FLYING THE COMPETITIVE SKIES: U.S. AIRLINE INDUSTRY

Dale Krueger and Denise Bartles

According to a *Fortune* Magazine article entitled "Airlines, Why the Big Boys Won't Come Back," the traditional airline industry (the majors) has been facing major competitive changes that were brought about as a result of the business practices of the discount airlines. For the six major airlines that were established prior to deregulation of the industry—American, United, Delta, Continental, Northwest and U.S. Airways—the competition has been so intense (with soft economic conditions) that they have been unable to raise prices sufficiently to cover higher fuel costs, labor costs, and security costs.

As a result, the majors have lost market share and the trend apparently has continued as the discounters, principally Jet Blue, America West, and Southwest, have continued to increase their market share. The discounters now control 25% of the market. The question is whether the majors can adapt to the external environmental threats and the competitive industry environment, or will they continue to lose market share and eventually go out of business. With the different business models in the airline industry, the questions become: What is the forecast and what are the possible scenarios in the airline industry?

Despite the airline industry's lack of profitability, an editorial in the *Washington Post* entitled "Airline Mogul Remains Upbeat," writer George Will states that Doug Parker, president of America West Airlines, has remained optimistic. He has attributed this optimism to America West's hubs. America West's hubs in Phoenix and Las Vegas enjoyed tremendous economic expansion in the last 10 years.

Parker, however, indicated that there are far too many airlines in an industry that has overcapacity. He suggested that causalities are inevitable, and with the industry competition, each airline has to put together various strategies to increase market share, maintain market share, or downsize the airline in an attempt to differentiate its service, while at the same time avoiding bankruptcies or entering bankruptcies to reorganize.

The Structure of the Airline Industry: Major and Discounter

There are two basic types of operational models used by the airline industry—the hub-and-spoke and the point-to-point. United, American, Northwest, Continental, Delta, Air Tran, U.S. Airways, Midwest Airlines, Frontier, and America West operate a hub-and-spoke system. In the hub-and-spoke system, flights from all over the United States fly into major hubs where passengers disembark ending their flight, or they take a connecting flight to the city of their choice. This model allows each airline to fly passengers from smaller cities into the hub and then funnel these passengers to destinations on its own airline or on a regional carrier airline. The hub-and-spoke model permits airlines, with the help of the regional carrier (with its smaller aircraft), to serve small cities, which have insufficient traffic flow to support a major airline. For example, America West, now U.S. Airways, has operated two hubs, Phoenix and Las Vegas, and with the help of its regional carrier, Mesa Airlines, it serves many other smaller sized cities in the Western United States. Delta has hubs in Atlanta, Georgia; Cincinnati, Ohio; South Carolina; and Utah; Northwest has hubs in Minneapolis, Minnesota; and Detroit, Michigan; United's hubs are in Chicago, Illinois; and Denver, Colorado; American's hubs reside in Chicago, Illinois; and Dallas, Texas; and Continental's hubs are located in Newark, New Jersey; and Cleveland, Ohio. The airlines that use the hub-and-spoke model usually have a variety of different types of planes; therefore, to service these different types of planes, maintenance, training, and inventory costs (plane parts) are more costly because of variety of aircraft. However, these airlines are able to maintain and increase load factors from smaller hubs to larger hubs to maximize revenue.