

Lean Production in the Air: Low-Cost Competition Taking Off in the Global Airline Industry and the Implications for Employment Relations: European Experiences

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Abstract

This paper examines the scale of the low-cost airline sector in Europe, some relevant business models, and the resulting employment relations effects that result, directly and indirectly, from these models. Illustrative examples of employment relations effects are provided for individual carriers.

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Introduction

In this brief paper we have essentially three sections: an outline of the scale of the low-cost airline sector in Europe, a discussion of the business model in the low-cost sector, and consideration of the resulting employment effects and implications. The material presented has been gathered by a variety of methods: existing literature, surveys, and other material in the public domain, together with some interview material gathered via “informal means” from union activists and lower line managers.

The Scale of the Low-Cost Sector in Europe

In the period August 2001–August 2003 the number of flights offered by the low-cost sector increased in total by 48 percent; in Europe the increase was nearly three times (140 percent) this average figure (Baseler 2004). By 2004 there were 60 low-cost airlines in Europe, carrying 80 million passengers (up from 47 million in 2003). This involved some 20 percent of the European market, a figure projected to rise to 40 percent by 2010 (*Economist*, January 27, 2005). More recently, a web-based exercise we conducted revealed that there are over 70 low-cost airlines; these were geographically dispersed with clusters in both eastern and western Europe.

There are numerous implications that follow from such a dramatic growth of the low-cost sector in Europe. Perhaps the most obvious effect has been the strong competitive pressure on the conventional carriers, which in turn has affected employment relations. In the UK British Airways (BA) has cut its pay roll by 25 percent in the past five years, but it is seeking to cut it by a further £300 million by March 2007. It is also facing a £1.4 billion pension deficit (a three-month employee consultation exercise is underway about this) and has experienced unofficial strike action in the last three summers (*Sunday Times*, October 2 and 9, 2005).

The Business Model: A Three-Way Split?

As an introductory exercise we initially compare and contrast two stylized business models of the full-service carrier (FSC) and low-cost carrier (LCC) models. This intersector comparison is then followed by a recognition of some important heterogeneity within the low-cost sector: here we talk about a “no frills” and “some frills” model in this sector. In Table 1 we initially present a “typical” profile of an FSC and LCC model organization.

It is clear from this comparison that the FSC carries much heavier overheads necessitated by the hub-and-spoke *modus operandi* and generally higher operating costs on account of the extra services provided, for which a premium price is charged. By contrast, the LCC has cut costs significantly by reducing overheads, providing a no frills service, and often using secondary

TABLE 1
Comparison of Full-Service Carriers' and Low-Cost Carriers' Business Models

Characteristic Feature	FSC	LCC
Generic Strategy	Differentiation	Cost minimization/cost leadership, entrepreneurial in character
Scale	Typically large	Generally smaller, but some major players
Operational Model	<p>Hub and spoke/multiple hub and spoke, linking with feeder routes</p> <p>Mix of short-, medium-, and long-haul routes</p> <p>Mainly short-haul routes</p> <p>Various aircraft types and engines</p> <p>Uniform aircraft types</p> <p>Moderate capacity utilization (c. 60%)</p>	<p>Point to point, no interlinking</p> <p>High capacity utilization, (c.70-80%), rapid turnaround between sectors, low margins</p>
Market	<p>Normally in competition with other FSCs, leading to differentiation by class (quality) of service, with high service image, including:</p> <ul style="list-style-type: none"> °Frequent scheduling and flight flexibility °Extensive in-flight services °Comprehensive ground services °Use of principal airports 	<p>Cheap travel sector of the market, segmentation by time of booking and choice of flight. Quality of service basic, for example:</p> <ul style="list-style-type: none"> °Little flexibility of flight changes (use or lose!) °No catering, or charged for °Ground services typically outsourced (but can be problematic, for example, EasyJet) °Often use of secondary airports
Inventory Management	<p>Pre-arranged tickets and seats;</p> <p>reservation system complex, due to feeder routes; use of travel agents</p>	<p>Inventory management simplified; direct or online bookings; ticketless, no use of travel agents</p>

Source: This table draws on ITWF (2002).

airports with cheaper landing charges. Faced with this competition, FSCs have attempted to fight back by adopting some of the LCCs' characteristics—such as online sales, more rapid turnaround times, and reduced use of travel agents or lower commission rates.

The best illustrative example is Aer Lingus. An operating surplus of 76 million Euros in 2000 became a loss of 52.1 million Euros in 2001, so a survival plan was drawn up by the airline, which saw it switch to a low-cost model. The key elements of this part of the model are set out in Table 2.

While Aer Lingus established a low-cost model based on price competition, it sought to balance this alongside frequency of flights, service enhancement, customer loyalty campaigns, international alliance membership, use of primary airports, and associated infrastructure. Thus, unlike Ryanair and EasyJet, the Aer Lingus model aims to provide some frills in the form of enhanced product features.

This some frills business model is not unique to Aer Lingus. It also characterized GO (the BA low-cost subsidiary), which was bought out by a senior management team (in June 2001) and then acquired by EasyJet in August 2002, and BMIbaby, the low-cost subsidiary (from January 2002) within the

TABLE 2
Detailed Elements of Aer Lingus Strategy, 2003

Element	Explanation
Low-Cost Structure	Aer Lingus has initiated further cost reductions (over and above the survival plan); cost savings of Ucircle130 million are envisaged.
Direct Distribution and Sales	Costs associated with sales and distribution have been reduced by cutting travel agent/trade commissions and focusing on sales through the airline's website. By 2003 32 percent of all sales were online.
Airports Served	Aer Lingus continues to use primary airports close to city centers.
Point-to-Point Services	Aer Lingus has moved toward direct point-to-point services with less emphasis on hubs and spokes.
Fleet Rationalization	In 2002 Aer Lingus had five different aircraft types, which was costly due to, for example, the associated maintenance and personnel. The company decided move toward a simpler fleet.
Low Fares	Aer Lingus moved toward offering much lower fares, with over 3 million low-fare seats in 2002-03. There was also a restructuring and reduction on business fares resulting in a total cost of Ucircle65 million.

Source: Aer Lingus (2003).

BMI Group (this group is a multispecialist carrier operating several specialized airlines within the BMI brand).

The Employment Relations Effects

The HRM literature suggests that for human resource policies to produce a significant, positive impact on the “bottom line” of any organization two critical preconditions must be achieved: (1) external fit (that is, a close two-way fit relationship between the nature of the business model and the composition of the HRM policy mix); and (2) internal fit (that is, the existence of a complementary, mutually reinforcing set of HRM policies). However, what still remains unresolved in the relevant literature is whether any positive bottom line impact comes via a negative impact on the workforce (“working harder”) or a positive impact on workforce attitudes and behavior (“working smarter”). To try and help provide some insights into this all-important debate we suggest that use could be made of two lines of approach:

1. Boxall (1999) draws a distinction in employment strategy between *human capital advantage* (recruiting and retaining outstanding human talent) and *human process advantage* (fostering learning, cooperation, and innovation). The detailed study of Southwest certainly suggests the importance of the human process advantage (Gitell 2003).
2. If we combine the insights of the HRM literature with that of the employment relations literature, an individual research theme to usefully pursue may be the notion of “management style.” This notion, which has been particularly popular in the British employment relations literature, offers a number of categorizations of management style that are based on attitudes toward the workforce as a source of competitive advantage and toward trade unions, which potentially offer insights into the use of particular human relations policies with their important consequences for shaping employee attitudes and behavior (Purcell 1987).

In summary, the nature of employee attitudes and behavior is likely to vary considerably within the low-cost airline sector as a result of differences in (1) the basic business model (no frills or some frills), and (2) the resulting mixture of employment relations policies, which will also be shaped by (a) the priority attached to a human process advantage approach and (b) differences in management style.

The Aer Lingus case certainly illustrates the powerful, direct impact on industrial relations of a change in the business model. Post September 11 the

main focus there has been on cost reductions and restructuring to be achieved by redundancies, job restructuring, greater flexibility, and pay freezes. The predictable result has been an increase in industrial relations activity with particularly heavy use being made of the labor relations institutions of the state. There have been major disputes over company proposals for compulsory redundancies, proposed amendments to the pension scheme, staffing levels, and outsourcing. These disputes have seen the industrial relations temperature at an all-time high, with an independent consultant expressing concern at the almost nonexistent bargaining relationship between the parties.

Turning to the UK, the findings from a large-scale survey conducted in 2002 of 4,765 unionized UK pilots, which obtained 1,451 responses, indicated considerable variation in employee satisfaction with different aspects of their work. In Table 3 we present separate results for flight crew satisfaction at GO ($n = 27$), EasyJet ($n = 61$), and BMI ($n = 95$).

The respondent numbers in all three cases are small, but what is so obviously striking is the much higher level of reported satisfaction at GO. For present purposes it suggests that reported satisfaction was higher in the some frills business model of GO as opposed to EasyJet (no frills). However, the nature of the business model would not appear to be the sole answer; the BMI satisfaction figures are higher than EasyJet, but not nearly as high as GO. The answer in the case of GO would appear to be the strong emphasis on human process advantage. The essence of their approach in this regard is well captured by the former chief executive, Barbara Cassani, whose perspective on the company involved the comments below:

Develop an antagonistic relationship with unions and allow poor employee morale to eat away at your organisation. *No thanks, I'd*

TABLE 3
Comparison of Human Resource Management in Low-Cost Carriers

Aspect of Work	Flight Crew Satisfaction at Go (%) ($n = 27$)	Flight Crew Satisfaction at EasyJet (%) ($n = 61$)	Flight Crew Satisfaction at BMI (%) ($n = 95$)
Management of Human Relations	89	23	27
Management of Industrial Relations Problems	85	3	5
Mean Satisfaction	81.7	41.4	52.8

seen enough of that in the US airline industry. (Cassani and Kemp 2003, 43)

Run the airline in compartments so one part has no idea what's going on anywhere else. Make sure your pilots never meet or talk to commercial people. And vice versa. *My personal bete noire.* (Cassani and Kemp 2003, 44)

Hire pilots and not pay attention to their personalities—pilots just fly planes and cabin crew should be hired for good looks, shouldn't they? *Sorry but no; this one really winds me up.* (Cassani and Kemp 2003, 44)

This is such an important insight in relation to the low-cost airline sector in view of the ITF survey (ITWF 2002), which reveals that the majority of recruits to the low-cost sector come from jobs in the aviation industry, many of them already members of relevant trade unions. In short, by what means have traditional employee relations attitudes and behavior been changed?

The human process advantage approach places great emphasis on the selection stage in which one tries to identify individuals who fit the company philosophy rather than the individual job (that is, the GO approach). But this can easily be undone by the effect of “management style.” The management of BMI claim to have implemented a full complement of sophisticated HR practices, but satisfaction levels in the 2002 survey (see Table 3) were relatively low in some aspects of the job. This raises all-important questions about how the nature of “management style” can adversely impact the implementation of a full complement of sophisticated HR policies, and hence not provide the desired impact on employee attitudes and behavior.

Summary

In summary, the major points emphasized here are the following:

- The existence and potential value of analyzing the low-cost sector in relation to the full-service carrier sector by utilizing a business model with three segments: the full-service carriers (all frills) and the low-cost sector (no frills and some frills).
- The nature of the business model adopted (particularly if a change from one model to another model is involved) has important direct effects on employment relations. However, the above point should not imply a straightforward mechanical relationship: the notion of “management style” and the relative emphasis on the human process advantage may also be highly relevant as explanatory factors.

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