissair – which was something that nobody really believed. If you have said at the end of the 90s that a number of airlines would go bankrupt they would say that you are an “idiot”. But this happened and suddenly it created a vacuum at the large hubs. For the
first time ever the big hubs declined in number of passengers - two major European airports were half-abandoned because of the bankruptcy. London Gatwick was half empty because BA decided to withdraw a big part of its European operation. Even Air France stopped their expansion at Charles de Gaulle airport at the same time as you have quite an extension building programme going on in Paris and so on. It meant that suddenly there were opportunities for new airlines to do something new. And of course the new airlines with new capital had found themselves in a very opportunistic situation as they have none of the costs of the old airlines, there were not bound by any agreements, they didn’t have the travel structure of old airlines, and so they found themselves with lots of cash and a manufacturing industry that suddenly didn’t have any orders which means that they had a fantastic opportunity to buy aircraft at a very cheap price. And this is basically the success of Ryanair – they understood they had a reasonably good company and they found themselves they could get cash quite cheap and so they could buy aircraft very cheaply. That’s the base of the whole success. So when all the old carriers cancelled their orders, Easyjet and Ryanair bought huge amount of aircraft at very good prices. They had totally different strategy because they were concentrated in one thing: selling tickets between two places. They didn’t care who they sell their tickets to. They didn’t bother to supply free services. They just cared about transporting people just like a simple bus company.

A: And 9/11 affected the way airports did their policies?
B: These companies (Easyjet and Ryanair) are not run by flag carrier airlines. The traditional airlines seem to, in my opinion, sometimes a bit commercialized flying clubs. People working in traditional airlines they are there because they love the airline business, it is such a different business, and they are there to fly the flag of their nations. In certain effect, as this industry has been regulated for 40 years, it’s doubtful if there was really any true commercial will in those companies. It was still part of the old thinking. When the downturn came and hit them, it hit them quite hard. New airlines are run by people who don’t care about which business they are. They are in the airline business because they don’t love flying, but they thought they could make money in that business. If you look at Ryanair and Easyjet, they treat their suppliers as suppliers. If you could find an airport which sells their landing slots for half price, maybe it’s worth trying. That’s the whole philosophy when it comes to specifically Ryanair but also to certain extent Easyjet because many of their bases are not located in primary airports like Liverpool, Luton, Dortmund, Glasgow, etc. They were opportunistic companies. These guys thought they had a possibility to set another type of air travel – an air travel that looked like a bus transport. And the time when they entered the business was ideal because their competitors were losing money and we had a quite severe economic downturn in Europe with quite high jobless rates and people were afraid of what the future will be after 9/11 based on the fact that terrorism was affecting your daily life. And entering into a high priced business with very low cost automatically makes it impossible; especially if you are questioned by the incumbent operators it was totally crazy. It could never work - this was what most companies were saying. But of course it worked. Just like it worked to produce cheap computers or cheap telephones or cheap anything. Because at the end of the day what matters for people most is what is the price of something, specially if you are not part of an exclusive club. If you don’t have any free frequent miles travel why you bother to pay an expensive ticket? What these guys were doing was took part of the market away from the old airlines who didn’t understand what was happening because they had already defined their markets to a certain segment. Suddenly their market started to growth and instead of attracting 20% of the population, you found yourself 3 or 4 years ago in a situation where there is nobody in Sweden who can’t afford air travel today. If you can’t afford a 200 euros ticket to London you can’t leave, at least in my opinion. Suddenly the whole game was changed and it meant you went through deregulated. And these two airlines were the airlines who took advantage of deregulation in Europe. And the effects of these two airlines were tremendous – they are very big, they are very active in the market, everybody knows about them, everybody has an opinion on Ryanair and Easyjet (you either like them or hate them, but even
if you hate them you found yourself flying with them because it’s the cheapest alternative). If you look at SAS, people don’t have an opinion about SAS – it’s just an airline. Ryanair is more than an airline - is a phenomena - and people like having an opinion about phenomena. To sum up these were the airlines which started with the deregulation in Europe. Since the growth and expansion of these airlines, you have a big number of new entrants in the market trying to do the same thing or something similar to what Ryanair and Easyjet have done.

**A:** How do you see the future for these low cost carriers because they receive subsidies…

**B:** Who doesn’t receive subsidies nowadays…

**A:** Do you think it is fair based on the fact they don’t receive the same amount of money than other flag carriers?

**B:** The question is who gets the money and who pays what. SAS and other domestic airlines receive each year subsidies in Sweden that account for 250 million Swedish kronor. And this is the cost of the regional airports in Sweden. If you fly to a small airport in Sweden you pay less than an half of the cost of the airport. When the airlines receive the bill from the airport, they only receive a small part of the bill. And this is a very big subsidy. And this is true in most countries in Europe. So, in my opinion, if you look at indirect subsidies in these two, it also affects the airline profitable accounts. Traditional airlines get more subsidies than Ryanair or Easyjet.

**A:** So it’s fair…

**B:** I think it’s fair because as there are very few transportation business that are totally sustainable, every transport business get subsidies in different ways because of the fact that infrastructures in small towns is public utility it’s not self-sustainable business. And by selling your airport at a price which is not the price that is not the cost based means there is a subsidy to everyone that is using. This means that everyone gets a subsidy. So there’s no difference when SAS gets a subsidy in Kiruna paying a third of the price cost, or Ryanair getting a subsidy in Charleroi by not paying the full price. There’s no difference. What Ryanair has done, in excess of that, is that they have found that this business is changing. When you are in the business travel people are travelling because the have to go to work. But the business today it’s not business travel – it’s leisure travel. And leisure travel is trying to attract someone to your region. So leisure travel tourism is huge market. So destination market is one of the biggest markets in Europe. And it’s a huge and profitable business because people who come to your region spend and huge amount of money. The income tourism business in Sweden it is valued 190 billion Swedish kronor, which is more than the Swedish export volume. So tourism is more valuable even for such a small nation as Sweden compared to its industrial output. Nobody believes that. When you look at France or Portugal you will find immensely big profits with that. Most people spend 200 euros a day and you need to get them. And if you don’t find anyone to transport them there, of course you buy the transportation. That’s what Ryanair found out. It’s all about destination market: “We are ready to transport tourists to your town but we aren’t doing it for free, we are taking risk, and we have to be a part of the risk sharing and a price for that is 5, 10 million Swedish kronor. If we are both successful, your income in the other hand is going to be much higher. So you make your calculation and we made our calculation and if we agree we make business.” That’s what happening in Catalonia. They found the cost of supporting Ryanair is far less than the profits they make with tourists who come there. And this is open for everybody. And the old airlines never found out that this was a business. They never believed they could sell flights to a region. The Americans are doing this since many years ago when it comes to attract people to destinations. The route of Venice, or Lyon was supported by their respective communities. You have something called travel banks in the USA or companies and communities guarantee a income of the airline to attract it. Subsidies are everywhere. It’s just a matter how you use them and how direct they are. Old airlines didn’t understand the changing nature of this business. For instance, the new route of SAS between London and Kiruna will be
Appendixes

subsidized – SAS would never open a route to Kiruna from London without supports and
guarantees from the local community. Ryanair business is positively influenced by the subsidies
they receive from the region, and this one of the reasons they make so many profits. When you
travel in Europe the first thing you do is to check the prices in Ryanair website and then the price of
the old carriers. Nothing is free on low cost carriers. If you can sell something that doesn’t cost
anything is always good money. Service on board is tremendously expensive, production
philosophy is simple, all aircraft returns to base, you fly much more – it’s like a bus company. If
you have a cheap asset (because they bought cheap aircraft) the best way to get money is to sweat
the asset. They fly 50% more than other companies. The income per aircraft is much higher.
Ryanair produces 300,000 passengers per aircraft per year while SAS produces half of it. This
means that SAS to be in the same income level needs much higher prices. The success of Ryanair
can’t be only justified only by the subsidies.

A: That new business model as well as other creative behaviour (like the frequent flying
programme), do you think it was a consequence of the deregulation?
B: It all came from competition that fostered these new things. Now competition is really hard,
especially in the internal market is really intense. There are lots of players out there that are losing a
lot of money. Innovation is very important nowadays. If you are not the biggest and the cheapest in
the market you need to find a niche to survive, because at the end of the day it would be hard to beat
the one with the lowest cost. Big part of the market can’t afford high tickets and it will affect the
whole thing. Even rich people want to travel cheap.

A: Can you tell us more about the slot allocation in the airports? There is any discrimination
based on the type of aircraft or airline?
B: The answer is no. It’s all based on EU regulation of the beginning of the 90s. That’s a very strict
regulation. And the allocation of slots is fairly done in most airports. What you do is a grey market
which is something that the fathers and the mothers of the deregulation really think about it.
Distribution of slots is very fair but when slots are distributed the horse riding starts. If you are a
small airline, a new comer in the market, you have priority to receive the slots. So there are
company which acquire the slots, they don’t fly and then the sell to existent airlines. There’s a grey
market. At certain airports that’s a very good market. In the newspapers these days there’s a rumour
that with the effect of the new transatlantic agreement BMI is supposed to be bought by someone.
And it looks that BA may be one of them.

A: Perhaps can be Virgin Atlantic…
B: Yes, or Virgin too. The reason is very simple. The only valuable asset BMI has is its slots
because it’s a quite normal company, it has nothing unique. The only unique thing is that they have
14% of the slots of Heathrow. And it’s going to take at least 20 years if they can increase the
capacity in Heathrow. So 14% of the capacity of Heathrow values 1 billion of pounds. Slot trading
and restrictions on capacity is leading to slots to become an asset that people are buying and selling.
There are no rules how do you regulate the secondary trading market. Commission tried to establish
the rules one year ago but failed. No one owns an asset if you look at the regulation. Normally you
fly and have certain grandfather rights, but that’s the member state who owns the slots. Assets are
changing hands.

A: The slots belong to the country, and they sell the slots to the company…
B: No airline owns a slot. You’re allowed to operate you’re given a slot by the member state. But
you have no guarantee, by the time period you’ve been allowed to operate which is basically 6
months. If you’re operating a slot you have a grandfather right to continue to operate on that slot but
it’s not an absolute right. The member state can change your time of operation and can confiscate
your slot.
Appendixes

A: Does it change if the airport is privately owned?
B: It doesn’t matter. The legal ownership of the airport is not a decisive factor when it comes slot coordination. It’s the member state that decides if the airport becomes slot coordinated and not the airport company itself. The airport company can request to become slot coordinated. The slot coordination is a international bargaining process between airlines supervised by the member states. You apply for a slot and if the time available you automatically get the slot. If the time is not available you get something in the vicinity of that time. The member state can’t confiscate the slot from one airline to give to another airline. It can only confiscate for public services. It’s a self regulated process under the rules of the EU regulation of 1993.

A: Regarding the fares of airports, do you have a special policy like peak load pricing?
B: We don’t have that. Most airport prices are regulated by the member states. I think the only one which is not regulated is Switzerland. In all other member states the pricing is regulated by an independent coordinator or by the member state itself. For instance, Copenhagen is a private airport and the price policy is regulated by the Danish state which can decide what they can charge for passenger’s fees. In Sweden we have a price cap system a bit like in the UK – we can adjust our price to the net price index accumulated since 2001. But within this price cap we are free to set our prices. This is regulation for state owned airports. For private airports they are free to set the prices they want according to the agreement between them and the airlines.

A: So the fees are really low for private airports in order to attract the LCC…
B: Sure. Their geographic position is not the best, usually is quite far out. In order to attract that you need to have cheap fares. The airports themselves look at their market situation and you can look that at their pricing system – if you are alone in the area you’ll find quite high fares such as Amsterdam or Frankfurt…

A: Are you allowed to practice price discrimination based on the objectives of the airline?
B: Airport prices are subject to EC competition law, which means that under those rules, if you have a dominant position you’re not allowed to discriminate between users. So if we give a lower price to SAS than to BA it would be a court case and probably we would lose it. The only discrimination or differentiation we have is that we charge lower costs for domestic flights because the market is much more competitive. And then we have another set of tariffs for international flights. The only exception is if you start a route that is not flown by anybody else you are allowed to be given incentives for a limited number of years. Those programmes can last 5 years where we give discount in a number of fees when they introduce a new route. After that period you’ll pay normal price.

A: Are the fares based on the type of aircraft?
B: We apply take-off fees which a means that we charge based on the weight of the aircraft. We have some adjustments, for instance, in Sweden small aircraft have very cheap fees and there’s a regional policy for that. We have very cheap fees for very large aircraft because the market is very thin. To try to attract intercontinental routes we have a lower tariff for very large aircraft. Regarding the passengers, we apply a flat fee per passenger.

A: Does it change with the time period?
B: No. We don’t have any restriction or constrain. The reason for not having peak pricing is that it affects your home based carrier. We are not in the process to extent our facilities because of having peak.
A: Do you think that in the future will be possible for airlines to have their own terminal?
B: Oh yes. That’s the American way where the companies to have their own terminal. The disadvantage of having unique terminal for airlines is that you’ll get a suboptimum capacity structure. You have more terminals than the traffic you have. In totally it should be less expensive to have common terminals than private terminals. Although, European airports have the tendency to build monuments. The major airports in Europe are monuments, masterpieces. Either they look like shit or they are monuments. If you look at Paris or Madrid, they look more like monuments than practical buildings, in my opinion. These monuments are not very cost effective and not very cheap to operate. Airport operators based on their local monopoly they take little care about what airlines want. If you are a true business you wouldn’t build an airport they way airports are built. You would build much cheaper based on the fact that the business is changing faster and faster, and probably it would be much better decision if you build a cheap building so you can adapt yourself rapidly to the change of the market. But you can’t do that when you build masterpieces which cost billions of dollars. Sometimes the airlines pay a lot for something they don’t need. The fact that airlines can’t build their own terminal is a sign that airport business is not a truly regulated business. Private airports can be worst than public airports. Private airports only run for one reason – to maximize the profits. I haven’t seen any difference between them. You’ll see a difference if an airport is running in a competitive environment.

A: So there are no advantages for a LCC to land in private airports?
B: There’s one advantage of using private airports. Private airports can support airlines in any way they want. No member state can’t regulate how a private investor uses his money. They can only regulate public investors. If you are a private investor and give money to an LCC no one can stop you. When it comes to private airport fees it depends on what type of regulation you have in your country. In the future if EU is successful is implementing its airport charges directive then all the airports would become price regulated and then would be any difference if you are a private or a public airport. But the difference would still be there when it comes to the use of supporting money because you’re private.

A: Would it be possible to build terminals only for LCC?
B: Sure, you have those already. Marseille MP2 is one of them. This is probably the best example.

A: What do you think there are the regulatory barriers for airports?
B: It looks like you’re moving into a situation where the infrastructure pricing would be regulated, which is quite bad. But that’s the only part of the business that is being regulated. The airport business is more or less like any other business. You can apply any strategy you decide as long as it’s allowed by the community. I think airports have a lot of opportunities to grow.

A: Do you have specific agreements with charters?
B: No. We have the same type of operation. There’s no difference.

A: What are the main costs and profits of an airport?
B: When it comes to our airports, airport operation is a loss making activity. Within 16 airports, there is only one where aeronautical charges basically cover the cost and that’s the Arlanda Airport in Stockholm. The profit for the aeronautical activities is 300 million kronor and revenues for the commercial activities are between 6 and 7 million kronor. All other airports lose money. All the other money comes from commercial activities. So, our main income from the commercial side is parking, the rental for offices and shops.

A: Extending the number of shops inside the airport is a good solution to rise the revenues for the airport?
Appendixes

B: If your market is big enough, yes. What you need is business-like thinking and you can get that by hiring some people – you don’t need to be a private airport.

A: Would it be a trend to privatize airports to solve this situation?
B: If you are a public owner and you want to make an exit and leave the business in order to get as much money as you want, there’ll be a reason to privatize. Other reason is that where we’re not in a position to raise money. Any of those circumstances are reasons for privatization. It would be hard to find reasons to privatize if there’s no problem of money. The state of Sweden is in a real good shape and so there’s no reason to sell the airports because what you lose may be bigger than what you gain because you lose control. If you are the community you’d like to control the airport because there’s a tool for making your region attractive, which is more important than getting more quick money. If you’re a large city airport you’ll probably like to control part of the investment of the airport. It’s only in UK where you have very large private airports, but in other countries the state owns them and its very active in controlling the destiny of the airport, like happens in France where the state has big control of the airport. So, private airports are a tool that is used in certain developing economies if you need to attract capital and or if your public structure is not good enough. And that’s not the case of Sweden. You need to have a minimum size before the airport gets profit.

A: If you want to extent the size of the airport, you need to ask the member state or the airport can do it by itself?
B: If it’s a very large investment it has to pass through the board of directors and has to be notified to the state. Investments below 100 million Swedish kronor can be decided by the director of the airport. In this case it’s like a private company. Investment decisions are not a problem at all.

A: How is possible to have a foreigner carrier outside its country to operate between two other countries, one outside Europe?
B: Charters can do that. Most bilateral agreements only regulate scheduled travel and charter travel is regulated piece by piece, flight by flight. So it’s not impossible for an operator like LOT or Air France to apply for a license to operate during a season for a country outside the EU. But it is dependent of both authorities’ policies. In Sweden we demand that the airline is operated by a safe country, which has a good flight oversight. For instance, Finnair has a summer flight from Stockholm to Boston, and takes advantages of Open Skies policies and authorities from both countries. Today the basic rights are between nations, Open Skies basically says that any EU airline can operate from any point in Europe to any point in US and any US airline can operate to any point in Europe. It would take time to see some market development. For instance, there’ll be difficulties for Air France to have a flight from Lisbon to New York, or to TAP to have a flight from Paris to New York. Virgin Atlantic would probably try to get advantage of this agreement. Lufthansa may try also. The biggest transatlantic market is between UK and US, so I won’t be surprised if there were companies trying to get advantage out of that.

A: Do you think LCC can have transatlantic flights in the future?
B: The production advantages of Ryanair and Easyjet is that it is restricted during a 24 hours period. The low costs are flying more hours in this period than its competitors, and that’s why they get cost advantage. You can only fly two legs within 24 hours. There’s no way you can increase the productivity of the aircraft. Therefore they would have no advantage expect of the low cost base like salaries. But that’s not going to be decisive. There are people trying to find niches. But I would be surprised. The intercontinental market is totally dominated by leisure flights. 80% of the world passengers that are in this market are leisure passengers. Business part is very small but is very profitable and expensive on board. Airlines use this to get a wide range of price categories. And if you are a low cost you have to shrink this cost because you’ll never attract passengers that pay very
much. So all the money would be made in the low cost segment. That’s not sure this mix can be profitable if they don’t have a cost advantage. Intercontinental flights are very seasonal.

A: What are the main driving forces that fostered deregulation in Europe?
B: I think today there is a combination between industrial and political actors. There’s something wrong with this market because it’s much more fragmented than a normal market. The true global business has 300 actors. There’s no other industry where you have so much small companies. In most business you have a few big companies, and a reasonable number of small companies trying to get into the market and niches in the market to explore. But there’s no one world wide airline. So I think there’s a political driving within the Commission which is trying to get European actors that are not ethnic based. For instance, Air France is a company for French to travel abroad, SAS is a company for Scandinavian to travel abroad. If you go outside the country no one knows about your national airline. They have no market presence. If Air France would start an domestic flight in Umea today it would have problems. Ryanair is much more well known than SAS in Europe, but no one knows about Alitalia, Iberia… And that’s the problem – you have a global industry that is ethically based. European airlines are very well managed. So there’s an opportunity for them to grow, and so that’s the main aim of the Commission in order to create strong European factors.

A: Do you think there are some economic factors behind the deregulation?
B: Oh yes. Creating strong economic airlines will lower the overall cost because they are cost synergies for large airlines, especially on the overhead side. And they will be financially very strong. There’re industrial players that look the same way that think they can create large European players. Lufthansa is trying to become a truly European airline – they have the strength, the interest and the money to do it.

A: Do you think the consumers played any role in process of the deregulation?
B: I think the consumers know very little about airline. This business was not a consumer product until 5 years ago. Now it’s a consumer product. Since LCC is here to stay, although there’ll certain increases in the environmental effect. But I don’t think the consumers are not bound for certain airlines. It’s like shopping cars - some people buy different brands others buy the same car along their life. Airline it’s a commodity product nowadays. I don’t think the choice doesn’t have to be between 20 airlines for one destination. I don’t think there’s a consumer drive to have a market fragmentation. They like to have strong companies that give them a good value for money.

A: What do you think about the future of airline industry? As nowadays we are assisting to a privatization and consolidation process – do you think that can be the trend in European market?
B: Yes. There’s no reason for states to own their airlines, because they are true business. You can start an airline tomorrow, but the barriers to entry and exit are really low. Aircraft are already available, they are international, so there’re no reasons for states to own airlines today. If a state loses its airline today and decides it wants to secure airline transportation they can only set up easily an airline tomorrow. Therefore I don’t think there’s no reason for states to own airlines. Only the poorest countries in the world see airlines as a strategic tool. Even in China and India, states are starting to sell their airlines, because the market is enough to guarantee a supply of airline transportation.

A: And regarding the process of consolidation…
B: Exactly what way consolidation will go you can always discuss. Airlines seem to have very strong conscious individual culture. Culture in Air France is different from KLM. Taking over a
Appendixes

company can be a disaster when it comes to product. Airlines own other airlines but they keep part of the structure intact because of the local differences in business culture. If you look at other companies you have a local base. The goal is to have the best synergy possible. One example is the Swiss ownership by Lufthansa. They are consolidating in certain areas but Swiss is still a local business of Lufthansa. They found out that is the best solution because Lufthansa is not an important brand in Switzerland. So you can have an airline that owns 5 or 6 other airlines and the structure behind the flights makes them look like local brands.

A: What do you think about the differences between the LCC subsidiaries of flag carriers and normal LCC like Ryanair and EasyJet? Do you think Snowflake is a real LCC?
B: Snowflake is dead today but they have still painted planes with their colours. They are dead for the reason that they had never been a low cost. It was just a brand name.

A: Would you say it was a fake LCC?
B: Yes. It was a way to try to experiment in a downturn. They had planes they could utilize and the leisure market increasing dramatically, they had no tools to handle that leisure market (SAS was not even active in the internet business), so it was a good place to experiment and know the costs and what they need to do to enter the market. The result is that if you look at SAS pricing philosophy has changed; totally based on the experience they had with Snowflake. They extended their price range downwards and let a number of seats in each plane at a low price in order to be a player in the real low cost market. Not to compete head-to-head with Ryanair but to be an alternative to the low cost business. And I think they have succeeded.

A: What do you think about other LCC from old carriers, like Transavia? Do you think they can compete and that they are a real low cost?
B: I think Transavia makes money on charters like Air Berlin. As long as they have a good charter business Transavia will be a profitable company. But I would be surprised if they make any money on scheduled business because most of their schedule business is long-haul compared to other LCC. If you look at EasyJet their flights last less than 2 hours. If you look at Transavia should be between 2,5 hours and 3 hours. So it’s a converted charter operation. Transavia does not fly between big hubs. They are there to be sure that Easyjet doesn’t enter in the Dutch market more than they are doing today. KLM doesn’t want to do it itself because it could put pricing pressure on their other business and so Transavia is the cheapest tool they can find to make sure that other LCC don’t enter in the market. Apart from SAS, they had already that tool, so it was easy to convert this company to a middle size low cost.

A: Do you think Transavia and KLM will operate on different routes? They have totally different routes and objectives…
B: It’s like when Lufthansa operates German Wings. I’ve never seen them competing on the same route. When German Wings entered in a route that was operated by Lufthansa (Goteborg – Köln), Lufthansa loads dropped drastically for 40%. For some reason, German Wings stopped flying in this route despite of having very good loads. From the corporate point of view it’s useless to compete with the mother company.

A: Don’t you think that there will be competition between Transavia and KLM?
B: Of course there would be. That’s a problem when you have two companies on one route. But the management should make sure it doesn’t get too complicated and sub-optimized. But as Lufthansa shows, German Wings is a really profitable and sustainable business. And they have been
Appendixes

successful of keeping Ryanair and Easyjet away from their market. It’s a strategy to limit the
growth for them and to sustain the major brand from being diluted. Transavia looks like a low cost
because of their charter flights. But that’s not from their effectiveness but from their long flights
that automatically give low unit costs.

A: Why do you think that some subsidiaries failed like GO and Buzz while others like
German Wings have been successful?
B: The difference is the time when they were launched. When they were launched, their mother
companies didn’t have defined what strategy they wanted to do. In the Buzz case it was evident that
had a cost based that was not sustainable – they operated expensive routes, various aircraft. GO was
much better. GO could have been profitable if they had a sustainable business. But I doubt that they
had a clear strategy about what to do. And at that time airline pricing was quite different from that is
today. The low cost business was not developed as it is today. And there were a lot of doubts in the
airlines about their sustainability. When Ryanair and Easyjet raised their volume, Go and Buzz were
under pressure because they weren’t big enough and not streamlined enough to be really
competitive.

A: Do you think the future of LCC is still good?
B: Sure. There are lots of markets to develop.

A: Do you think they will change their strategy or continue like today?
B: They will change like everybody will change. If they move into the largest markets, the big city
primary markets, then they will have to change somehow. The question is: Are they ready to change
the model so they can attract also higher number of passengers of the market? Easyjet is trying a
little bit. They are experimenting pre-boarding for certain passengers, seat-selection, and things like
that without changing their basic philosophy. Also if you move into this market you will get more
pressure from your customers to provide certain services at the airport, and these airlines provide
nothing at all. And this one the game becomes difficult because you start to become like another
airline. And this is going to be the biggest issue. Maybe they will move to the biggest airports and
perform like they behave today, targeting certain segments of the market. Which strategies they will
do, we can’t know at this stage. But the secondary airport market will become saturated and these
airlines operate very large aircraft from the European perspective. Then the question is: should we
go to this markets the way we are or should we dress up? I don’t know, it’s very difficult to say
because these changes will have implications in the whole business and corporate culture.

A: Do you think that can be business class in LCC like in Virgin America?
B: Maybe. It’s possible. Why would Ryanair buy Aer Lingus? To kill it? No. They are big enough
today to kill them because they are so much big today. But maybe Aer Lingus could provide
Ryanair with a business class segment. It would be the reverse of Transavia. If we do share of the
Bergamo market, perhaps we can use Aer Lingus from Brussels to Milan and be active in those
markets because Aer Lingus is a different product and culture and still gets a lot of money. So
Ryanair could use Aer Lingus to enter in the big markets. Computer Systems would be the same,
maintenance and aircraft would be the same, administration would be the same, the only difference
is that one aircraft would be blue and another green. The rest is the same, just like there’s no
difference between a Peugeot and a Citroen. Only the shape is difference, the ownership is the
same. Aer Lingus could produce Ryanair with the long haul carrier which they could use anywhere
in the world. So it would be a interesting move to buy Aer Lingus. Austrian Airlines is another
airline that is not sustainable. SN Brussels is another company that would be able to survive the way
it is. There are opportunities to do things because at the end of the day there will be only two big
airlines to become major airlines and that’s Air France and Lufthansa. BA is an island airline and
they tried so many times to go through and they failed all the time. They are based on the continent.
And one indication is who will buy Iberia? What will happen to them? It is the same with Alitalia. No one wants to buy Alitalia the way it is like today. Iberia carries a lot of potential which has the biggest share in the South American market. In the north of Europe few people go to South America. Someone will buy TAP or Iberia because they are already present at the South America which is a huge market and those two companies are too small to become major players. We will see. There will be very interesting moves in the future.

A: What do you think what will happen to SAS?
B: I think it will be owned by one of the big carriers. Right now SAS is not in a financial condition to be a major actor on the European market. There are rumours that Lufthansa wants to buy them but there is no reason for Lufthansa to buy them because they already control it. And SAS doesn’t add anything to Lufthansa. Air France would be a much more natural partner for SAS because it would provide access to markets they don’t have today. But I think SAS will be swallowed by someone because it’s a very strange business today with a number of airlines with no internal connections between them – what synergies are between Spanair and SAS? There are very few synergies. So it’s a very strange corporation and on the paper looks much like Swissair. Time will tell…

A: Thank you so much for the interview.
B: It was a very interesting discussion. I enjoyed it. I hope you got something useful.
Appendix 3 - Interview with Mats Valinger, Vice President Corporate Development of the SAS Group

A: Gilles & Nuno
B: Mr. Lundvall

A. Could you briefly describe your own company and how it is behaving in the current business environment?
B. Ref Annual Report

A. What were the consequences for your company after the deregulation in Europe? What kind of opportunities did SAS get?
B. When the Airline industry was still regulated, SAS was assigned by the Scandinavian governments as the national carrier of Denmark, Norway and Sweden and was therefore granted traffic rights on domestic routes and international (subject to bilateral agreements with the national carrier at the other end). Therefore, SAS like any other European flag carrier, operated on monopoly or duopoly routes. There was hardly any price competition as prices and products were regulated through IATA. The deregulation gave us a larger freedom to develop products and prices, but, as we already had the right to fly to most European destinations, it did not mean a lot for our network opportunities.

A. What are the main hindering and supporting factors of the deregulation?
B. Apart from markets still regulated a major hindering factor for deregulation are congested airports (like Heathrow and Frankfurt) with a minimal room for additional flights, particularly at attractive times. (Ref Mr Näslund). Supporting factors are of course that it opened up for competition from a new breed of airlines with other business models, leading to lower prices and more options for the customers.

A. What were the direct and indirect innovations that came after the deregulation in your company? (Frequent flyer card…) What measures do/did you take to foster your market position after the deregulation?
B. A more flexible price setting, diversification of products, alliances, a more competitive and profit-oriented approach etc

A. Do you think that entrepreneurship or intrapreneurship could be an answer to develop your company after the deregulation?
B. Yes a lot!!

A. Do/Did you receive state or private subsidies to develop your company?
B. No, never.

A. How do you negotiate agreements with airports concerning taxes, schedules…?
B. Ref Mr Näslund. Schedules are normally negotiated at bi-annual IATA-meetings, where airport representatives meet with airlines.

A. Do you think it could be relevant for SAS to have its own terminal? (like the low-cost carriers are trying to do currently)
B. Could be - at our main hubs.
A. Could you give us information about your subsidiaries? Are they the best solutions to compete with the other low-cost carriers and with the other flag carriers?
B. You will find this information in our annual report.

A. What are the differences or similarities between charters and low-cost carriers?
B. They are both operated at a low cost level. Charters and LCC differ in customer base and distribution (individual vs. tour operators) and partly in route net (any market vs. resorts).

A. How do you consider your competitors? Is there a tough competition? Who are your main competitors? Do you fear low-cost carriers?
B. Competition is fierce, particularly from low cost carriers. Main competitors differ by market.

A. Do you look at other airline companies, which belong to Star Alliance, when you develop strategies?
B. We follow the development of all types of airlines when formulating strategies.

A. What are the regulatory barriers to airlines’ policies?
B. Please ask also Mr Näslund for this question.

A. What is your strategic planning for the next years? (mission, vision and general strategies…)
B. Unable to tell you at this point in time. We are just in the process of a major revision of our strategies (ref Annual report p 6-7)

A. How do you see the future of the air deregulation in Europe within the next years? And what could be the impacts for your company?
B. Please ask also Mr Näslund for this question
Appendix 4 - Interview with Kjell Wilsberg, Director Government Relations of SAS Braathens

A: Gilles & Nuno
B: Mr. Wilsberg

A. Could you briefly describe your own company and how it is behaving in the current business environment?

B. SAS Braathens will officially be renamed "SAS Scandinavian Airlines Norge" from 1st June 2007. The company represents the Norwegian part of Scandinavian Airlines and is a merger between the former Norwegian carrier Braathens and SAS Norge, the Norwegian part of the SAS Group. SAS Braathens is a network carrier. In 2006 the airline in average operated 440 daily flights, carried 9,6 million passengers on route service within Norway and Europe, in addition carried 400 000 passengers on charter flights. Turnover 10 173 mill SEK, Result before tax (EBT) 338 mill SEK. The company had (2006) ca 3 800 employees, full or part time, corresponding to 2604 FTE (full time employees). SAS Norge will stress punctuality and regularity and has together with sister companies in Sweden and Denmark introduced NKS (Nye Kommersielle SAS or New Commercial SAS), stressing value for money. Cost saving program has been going on the last 2 - 3 years and is still a priority issue.

A. What are the consequences for your company of the deregulation in Europe? What kind of opportunities did SAS Braathens get?

B. When deregulation went into effect, SAS and Braathens were competitors in the Norwegian market. Braathens were mainly a domestic operator (60 % market share) plus charter operations and some few international routes, while SAS was the other domestic carrier (40 %) but was the main international carrier from the Norwegian home market. Both airlines were "traditional" network carriers and the main challenge has, specially the last 5 – 6 years, been the growth of the Low Cost carriers.

A. What are the main hindering and supporting factors of the deregulation?

B. The deregulations made it clear that a structural change in the business had to take place. No hindering to establish new airlines occurred. Equal competing terms is important. Norway has, as the only country in the world, since August 2002 banned earning points on frequent flyer program on domestic routes 100 %. This is negative for SAS Norge only, in the company's competitive position towards foreign network carriers which are allowed to use their frequent flyer programs unrestricted both in their home market and on their service to/from Norway. The problems of the airline industry were structural. The traditional airlines had high cost level and low productivity – thus they had a big challenge to adapt to a deregulated industry. Expensive and complicated infrastructure like the booking and check-in systems and to a large extend internal support like maintenance and handling result in higher fixed costs than for the new entrants. Air transport on short and middle distances has become a commodity. Earlier price policy with a lot of restrictions in order to avoid businessmen from traveling at low fares is not longer possible. Internet sale has an enormous impact on sales and distribution and is a key element of the Low Cost airlines success.
Appendixes

A. What were the steps of deregulation in Scandinavia?
B. In Norway, the domestic market was deregulated 1st April 1994. Norway, though not a member of the EU, adapted the EU aviations policy as from 1st April 1997. The intra-Scandinavian market was partly and step by step deregulated from 1989.

A. What measures do/did you take to foster your market position after the deregulation?
B. SAS Braathens was the first traditional airline to establish one-way fares on the intra-European market in order to try to match the new entrants in the market. (see also price policy question 3 above). More focus on cost level, out-sourcing of tasks that were not main business. Aircraft and crew utilization, more dynamic network planning, thus closing uneconomic services.

A. Do you think that entrepreneurship or intrapreneurship could be an answer to develop your company after the deregulation?
B. Probably…

A. Did the deregulation modify your strategies?
B. Yes. Important to speed up implementation of new product, define strong and weak positions in the various market segments and push cost cut programs. Important to convince the employees that changes are necessary.

A. Who are your main competitors? How do you consider them? Is there a tough competition? Do you fear low-cost carriers?
B. Network airlines’ hubs reduce their importance in the European market. "Hub and spoke” results in lower productivity and a lot of extra costs related to handling and support. More and more segments of the market are no longer willing to pay for this. Hubs are vulnerable for irregularities. More point – to - point services will develop. Low cost carriers will take a larger share of the European market (up to 50 %?) LCC catch a lot of traffic from traditional carriers, however, they also create substantial new volumes. The big network carriers will be less affected. Our main competitors are both the big network carriers like British Airways and KLM/Air France and the new Low Cost companies. As an example: KLM has 19 daily departures to Amsterdam from various Norwegian airports. SAS and Widerøe has 32 daily to Copenhagen from the same airports, however, Amsterdam has a far better connecting network worldwide and thus is a main competitor in the Norwegian market. Norwegian is a fast expanding Low Cost carrier operating both within the Norwegian market and as a main international carrier from Norway. There is an element of risk for mid sized traditional network carrier, like SAS Norge, to be "stuck in the middle” competing both with stronger network carriers and more cost efficient Low Cost airlines.

A. Do you look at other airline companies, like SAS Airline, when you develop strategies?
B. There is a co-operation between the various companies in the SAS group in developing strategies, however, each carrier is allowed to and has to stick to their special position in their respective home markets to tune their own position.

A. What are the regulatory barriers to airlines’ policies? Were there any regulatory barriers that hindered you in the past? Were/Are there possibilities to “bend” the regulation?
B. Before deregulation (Norway) on the domestic market, the Ministry of Transport granted concessions to SAS and Braathens for 5 years periods. This meant traffic rights but also obligations, to operate the routes granted and the Ministry's approval of
schedule/frequencies and capacity, prices, discounts etc. Internationally, SAS was, as part of the 3–country agreement from 1950, granted exclusively traffic right on the international routes from the three countries, based on bilateral agreements between the Scandinavian countries and the other countries involved. Within EU and the ESA countries there are no barriers today.

A. **What are the differences between SAS Airline and SAS Braathens? What is your pricing policy?**

B. SAS Braathens (Norge) was the biggest contributor to the SAS Group turnover in 2006 and contributed with 17% of the SAS Groups turnover in 2006. SAS Braathens (Norge) has a bigger part of its operations within the domestic market than the other SAS companies. The Norwegian domestic market were 11 mill passengers in 2006 (4.5 mill inhabitants). SAS Braathens (Norge) has an expanding Norwegian competitor (Norwegian). From the start in 2002, the new company has established a strong position in the Norwegian market based on low fares and also a strong network on the main domestic routes. In addition Norwegian has developed a strong foothold in the leisure market from many Norwegian airports.

A. **How do you see the future of the air deregulation in Europe within the next years? And what could be the impacts for your company?**

B. •Flexibility and ability to change focus – market adjustments.
  •The challenge for the network airlines is to reduce the cost gap as much as possible, keep the advantages of the hub/spoke system and still serve the passenger segments that are willing to pay for extra service, and give value for money:
    – Flexibility, time table/frequencies, in flight service, lounges, seating, pre-check in and other service elements
  •Reduced income means reduced costs to survive.
  •Sales and distribution costs to be further reduced
    –Easy access on internet, easy to communicate, plain price structure
    –Easy and convenient procedures on ground and on board
  •Extra income beyond ticket price is needed – sale of additional product, pricing of services.
    –Easyjet, Ryanair and Air Berlin have ordered 300 + aircraft, where will they fly??
  •Capacity at main airports and in the air
  •War, terror and international crisis, pandemics
  •Increased international focus on environment
  •Security (costs and time spending)
  •Fuel prices
  •Airline ownership. Less state ownership, more international ownership, airline as an investment object for shorter or longer periods, mergers. Many of the new entrants will disappear.
  •Airport ownership: Copenhagen airport has Australian owners.
  •Competition will occur between various airports to attract traffic. Most airports have spare capacity and high fixed costs. Incentives from local business and tourist authorities will support new routes.
  •Consumer rights have become a main political target within EU.
  •Consumer rights as a result of irregularities result in higher compensation than ticket value in many cases.