Low-Cost Airlines' Product and Labor Market Strategic Choices: Australian Perspectives

Gregory J. Bamber
Griffith University, Brisbane

Russell D. Lansbury
University of Sydney

Kate Rainthorpe
Griffith University, Brisbane

Clare Yazbeck
University of Sydney

Abstract

This paper examines the domestic airline sector in Australia. It discusses the product and labor market strategies of the main Australian low-cost carriers (LCCs). It considers how labor-market strategies in these LCCs have been influenced by the strategic choices that they have adopted in the product market. It also makes some comparisons with LCCs in the United States and Europe. It concludes that these Australian LCCs are moving to adopt some product market characteristics similar to those of legacy carriers. This may have implications for the future recruitment and training of frontline staff, who would be required to provide services to a wider market than previously.

Introduction

From an airline industry perspective, Australia comprises about a dozen key cities, most of which are separated by long distances and near the coast of a large island continent. There are about another sixty towns, some of which are inland and remote. For most of the post-1945 period, the Australian

Author's address: Griffith Business School, Griffith University, Nathan, Queensland, Australia, 4111

government had a "two-airline" policy, which was, in effect, a cozy duopoly whereby the domestic market was shared between Qantas and Ansett.

Qantas was founded in 1920 and is Australia's dominant legacy carrier. Since it was privatized in the 1990s it has operated profitably in international and domestic air services and a range of related businesses. Ansett was founded in 1936, mainly as a domestic carrier.

Following several short-lived attempts since the 1980s to start a third domestic airline, Impulse and Virgin Blue (VB) were launched in 2000. Their launch reduced fares to historically low levels. Qantas and Ansett dropped their fares to match start-up deals. As Ansett and Qantas had higher overheads, the fare reductions challenged Qantas and induced losses for Ansett. Against the background of this price war, Qantas took over Impulse, which was later relaunched as Jetstar (JS), and Ansett collapsed in September 2001. This paper examines the product and labor market strategies of VB and JS—the two main low-cost carriers (LCCs) in Australia.

Product Market Strategies

Richard Branson initiated the Virgin brand in 1973, and it has since grown into an international brand and a conglomerate. Virgin purchased EuroBelgian Airlines in 1994, then renamed it Virgin Express. In 1999 Brett Godfrey, an Australian executive of Virgin Express, and another Australian, Rob Sherrard, proposed to Branson the establishment of a "Virgin branded, low cost, low fare carrier operating in the Australian domestic market" (Virgin Blue 2003, 52). The LCC model that Godfrey proposed was similar to Southwest Airlines (SWA): a "no frills" airline. Godfrey said "the airlines that are clearly succeeding are those that have stuck to the consumer friendly Southwest low fare model" (CAPA 2002, 34).

The Virgin Group invested approximately US $7.5 million for start-up costs. Godfrey became the CEO. VB initially used second-hand planes, endeavoring to be low cost, but offering reasonable customer service. Its start-up strategy was influenced by the prevailing market domination by Qantas and Ansett, which were full-service airlines (FSA). The collapse of Ansett in 2001 left a large gap in the market, which VB and Qantas moved quickly to fill. After Ansett's collapse, Qantas held more than an 80 percent market share but had concerns about VB's aggressive expansion based on lower costs, which were 30–40 percent less than Qantas's. This helped VB to win about one third of the domestic market within three years.

To respond to the competitive threat of VB, Qantas CEO Geoff Dixon drew a "line in the sand" by creating JS, to restrict VB and other carriers from taking more than 35 percent of the domestic market (Harcourt 2004). Qantas adopted a "pincer-movement" strategy: it established an LCC to compete with

VB on price, especially in growing leisure markets, whilst using Qantas as an FSA to concentrate on business markets. Qantas intended to force VB to respond either by reducing costs to compete with JS or by increasing costs to compete with Qantas in the corporate market. This strategy, using two brands to target different markets, aimed to close the gap at the lower end of the domestic market and also to reduce the risk of "cannibalization" of the mainline carrier. (Such cannibalization had occurred between British Airways and its low-cost carrier, GO.) The parent companies of JS and VB played different roles. From its inception, VB's competitive position was assisted by public recognition of the Virgin brand. However, after its first couple of years, VB had relatively little direct association with the Virgin Group other than in branding (Virgin Blue 2003). The Virgin Group is no longer the primary shareholder in VB, but it still holds two seats on VB's board. Nonetheless, Branson has said he wishes to buy back enough shares in VB to regain control of the airline.

Whereas VB is a *stand-alone carrier* (it operates as an autonomous Australian-owned company), JS is a wholly owned subsidiary of Qantas and so is a *carrier-within-a-carrier.* JS has the advantage of guidance and financial support from Qantas, including buying planes, lobbying governments, fuel hedging, and treasury advice. Nevertheless, JS tries to differentiate itself in branding and its labor market strategies. Similarly to VB's association with Virgin, JS's relationship with Qantas seems to be attractive to customers, partly because of Qantas's excellent reputation for safety. However, the connection may also have disadvantages. For instance, JS operates in the shadow of the work practices and high-wage costs associated with the forty-eight enterprise bargains (labor contracts) between Qantas and the sixteen unions with which it negotiates. Furthermore, while VB was set up almost as a greenfield venture, JS was effectively the rebranding of another airline that Qantas had taken over: Impulse, which had been a quasi-LCC.

Both Qantas and Impulse, then, provided foundations for JS's start up. Qantas used the Impulse entity because it provided fourteen aircraft; an Air Operators' Certificate; a maintenance base; and a workforce whose employment contracts could be taken over by JS. Such use of Impulse helped Qantas to provide JS with a degree of autonomy, learning from the experience of airlines such as Delta's Song (Song failed to achieve lowest costs because it was too closely associated with its legacy carrier parent). To foster independence, JS organized its own commercial and airport operations. It outsourced certain services (for example, call centers) to entities outside the Qantas Group. By contrast, VB supplies its own customer and ground handling services at its busiest airports but outsources these functions at other airports. It also outsources catering at all airports, some maintenance services, and the overflow from its call centers (Virgin Blue 2003).

Although VB primarily used SWA as a model, for JS Qantas sought to select the best features from leading LCCs around the world and apply them to the Australian market. It aimed to adopt the *efficiency* of Ryanair, the *branding* of easyJet, the *innovation* of JetBlue, and the *customer service* of SWA (Joyce 2004).

Both carriers introduced features used by LCCs in the United States and Europe, including no interlining of passengers' baggage. JS introduced a twenty-five-minute flight turnaround. It also adopted "freestyle" seating (although subsequently introduced staggered boarding). In contrast, VB allocates seats in advance, which is more popular with passengers. Both LCCs try to implement a thirty-minute flight "close out" notion, though VB is more flexible about its application. During the early phase of its operations, JS's stricter policy caused irritation among passengers, which led to some negative publicity and prompted JS to soften its stance in this context.

Labor Market Policies and Practices

As a stand-alone LCC, VB was freer to establish labor-market strategies that complemented its business model, whereas JS was more constrained by its carrier-within-a-carrier association with its FSA parent. These differences may be illustrated by examining the LCCs' behavior in terms of selection and recruitment, labor relations and unions, and work organization.

Selection and Recruitment

As a "greenfield" stand-alone business, VB used its recruitment process to select a particular type of employee and to cultivate a distinctive organizational culture. VB looks "for team members who display achievement drive, guest service orientation, integrity, team work, and a desire to create memorable, positive and fun experience for all" (Virgin Blue 2005). Emphasis on the "Virgin Flair" reflects SWA's strategy to select employees with a particular attitude. The VB culture is reinforced by training programs, performance-based compensation policies, and the promotion of its corporate values and goals, which include "safety, on time performance, lowest possible cost base, great place to work, great service" (Highfield 2005, 2). Qantas also wanted to establish a distinctive organizational culture for its new subsidiary and was aware of the potential disadvantages of JS being too closely associated with its parent. To help distinguish JS as an LCC, Qantas used the Impulse entity as "a ready made airline" with "a low-cost culture" (Joyce 2004). More than 400 former Impulse employees joined JS, mainly pilots, cabin crew, and engineers. To supplement this workforce, JS recruited managers and staff from within the Qantas Group, as well as new employees (Jetstar 2004). JS was also inspired by SWA to establish a selection process to recruit employees with a customer service “attitude” and then “train for skill” (Joyce 2004). Although JS aims to emulate Ryanair’s efficiency in terms of work organization, its rhetoric at least emphasizes excellence in customer service and a highly committed workforce, like SWA.

Labor Relations and Unions

There is generally a high union density in the Australian aviation industry. This has developed against the background of a centrally regulated industrial-relations regime and the concentration of employment in a few workplaces (that is, large airports). In Australian aviation, unions are mostly organized along occupational lines (on the Australian context for employment relations, see Bamber, Lansbury, and Wailes 2004, chap. 5). VB and JS have taken different approaches to labor relations compared both to each other and to Qantas, which is highly unionized.

From its inception, VB invited union involvement. In doing so it attempted to legitimize the employment contracts it was offering to employees; foster trust between the airline, employees, and their unions; and avoid union recognition conflicts that may have arisen if union representation had been denied. Unlike Qantas, VB limits its industrial relationships to three unions. It wanted to deal with unions that would support flexible work practices and broader job classifications and would not seek to enforce the occupational demarcations that prevail in legacy carriers. Consequently, the Flight Attendants’ Association of Australia–Domestic/Regional Division (FAAA) represents cabin crew, while the Australian Federation of Air Pilots (AFAP) represents pilots. The Transport Workers Union (TWU) covers the largest proportion of eligible VB employees, including pit crew, engineering, and “guest services.” This broad coverage has caused some friction between the TWU and the Australian Services Union (ASU), which VB does not recognize, even though the ASU represents ground staff at Qantas, JS, and most other airlines in Australia. Nevertheless, the TWU views its relationship with VB as generally positive and has been able to settle most grievances and disputes at the enterprise level through negotiation.

JS established different labor relations foundations to its parent by using former Impulse arrangements, several of which were non-union agreements. JS has since negotiated new agreements with most occupational groups, but they are broadly similar to the former Impulse contracts. Qantas hoped that the lower-cost culture of Impulse would make it easier to negotiate low-cost agreements with employees and unions than at Qantas, where they are accustomed to more generous benefits in terms of working hours, wages, and conditions.

Since JS was developed from Impulse, it has unionized and non-unionized occupational groups. The only unionized employees are cabin crew, 85 percent of whom are members of the FAAA, and ground staff, who are represented by the ASU. Ramp and baggage handling workers are represented by the TWU, but JS outsources these processes to a Qantas subsidiary. For non-unionized employees JS maintains "works councils" inherited from Impulse to facilitate consultation. For example, for engineers there is an Engineering Consultative Committee, which comprises elected employee representatives and management representatives. It oversees the operation of the agreement, assists with dispute settlement, and is part of a broader communication and consultation process to help JS cope with challenges that may arise.

Work Organization

Both LCCs highlight "efficiency" and "functional flexibility" as key components of their low-cost strategies. VB employees are trained in a wide range of skills and have flexible job classifications. This is particularly the case for ground crew under the TWU agreement, whose duties may include handling aircraft and auxiliary equipment, freight, and passengers and their property; making and changing reservations; issuing boarding passes; cleaning aircraft; flight operations and/or ground crew administration; load control; notifying passengers of changes and cancellations; handling queries, emails, and surveys; reception, guest lounge, and administrative duties; and supervisory duties. At VB ground crew can become flight attendants and vice versa, which is unusual in legacy carriers because they tend to have strong demarcation and seniority lines. VB is introducing a "unit crewing" process to coordinate rosters, which enables cabin crew and their supervisors to fly in the same teams as often as possible. This is intended to enhance the role of supervisors, to increase employee commitment by building teams, and to foster consistent and high-quality customer service. JS takes advantage of broad job classifications for its own employees and the companies to which it outsources processes. It also relies heavily on minimizing costs through operational efficiency by adhering to typical LCC policies such as freestyle seating and a thirty-minute flight "close out" in an attempt to maximize the efficiency of aircraft and labor by increasing check-in and boarding efficiency.

The LCCs' different approaches may be illustrated by VB's comments on some of JS's practices. For example, VB has declared that it would not match JS's twenty-five-minute flight turnaround because "we focus on 30 (minutes) to allow a reasonable amount of time to look after the wellbeing of our staff and guests" (Creedy 2004). It has also been skeptical of JS's ability to match VB's costs and achieve the same level of staff flexibility: "Our efficiencies are gained not by hurrying, but by multiskilling people to ensure the most effective operation" (Creedy 2004). As a stand-alone carrier, VB may have an advantage over JS in that, apart from pilots and other specialist technical occupations, many VB employees are working in the airline industry for the first time. As such, VB had a "clean slate" from which to establish flexible work practices and less traditional labor relations. On the other hand, it could be argued that previous airline experience may mean that employees will be more skilled and experienced in airline operations.

Conclusions

A common feature of the two Australian LCCs is that they were both created by wealthy parents. However, they can be distinguished by the way in which they were created, how they maintained their relationship with their parent, and their product and labor market policies. Qantas was more closely involved in the strategic planning of JS's start up and continues to be involved as it retains 100 percent ownership of JS. For Qantas the establishment of JS reflected an attempt to try alternative strategies in the product and labor market arenas that would differ from its own legacy-carrier strategies. However, JS also built on the foundation it inherited from Impulse and tried to learn from the experiences of successful but contrasting LCC models (for example, SWA and Ryanair) as well as trying to avoid the problems experienced by other legacy carriers and their LCC offshoots.

In contrast, the Virgin Group was a much less interventionist parent. This is understandable since it is led from the UK, on the other side of the world. Within a few years, it had floated VB on the Australian stock exchange as an independent company. Branson's flamboyant style influenced VB's product market strategies, but VB had autonomy to devise its own labor market practices as a "greenfield" enterprise. In these circumstances VB's labor market policies were inspired less by those of the Virgin Group and more by those of SWA and of other exemplars of best practice human resource management in Australia and overseas.

The rhetoric of both LCCs emphasizes customer service and employee engagement, reflecting the approach taken by SWA. However, the extent to which the reality for their employees and customers matches the rhetoric is mixed and is subject to various contingencies and management styles. JS aims to adopt the best strategies of successful LCCs, particularly Ryanair and SWA. However, since Ryanair and SWA have contrasting strategies to achieve low-cost competitiveness (compare the "low-road" and "high-road" paradigms), it will be interesting to see how well JS can marry successfully the two models over the longer term. To what extent were the new LCCs' labor market strategies influenced by the strategic choices they adopted in the product market arena? While both companies initially focused on providing cheap fares for leisure travelers, they have gradually shifted to a more diversified approach and are beginning to adopt some of the product market characteristics of FSAs. This may have implications for the future recruitment and training of cabin crew and other frontline customer service staff who will be required to provide services to a wider range of customers than when these LCCs were focusing mainly on leisure travelers.

These LCCs recognize unions and negotiate collective agreements for at least certain sections of their workforce, but both also have forms of works councils for consultation with employees. They have so far avoided the overt industrial conflict that has sometimes characterized the airline industry. But given changes in labor market legislation implemented by the Australian government in 2006, these new airlines might seek to take advantage of opportunities to replace collective labor contracts with more individual ones. Such a development would probably meet strong resistance from unions. Both LCCs have recently begun international expansion, which affords them cost advantages over legacy airlines and opens up new markets. However, this move may exacerbate tensions between Qantas and its unions, which fear that Qantas may use JS to "offshore" and to undermine wages and working conditions of employees in the legacy carrier. Historically, it has proved difficult for three airlines to survive in the relatively small Australian domestic sector. It remains to be seen whether two LCCs can survive for long in the same market, alongside Qantas.

Acknowledgements

We thank the Australian Research Council. We are also grateful to Jetstar, Qantas, Virgin Blue, and the unions, who provided information and allowed us to interview them in 2005. We also appreciate the help and encouragement from academic colleagues, including Michael Barry, Jody Hoffer Gittell, Tom Kochan, and others in the Airline Industry Council of the Labor and Employment Relations Association.

References

Bamber, Greg J., Russell D. Lansbury, and N. Wailes (eds). 2004. *International and Comparative Employment Relations: Globalisation and the Developed Market Economies,* 4th ed. Thousand Oaks, CA: Sage.

CAPA. 2002. *Low Cost Airlines in the Asian Pacific Region: An Exceptional Intra-Regional Traffic Growth Opportunity.* Report, Centre for Asia Pacific Aviation, Sydney.

Creedy, S. 2004. "Union Agreement Gives Jetstar Flexibility." *The Australian,* January 31–February 1.

Harcourt, Tansy. 2004. "Qantas in Radical Plan for Jetstar." *Australian Financial Review,* February 25, p. 1.

Highfield, Bruce. 2005. "Retaining the Competitive Edge." Australian Human Resources Institute. Available at http://www.ahri.com.au.

Jetstar. 2004. "Queenslanders Celebrate New Careers with Jetstar." *Media Release,* August 27. Available at http://www.jetstar.com.au/pdf/news/20040830.pdf.

Joyce, Alan. 2004. "Address to National Aviation Press Club." *Media Release,* July 22. Available at http://www.jetstar.com.au/pdf/news/20040722PCA.pdf.

Virgin Blue. 2003. "Prospectus." Available at http://www.virginblue.com.au/pdfs/investors/shareoffer/Virgin_Blue_Prospectus_17nov03.pdf.

Virgin Blue. 2005. "Jobs@Virgin." Available at http://www.bfound.net/employers.aspx?CoId=43.