

One Year Later, Airlines Struggling With Fleet, Capacity Issues

In the last year, the airline industry has faced difficult and unprecedented operational decisions to adjust to post-9/11 market demand. Everyday business is now very different and the new conditions of the marketplace are requiring airlines to make extraordinary management decisions, including applying for Chapter 11.

PERCENTAGE CHANGE IN PASSENGERS, REVENUES AND OPERATING EXPENSES
FIRST HALF 2002 VS. FIRST HALF 2001

	EPAX	Revenue	Operating Expenditures	Non-Security Capital Expenditures
1	-10.90%	-4.70%	3.00%	-58.60%
2	-18.50%	0.90%	-8.90%	-63.90%
3	-8.45%	-2.90%	34.00%	n/a
4	-24.00%	-16.00%	2.00%	0.00%
5	-6.96%	-5.00%	16.40%	-96.60%
6	-8.03%	-3.00%	15.80%	-7.00%
7	-50.00%	0.00%	0.00%	0.00%
8	-20.08%	-14.60%	28.00%	n/a
9	18.00%	0.00%	-3.00%	0.00%
10	-29.90%	0.50%	2.80%	0.00%
11	1.70%	10.30%	11.90%	0.00%
12	-3.93%	-3.00%	12.00%	-31.00%
13	24.00%	-2.00%	-2.80%	0.00%
14	-50.00%	-85.00%	5.00%	-35.00%
15	-11.00%	0.01%	0.02%	-95.00%
16	-9.00%	4.60%	-7.60%	n/a
17	-35.00%	-15.00%	100.00%	n/a
18	-9.70%	-9.40%	5.60%	-13.20%
Average	-10.66%	-8.02%	11.90%	-23.59%

Airline restructuring is affecting the supply of flights and available seats in most markets. Numerous jobs have been eliminated and many more are threatened; wide-ranging negotiations with unions and other airline workers are still taking place. As of mid-August 2002, USAirways had filed for Chapter 11 and United Airlines has announced that it may consider this step as well if it cannot reduce its costs to meet the needs of the Airline Transportation Stabilization Board. Smaller carriers, such as Midway and Vanguard, have not been as lucky and will effectively go out of business.

Most of the largest U.S. airlines, based on information supplied by the individual carriers, have reduced capacity by 10-20 percent in comparison to the same month one year ago. The exception is Southwest, which since December 2001 has offered approximately 5 percent greater capacity. Continental Airlines also increased capacity in June 2002 compared to the same 2001 month.

The airline industry is replacing short to medium range aircraft (such as 737s, 727s and DC-9s) with regional jets and even turboprops to eliminate excess seat capacity and take advantage of the lower costs of their affiliated commuter airlines. The capacity cutbacks have increased load factors. However, the drastic reduction in the number of available seats will have an impact on frequencies, air fares and total landed weight at most airports, a major customer service cost.

Most airlines have been earning 5 percent to 15 percent less in revenues in comparison to the same month one year ago, with the exception of Southwest (close to last year's revenues or somewhat higher) and USAirways (close to 20 percent less).

At least today it appears that all passengers—leisure and business—are making purchase decisions heavily based on price, giving low-fare airlines a significant advantage. Without a doubt, the presence of Southwest, Air Tran and Jet Blue bestows on any given airport the "Midas" touch, with few exceptions. For exam-



ple, Long Beach (Jet Blue), Flint (Air Tran) and Midland/Odessa (Southwest) have recently seen their air service index increased by over 30 percent (August 8-14, 2002 versus September 1-7, 2001).

Airport Adjustments

IMG recently contacted airports about the impact of 9/11 and the aviation recession. Eighteen airports provided complete answers to the survey, which asked about changes in four areas – passenger levels, revenues, operating expenses and capital expenses – in the first half of 2002 compared to the same period of 2001. The answers portrayed a good illustration of what the new airport reality is, as shown in the chart on page 22.

Overall, airports have endured a significant change in the way their businesses are run. Their bottom lines were affected by airline performance, but multiple variables such as airport size, location, type of traffic generated (general aviation, air taxi, air carrier or military), type of contract (compensatory versus residual) and the presence of a major airline or low-cost carrier dominating the market will determine how airports will ultimately weather the drought.

In general, passengers are still down from pre-9/11 levels by about 8 to 10 percent. Most regional airports have been able to remain afloat but have seen their revenues decrease and their operating expenditures rise. Airports' handling of non-security capital expenditures varies significantly, as expected, since it is difficult to make short-term changes in ongoing capital programs.

Airports with significant cargo presence like Memphis and Louisville have seen decreased numbers of passengers, but their cargo volumes helped them hold their balance in terms of total revenues. Memphis lost 81 daily scheduled passenger flights in October 2001, but

has since recovered 40 flights even when it increased terminal rates to meet bond covenants. Both Louisville and Memphis have decreased non-security related capital expenditures in the first six months of 2002.

Smaller airports like Panama City, Florida, have lost flights because mainline carriers have reallocated the equipment of affiliated carriers to other markets in which larger aircraft is being retired or scaled back. Eugene Airport's reduced landing weights due to aircraft downsizing and loss of flights led to increases in landing fees.

Of course, cost-cutting measures are crossing over to the airport arena as well.

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Airlines continue to emphasize the importance of keeping airport costs as low as possible.

The new airport security measures have added the burden of increased dwell times for passenger screening and the need for security-related capital expenditures that, in most cases, have delayed other non-security related capital expenditures.

Courses of Action


Most airports are painfully aware of the risk of losing frequency of service or service altogether. Unfortunately, airline decisions are generally outside of the control of airport managers, yet airports have some influence on airline scheduling decisions. Most importantly, airports should be very vocal in communicating with carriers how important service is for the airport and the community. Proactively approaching the airlines before service decisions are made is key to maintaining service frequencies. One small hub reported that it took a strong stance on the high prices of its dominant airline; within a month of sending the letter, average fares decreased significantly. Whether this was the only reason for the fare decrease will never be known, but the effort came at little cost.

Second, keeping costs low is always essential. Yet, this has to be carefully balanced with maintaining service—to airlines and passengers—most importantly by keeping delays to a minimum. In some cases, active marketing, usually in conjunction with the local community, which may include discounts, travel banks and outright subsidies, may help sway existing carriers and new ones to maintain service or to offer new service. Nevertheless, since airport costs are generally only 5-8 percent of an airline's total costs, a reduction in this area alone is unlikely to "make or break" an airline's service decisions.

Third, having the right, well-managed facilities available at the right time is essential. One medium hub we recently talked with believes that it could attract a low-fare carrier if it only had the facilities to allow for the required 8 to 10 turns per day. In addition, keeping a productive, customer-friendly workforce has become an important variable in the struggle to

sustain and foster the growth of future passengers.

Finally, the remarks of Glenn Januska, A.A.E., airport director of Sioux Gateway Airport in Sioux City, Iowa, summarize how many are feeling in the business: "It's hard to find a lot to be optimistic about with the airline industry at this time, at least at a small non-hub facility. However, with change comes opportunity. The industry certainly is in a state of change. We are looking to take advantage of any

opportunities that present themselves as the industry moves toward 'normalcy,' whatever state that will be." 

Has this reflected the experience at your airport? If you would like to share your ideas and information, please e-mail to wradall@imggroup.com or spage@imggroup.com.

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