

RYANAIR STRATEGY REPORT



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APRIL 19, 2013



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EXECUTIVE SUMMARY

Ryanair Holdings plc (NYSE: RYAAAY)¹ was established in 1985, making the company Europe's first low cost airline. Today, they are Europe's third largest carrier by number of passengers flown and seventh largest by revenue. In March of 2013, Ryanair and Boeing agreed on a transaction of 175 new Boeing 737-800 jets, the largest deal ever for an Irish airline². Ryanair operates out of 168 airports (51 of which are bases), 28 countries, and has a fleet of over 300 Boeing jets already in operation³. Ryanair flies over 1500 different routes and carried more than 79 million passengers in 2012. Ryanair boasts having the best customer service in the industry: with 92% of flights leaving on time, the fewest number of flights canceled, and the least number of bags lost in the industry.

By flying only profitable, point-to-point routes, and cutting costs once considered standard in the industry, Ryanair has established itself as Europe's cheapest airline. With an average ticket price of €46, Ryanair has positioned itself much cheaper than main competitor easyJet, which had an average fare of €71 for fiscal 2012. Ryanair posted revenues of €4.325 billion in fiscal 2012, up 19% from the previous year. Profits grew roughly 25% to €503 million over the same span.

As Ryanair expands, it is important that they continue to find innovative ways to keep costs down and offer the cheapest tickets in Europe. As of now, they attract customers with the lowest prices, reliable air travel, and controversial advertising. CEO Michael O'Leary has continually attracted press coverage with controversial statements such as labeling EU regulations as "communist"⁴, and with proposals such as charging to use the bathroom⁵. However, for an airline that sells such cheap seats, it may be that any press is good press. As other airlines continue to cut costs as well, Ryanair will have to make sure its image is in good enough standing to retain its customer base. If Ryanair can successfully continue to lead the industry in cutting costs and expanding to underdeveloped markets, they should maintain their status as the number one low cost carrier in Europe for years to come.

¹ <http://finance.yahoo.com/q?s=RYAAAY>

² <http://www.forbes.com/sites/davidewalt/2013/03/19/boeing-lands-a-15-6-billion-737-order-from-ryanair/>

³ www.ryanair.com

⁴ <http://www.europolitics.info/sectorial-policies/ryanair-s-o-leary-takes-on-eu-bureaucrats-art350194-46.html>

⁵ <http://www.dailymail.co.uk/news/article-2251647/Brave-soul-needed-OLearys-sidekick-Ryanair-admits-worst-job-PR.html>



COMPANY BACKGROUND

Ryanair was founded in 1985 by Christopher Ryan, Liam Lonergan, and Tony Ryan (after whom the company is named). The initial flight took place between Waterford, Ireland and London Gatwick on a 15-seat airplane. The plane was so small that prospective flight attendants were required to be less than 5'2" tall. With just 51 employees and 5,000 passengers in its first year of operation, Ryanair was one of the smallest commercial airlines in the world. Founded during a period of European air travel regulation, Ryanair had the intent of breaking the duopoly on London-Ireland flights held by British Airways and Aer Lingus. In 1986, a new EU ruling brought about partial air travel deregulation, which stated that airlines could operate new international routes as long as one of the two countries agreed. As a result, Ryanair opened a second route from Dublin to London Luton in direct competition with the duopoly. The Irish government refused approval for the route in order to protect Aer Lingus, but Margaret Thatcher and the deregulation-seeking British government approved the addition of Ryanair to the route. While Ryanair's price of £99 for the Dublin-Luton is quite high by today's norms, it far undercut the £209 regulated rate offered by British Airways and Aer Lingus. Despite offering just two short routes, Ryanair became Europe's first low-cost carrier and changed the continent's air travel pricing structure forever.

In the late 1980s, Ryanair underwent rapid expansion, acquiring new airplanes and expanding its route offerings. Flights outside of the United Kingdom were available and Ryanair became a major player on all main routes within the United Kingdom. In its attempt to become a serious competitor to Europe's established airlines, Ryanair introduced a frequent flyer program and offered business class seats. Neither of these offerings was successful, however, and both were eliminated within a year.

Despite rising passenger numbers, Ryanair was losing money. Ryanair was a low-fare airline, but not a particularly low-cost airline. It attempted to offer similar service as the major airlines at a lower price, and with the major airlines starting to lower their own prices to force Ryanair's down even further, Ryanair could not survive. After restructuring in 1990 and a £20 million cash injection from the Ryan family, Ryanair installed new management and lowered prices even more, vowing to offer the lowest fares in every market it served. This was accomplished by eliminating especially costly routes, increasing flight frequency on profitable routes, and moving to a single type of airplane



in order to reduce maintenance expenses. By flying between regional airports with lower landing costs and quicker turnaround times, profitability was attainable even with the cheapest flights Europe had ever seen. The new CEO, Michael O’Leary, followed Southwest Airlines’ lead and eliminated free meals and beverages during flights, a radical move for the European airline industry, but one that soon paid off. The Gulf War resulted in diminished passenger numbers in 1991 (the only year passenger numbers have ever declined for Ryanair), but with O’Leary’s cost-saving measures in place, Ryanair managed to break its streak of unprofitable years.

When the EU deregulated its airline industry in 1992, allowing for non-national carriers to fly between any EU states, Ryanair seized the opportunity and expanded rapidly. 1995 saw Ryanair take over from British Airways and Aer Lingus as the single largest airline on every route it offered to and from Dublin. A successful IPO in 1997 raised previously unattainable amounts of capital, and in 1998, Ryanair bought 45 new Boeing jets. In 2000 the airline launched its website, and within a year, three quarters of all bookings were made online. In April 2003, Ryanair acquired Buzz from KLM, and by the end of 2003, the airline flew 127 routes. Ryanair recorded its first loss in over a decade during the second quarter of 2004 (€3.3 million), but the expansion of the EU in 2004 opened more profitable routes, particularly in Eastern Europe, and Ryanair quickly regained profitability. In 2006, Ryanair posted half-year profits of €329 million during which passenger traffic grew by more than a fifth and revenues rose by a third to €1.256 billion. Soon afterwards, Ryanair attempted to takeover Aer Lingus, but its €1.5 billion euro offer was rejected. On 1 December 2008, Ryanair again offered to takeover Aer Lingus, this time with an all-cash offer of €748 million, but the Irish government, who possesses a large stake in Aer Lingus, denied the takeover for competition concerns.

In June 2009, Ryanair reported an annual loss of €169 million. In October 2009, Ryanair eliminated all traditional check-in desks in favor of simple baggage drops in a new cost-saving move. Later that year, Ryanair announced negotiations with Boeing over 200 aircraft order had failed. Despite this setback, profits rose to €318 million the following year, even with the recession’s effects. As of February 2010, Ryanair had an average fare of €32, less than half that of competitor easyJet at €66. In June 2012, Ryanair made another bid to buy Aer-Lingus, but the European Commission blocked this bid since the combined companies control 80% of flights between the UK and Ireland.



Ryanair's growth has been extremely impressive during a period in which established major airlines have struggled mightily and gone bankrupt in many cases. Between 1985 and 2011, Ryanair's passenger numbers increased by more than 15,000-fold, from 5,000 to nearly 76 million. Europe's first low-fare airline has maintained its position of offering the cheapest flights, and with rapid expansion still occurring into new airports, Ryanair's passenger numbers continue to grow.



FINANCIAL ANALYSIS

Profitability & Shareholder Returns

Ryanair, perhaps Europe's best-known low-cost airline, has also consistently been among the continent's most profitable. Although Ryanair was not immune from an industry downturn following the financial crisis in 2008-2009, the company rebounded to solid profitability in fiscal 2010. For fiscal 2012, the company posted a profit of \$747 million and revenue of \$5,855 million, or a net profit margin of approximately 13%. 2012's numbers compare with net income of \$528 million in fiscal 2011 and revenue of \$5,117 million; this translates to a net profit margin of roughly 10%. In comparison, competitor easyJet had a net profit margin of only about 6.5% in fiscal 2012 and fiscal 2011.

Airline Specific Metrics

Available seat-miles ("ASMs"), a measure of passenger capacity that multiplies the total number of seats by the number of miles flown, increased 12.3% in fiscal 2012 to 71.1 billion. Three factors drove this increase in capacity: a net increase of 22 737-800 planes in the Ryanair fleet, a 5.8% increase in the number of flights flown, and a 6.1% increase in the length of each segment.

The airline's revenue passenger-miles ("RPMs") increased approximately 10% from 53.2 billion in fiscal 2011 to 58.6 billion in fiscal 2012, largely because of the increase in ASMs over the previous fiscal year. Revenue from scheduled passenger service increased approximately 24% from €2,827.9 million in the 2011 fiscal year to €3,504.0 million in the 2012 fiscal year. Average yield per RPM was €0.053 in the 2011 fiscal year and €0.059 in the 2012 fiscal year. Average yield per ASM was €0.048 in the 2012 fiscal year, an improvement over the €0.045 figure seen in fiscal 2011. Cost per available seat-mile was €0.051 in fiscal 2012, an increase of €0.002 from the €0.049 seen in fiscal 2011. Higher fuel costs per ASM of €0.022 in the 2012 fiscal year were the primary reason for this cost increase.

Breakeven load factor in fiscal 2012 was 70%; the booked passenger load factor for the year was 82%, broadly in line with the norms for the US airline industry in the same year. The breakeven



load factor for fiscal 2011 was 2 percentage points higher, at 72%, and the booked passenger load factor in the 2011 fiscal year was 83%.

Ryanair has a policy of grounding approximately 80 of its aircraft during the slow winter travel season. Management believes that the grounding of these aircraft does not materially affect profitability, as the costs of operating these aircraft during the period of low demand would slightly exceed the revenues derived from such operation.

Liquidity & Solvency

Revenues

Scheduled passenger revenues represented 79.8% of Ryanair's total revenues fiscal 2012, an increase over the 77.9% of total revenues in the 2011 fiscal year. The remaining revenue category, ancillary revenues, was 20.2% of total revenues in fiscal 2012 versus 22.1% seen in the 2011 fiscal year.

Ryanair's ancillary revenues, which comprise revenues from non-flight operations, in-flight sales and Internet-related services, increased 10.6%, from €801.6 million in fiscal 2011 to €886.2 million in fiscal 2012. On a per-passenger basis, ancillary revenues increased to €11.69 per booked passenger in fiscal 2012 from €11.12 the year before. The rate of increase in revenues from all ancillary revenue categories, including baggage fees, vacation packages, and travel insurance, exceeded the increase in overall passengers booked.

Costs

Ryanair's largest cost, fuel and oil, increased by 29.9% from €1,227.0 million in fiscal 2011 to €1,593.6 million, or 36.2% of total revenues, in the 2012 fiscal year. For comparison purposes, fuel costs as a percentage of revenues for the eight largest US airlines were 31.6%. The factors contributing to this 29.9% increase in overall fuel costs were an 18.2% increase in average fuel prices paid, a 10.5% increase in the number of hours flown, and a 6.1% increase in the average sector length. Ryanair's average fuel price rose from €1.76 per U.S. gallon in the 2011 fiscal year to €2.08 per U.S. gallon in the 2012 fiscal year (after taking into account fuel hedging activities).



Aircraft rental expenses are relatively small for Ryanair, as the company finances most of its planes. Rental expense was €90.7 million fiscal 2012, a 6.7% decrease from the €97.2 million reported in the 2011 fiscal year. Three aircraft were returned to their lessors during fiscal 2012, and newer leased aircraft had lower costs. Larger airlines are typically able to negotiate better prices on leases and aircraft purchases, so Ryanair's costs per aircraft have decreased as the airline has expanded.

Although Ryanair depreciates its aircraft over an estimated useful life of 23 years to a residual value of 15% of market value for new aircraft, the company disposes of its aircraft well before the end of their useful economic lives. Ryanair's aircraft operating lease agreements typically have a term of seven years, which closely correlates with the timing of heavy maintenance checks. Ryanair's depreciation and amortization per ASM decreased by 0.8%, but in absolute terms the costs rose 11.3% from €277.7 million in the 2011 fiscal year, to €309.2 million in fiscal 2012. The increase was primarily attributable to the addition of 14 owned aircraft (net of disposals) to the fleet during the 2012 fiscal year.

Maintenance and other costs increased by 10.8% from €93.9 million in fiscal 2011 to €104.0 million in fiscal 2012. As Ryanair's fleet and average sector length have grown (its larger number of planes are flying more), the company's maintenance costs have increased as well.

Stock Performance

Price/Sales	1.81
Price/Equity	14.45
Price/Book	2.74
Price/Cash Flow	8.23
Current Ratio	2.14
Quick Ratio	1.95
Leverage Ratio	2.72
Total Debt/Equity	1.14
Interest Coverage	7.73



Analyst Expectations

As Ryanair stock has risen by over 40% in the last six months, thereby beating the S&P 500 Total Return Index by approximately 12 percentage points, analyst ratings have fallen considerably to mostly neutral sentiment. In December 2012, of ten analysts surveyed, seven had buy ratings on the stock, and the remaining three had a neutral outlook. In March 2013, of the nine analysts surveyed, three had buy ratings on the stock, five were neutral, and one had a sell recommendation. The



Market Research Team downgraded Ryanair from “buy” to “hold” in early February based on the stock’s significant outperformance of its benchmark in late 2012 and early 2013. According to data from Thomson/First Call, the mean price target on the stock is \$46.67; the median target is \$45.00. However, these estimates may not be as robust as those from other sources because only three brokers were surveyed. As of the close of the market on April 18, the stock traded at \$43.55.



COMPETITIVE ANALYSIS

Market Definition

The European airline industry has been tremendously active since the liberalization of the EU internal market in 1993 and the granting of cabotage rights in 1997. One of the main drivers behind the movement has been the emergence of low cost carriers, which now compete with full service network carriers (FSNCs)⁶, holiday carriers, regional carriers, and hybrid carriers. In 1998, low cost carriers had a significantly smaller share of the market than holiday carriers. In the next five years, however, low cost carriers almost tripled in size every five years. Their growth rate from 1998 – 2003 was 181%, which was topped by a growth rate of 272% over the next five-year span.

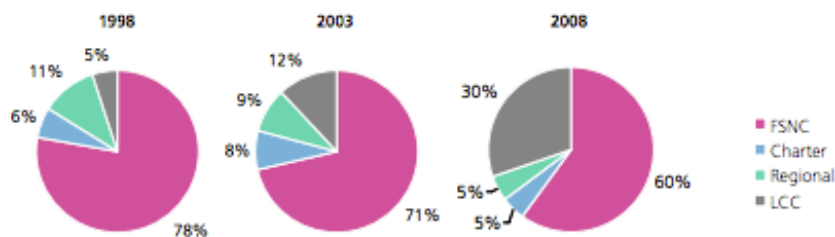


Figure 3-2: Market Share Development (various business models within geographical Europe)

Source: OAG

All together, the global airline industry rebounded from the US financial crisis of 2008-2009, increasing passenger traffic by nearly 6% from 2010 to 2011. Yet, 2012 faced volatile and high fuel costs. While load factors increased, overall demand went down. This past winter season (2012 – 2013) saw a 3.7% decline in the number of flights from the previous winter season for European airlines. The north and northeastern regions of Europe did experience an increase in flights in 2012, notably Norway, Poland, and the Ukraine. Going forward, jet-fuel prices will continue to challenge the airline industry; particularly as fuel prices have become increasingly more volatile.

Internal Rivalry

The emergence of new airlines onto the European scene since the mid 90's has heavily increased competition in Europe. The EU is one of the few regions that grants cabotage rights to all of its member states, allowing airlines to operate with the domestic borders of another country. The competition in Europe has grown to such a level that the top five airlines in Europe have a combined market share of 31%, whereas the five biggest US airlines have 67%. One reason

⁶ Also referred to as legacy carriers throughout this report



attributable to this low level of consolidation is the rapid emergence of low cost carriers. Given the relatively expansive nature of European airlines, the industry is poised to consolidate in the near future. According to a report by the European School of Management and Technology, three airlines have both the financial and competitive competence, along with a strong change competence, in order to spearhead the consolidation process in Europe: Lufthansa, Air France-KLM, and Ryanair⁷.

Although no airline has a dominant share of the industry at large, fewer rivals exist within sub-industry markets. For example, low cost carriers rarely compete with FSNCs on long-haul routes because low cost carriers focus primarily on point-to-point, short-haul routes. In the sub-industry of low cost carriers, Ryanair and easyJet dominate the market, each of which is over four times the size of the next largest low cost carrier. Even so, Ryanair carried 34% more passengers than easyJet in 2012.

Entry & Exit

Large barriers to entry exist for the airline industry. The primary barrier is the large fixed cost that accompanies airline operations and start-up. New, commercial Boeing jets range from roughly 75 million dollars to 243 million dollars to buy. Moreover, rental costs for slots at airports are vast, not to mention airplane maintenance, which generally account for 10% to 45% of yearly operating costs⁸, which reach the hundreds of thousands or even the millions of dollars mark. Limitations of airport slots also inhibit entry into the airline industry. In Europe, many airport slots are contracted out to airlines on a long-term deal in which slots are grandfathered from year to year as long as the airline continues to use the slot. Moreover, regulations such as requiring flights of a certain distance limit entry into the industry. However, despite these large barriers to entry, the vast deregulation of the mid 1990's drastically reduced the barriers to entry for the European airline industry. Before deregulation, airlines were largely nationalized, and independent entry into the market was difficult to impossible. Since then, low cost carriers and other carriers have entered at such a rate in that no commercial European airline controls more than 9% of the market share.

⁷ <http://www.esmt.org/fm/479/BB-108-007.pdf>

⁸ <http://www.aviationpros.com/article/10387195/maintenance-costs-significant-but-tricky>



The exit barriers for the airline industry tend to be much higher than entry barriers. There are strong dependencies across many interested parties in the airline industry. For one thing, governments feel compelled to protect full service national carriers that offer convenient access to less popular destinations in order to support tourism and business travel. Additionally, credit card companies which sign contracts with airlines (such as Delta's American Express card) benefit from keeping a troubled airline from liquidating. Airplane manufacturers also rely heavily on large contracts with airlines, and are sometimes willing to burden a shared loss of profits in a cyclical downturn. Due to the large disincentives of liquidation, many airlines operate within bankruptcy while trying to restructure to get back to profitability. Filing for bankruptcy allows airlines to restructure their labor contracts, which were often very favorable for legacy carriers due to the protection of the industry. Since deregulation, however, low cost carriers have broken into the market with much lower labor costs. Therefore, the ability to file for bankruptcy in order to renegotiate contracts serves as a practical barrier to exit. Coupled with the strong external incentives to keep a troubled airline flying, perhaps below profitable prices, such barriers to exit harm the airline industry's profitability as a whole.

Substitutes & Complements

Substitutes to air travel are primarily car, bus, and train transportation. For European areas surrounded by bodies of water, travel by boat is another option. As distances increase, air travel grows to dominate that market for travel due to its much faster speed of travel. One popular alternative for relatively long distances in Europe is high-speed rail, which has a well-established infrastructure in various European regions. European high-speed rail can reach speeds over 200 mph, which is roughly a third of the speed of your average commercial jet once air-born. Trains hold the advantage of taking passengers directly into city-centers in comparison to more remote airports. Trains also have shorter boarding times and tend to be more reliable, although the reliability varies greatly by country. In 2007, a group of high-speed rail providers teamed up to coordinate and boost cross-border, high-speed rail networks in Europe⁹. A Trans-European high-speed rail network is a stated goal of the EU. France built the first high-speed rail line in 1981 from Paris to Lyon. Since then, France's continued development of a high-speed rail network has landed the country as Europe's second largest high-speed rail system, behind only Spain. In large part because of its extensive rail network, low cost carriers have not taken as big of a market share in

⁹ http://en.wikipedia.org/wiki/European_high-speed_rail_network#Early_national_high-speed_rail_networks



France as they have in other major European countries: such as the UK, Germany, and Italy. Since airplanes are roughly three times faster than the fastest high-speed rails, trains and planes are relatively weak substitutes today. However, one main trend that could make trains more viable substitutes in the future is increasing oil prices.

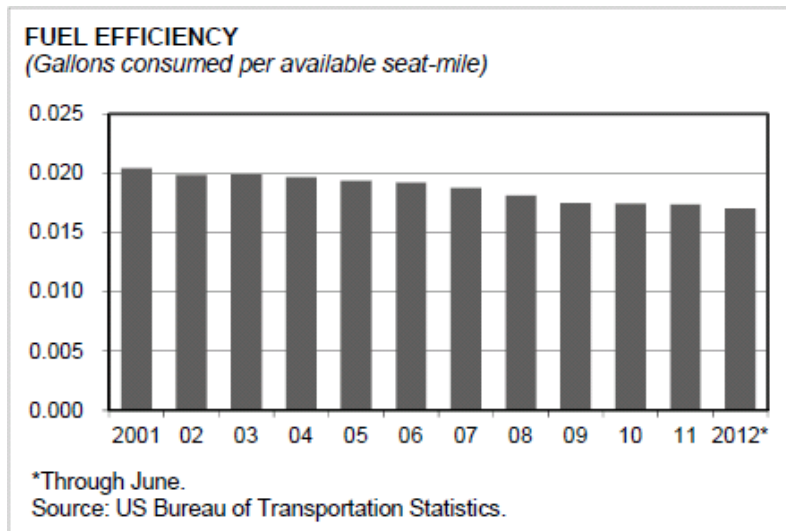
The main complements to airline travel are hotels and rental cars. This interdependence is evident by the frequent bundling packages offered by airlines, hotels, and rental cars. Companies such as Expedia, Travelocity, and Priceline seek to capitalize off of connecting these industries together in order to simplify the process for consumers. Although many customers ignore these bundles in order to seek better prices through separate reservation, hotels and rental cars remain strong compliments for airlines. Ryanair does not offer the option for customers to book bundled packages, yet you can search for hotels and cars separately on Ryanair.com.

Supplier Power

Suppliers tend to have a great deal of bargaining power in the airline industry. The primary suppliers for airlines are jet-fuel distributors, airplane manufacturers, and labor. Although not perfectly correlated with crude oil prices, jet-fuel prices have risen dramatically in recent years – a trend predicted to continue in the near future. In addition to increasing prices, jet-fuel has become increasingly volatile in price. Since oil prices tend to decrease as the economy worsens, increasing volatility in oil prices could actual mitigate the cyclical nature of the airline industry; which tends to boom and bust with the economy and external shocks such as the 9/11 terrorist attacks in the US or the volcanic activity of Iceland's Eyjafjallajökull in 2010, which covered European skylines with volcanic ash. Some companies, such as the US carrier Southwest, have developed a dynamic hedging strategy allowing them to use hedging to create a cap on prices in the future. While hedging oil prices generally results in a loss, it helps to protect companies from a sudden increase in oil prices. Delta, the world's largest airline, even bought an oil refinery in 2012 in order to help bring down fuel costs and ensure the airline has access to enough jet-fuel¹⁰. Oil prices will be naturally offset as aircraft get more fuel-efficient. One can see how oil usage has declined per ASM over the past decade in the table below.

¹⁰

<http://www.netadvantage.standardpoor.com/NASApp/NetAdvantage/showPublication.do?dataPosition=0&SPID=1558>



Airplane manufacturers and airlines are so interdependent that each has considerable bargaining power with the other. Only two major airplane manufacturers exist today, Boeing and Airbus. Given the relatively low competition in the airplane-manufacturing field, Boeing and Airbus likely have even slightly higher bargaining power than they otherwise would. On the other hand, as the air transport industry has struggled at times, manufacturers are reliant on airlines to continue ordering planes and requiring maintenance. One reason that competition is reduced between Airbus and Boeing is because there are tremendous costs associated with airplane maintenance that increases as the diversity of an airline's fleet increases. One of the major ways that low cost carriers save money is through purchasing similar aircraft to standardize maintenance procedures/parts. In fact, Ryanair recently bought 175 new Boeing 737-800 jets to add to their exclusively Boeing 737-800 fleet - a deal worth a market value of \$15.6 billion but likely heavily discounted by Boeing. In order for an airline to switch aircrafts, heavy investments must be put into to modify hangars, personnel, and other costs necessary to handle the change in fleet.

Labor costs are the largest expense in the airline industry, and thus wield extensive bargaining power with airlines. When the airline industry was nationalized and profit margins were higher, excellent employment conditions were one way in which airlines competed over labor. Powerful unions were created, generous pensions were promised, and wages were high. When the industry was deregulated, lower cost carriers entered the market with cheaper labor contracts. To compete, legacy carriers often had to file for bankruptcy in order to restructure their labor contracts



within the law. Current labor conditions vary vastly by airline; but, overall, the power of the labor supply has dwindled since deregulation of the airline industry.

Buyer Power

Buyers have little power within the air transport industry. Given the competitiveness of the industry, profit margins on ticket sales are already minimal. This absence of buyer power is evident by the non-effect that consumer dissatisfaction has had on the recent increase in ancillary fees. The regulatory bodies of the European airline industry have a great deal of power and act on behalf of consumers. Therefore, in a sense, buyers have collective power through regulation, but very little as individuals.

As a “consumer of airports”, airlines can have a great deal of power with airports when buying slots at airports. Ryanair frequently contracts with newer, secondary airports because of a higher level of buyer power. Consequently, Ryanair frequently gets very cheap rent for airport slots. Airports even provide labor for Ryanair or offer other incentives to bring the airline to its airport. Bigger airports, which have few open slots, yield much less power to airlines.



SWOT

<p>Strengths</p> <p>LCCs in general</p> <ul style="list-style-type: none"> • Homogenous, medium sized fleet • Small, regional airports • Ancillary fees <p>Ryanair</p> <ul style="list-style-type: none"> • Dominates new airports for cheap • Cheapest European LCC • Biggest market share of LCCs • New, young fleet 	<p>Weaknesses</p> <ul style="list-style-type: none"> • Public perception • Growth into congested markets • Trouble merging • Website
<p>Opportunities</p> <ul style="list-style-type: none"> • Growth in Eastern/Northern Europe • Improving image • Consolidation • Use for fleet during winter months 	<p>Threats</p> <ul style="list-style-type: none"> • Diminishing advantage as LCC with industry shifts • EU economic stability • Volatile/rising jet-fuel prices • Regulation

Strengths

First and foremost, Ryanair's biggest advantage in the European airline market is their ultra low cost for flights. Two firms, Ryanair and easyJet, dominate the low cost carrier subsection of the European airline industry. Ryanair flew almost 80 million passengers last year (2012), while easyJet flew just under 60 million passengers. Yet, Ryanair distinguishes itself as an "ultra low cost carrier" with an average flight price of €45 compared to easyJet's average fare of €71. Ryanair maintains low enough costs to enable ultra low cost ticket prices by operating a young, homogenous, medium-sized fleet; flying in and out of smaller regional airports, charging ancillary fees, and paying less for labor than other airlines. The table below summarizes low cost carriers' strategic measures to cut costs¹¹.

¹¹

<http://www.netadvantage.standardpoor.com/NASApp/NetAdvantage/showPublication.do?dataPosition=0&SPID=1558>



Table 2-1: Cost-cutting strategies by LCCs

Source: DLR

Cost category	Fleet		In-flight Service			Network		Marketing + PR		H.R.
	Homogenous Fleet	Young fleet	High-density seating, fewer galleys and toilets	No free meals and drinks, lounges and FFP's	No seat reservations	Use of smaller airports	No interlining, no flight connections	Focus on direct sales	"low prices sell themselves", aggressive PR	Variable remunerations, low hierarchies...
Unit Cost Category (costs per passenger kilometre)										
Maintenance	X	X	X							
Fuel		X	X			X				
Staff	X	X	X				X			X
Airport Costs			X		X	X	X			
ATC costs			X							
In-flight service				X						
Capital and leasing	X		X		X	X	X			
Marketing / Sales			X			X		X	X	
Overheads	X		X	X	X		X			X

The use of a young and homogenous fleet leads to a reduction of fuel, maintenance, staff, overheads, and – if the aircraft are bought in a large deal – capital costs. Ryanair operates exclusively Boeing 737-800 jets. To further save money on maintenance, Ryanair generally sells their aircraft on the secondary market before the first major maintenance repair. While in-flight, Ryanair saves money by not offering some of the services that come standard on most full service network carriers, such as free food and drinks. Ryanair also has higher density seating on planes, spreading out the high fixed costs of operating an airline over more passengers, while increasing variable costs per passenger only marginally. Ryanair also supplements costs with extensive ancillary fees, which account for roughly twenty percent of its revenue.

Ryanair also has a number of operational measures to reduce costs. By flying in and out of small regional airports, slot fees are cheaper. In fact, Ryanair has been successful getting start-up support from uncongested airports that they move into and often dominate. This support often includes providing labor, saving Ryanair the hassle and costs of investing in their own workers at a new destination. Smaller airports (and smaller aircraft) have shorter turnaround times, greater reliability



to leave on time, and fewer lost bags – especially considering that Ryanair flies only direct, point-to-point routes. To further reduce turnaround times, Ryanair withholds seat reservations, reducing boarding and deboarding times. Compared to an industry average of 60 minutes, Ryanair’s average turnaround time is only 25 minutes. To further save money on labor, Ryanair emphasizes productivity amongst employees, offering commission based incentives for flying hours and commissions for in-flight sales for flight attendants. Ryanair has an average cost of employee of €49,182 compared to over €70,000 for competitors Aer Lingus and easyJet¹². Ryanair also requires that passengers check in online, reducing personnel required at the airport terminal.

Weaknesses

Ryanair has faced ample criticism for some of its ancillary fees, customer service, and employee relations. Ryanair touts itself as a no frills airline, yet has fees that exceed those of other European low cost carriers. They charge €6 for online check in per person, and €60 if the passenger does not bring his or her own boarding pass or requires a reprint. Since the €6 fee is unavoidable (except on special promotional fares), many complain that this should be included in the ticket price.

Ryanair seeks to cut costs in any way possible, often leading to either not providing or charging for services that most people consider morally obligatory. In 2007, the Economist wrote that Ryanair’s “cavalier treatment of passengers” gives the company a “deserved reputation for nastiness.”¹³ Some notable instances of poor customer are in 2002 when the company refused to provide wheelchairs for disabled persons at London Stansted Airport and, also in 2002, when the company reneged on an offer to give their millionth customer a free travel prize. The company provides no means to contact them by email, a lack of service that was officially criticized by the British Parliament in 2006.

Although the lower labor costs and high labor productivity are strengths for the company, Ryanair faces frequent criticism for its employee relations. The airline refuses to recognize any unions, and one pilot won a lawsuit against the company after being fired for handing out a union form to one of his crewmembers¹⁴. The government of Norway has threatened a boycott of the company after

¹² <http://www.esmt.org/fm/479/BB-108-007.pdf>

¹³ http://www.economist.com/node/9681074?story_id=9681074

¹⁴ <http://blogs.mirror.co.uk/investigations/2011/03/ryanair-pilot-sacked-for-handi.html>



one ex-employee complained about working conditions¹⁵. In general, the airline is criticized for misleading contracts and unusual tax filing practices, such as requiring workers to set up bank accounts in other countries and paying them through those accounts.

The company has also struggled merging, with three failed attempts to buy Aer Lingus.

Opportunities

Ryanair currently operates short-haul, point-to-point flights within Europe, primarily the EU. One opportunity for them is to expand the market that they serve. Although they had planned to expand to offer cross-Atlantic flights, Ryanair recently announced it was abandoning plans to offer long-haul flights for the time being. One expansionary path that Ryanair does seem to be following is expansion in Northern and Eastern Europe. Not only did they just open a base in Zadar, Croatia, but the company also announced to add bases in Eindhoven and the Polish city of Krakow, and released a statement considering a new base in Slovakia.

Opportunities for growth outside of expansion revolve mainly around additional cost cutting techniques or additional ancillary fees. Ryanair has recently proposed removing the last ten rows of seats in order to offer 1.60 Euro tickets for flying in a standing cabin. Over its history, Ryanair has also proposed strategies such as removing all windows, charging to use the bathroom, and requiring passengers to either carry their own bags to the aircraft or face an additional fee.

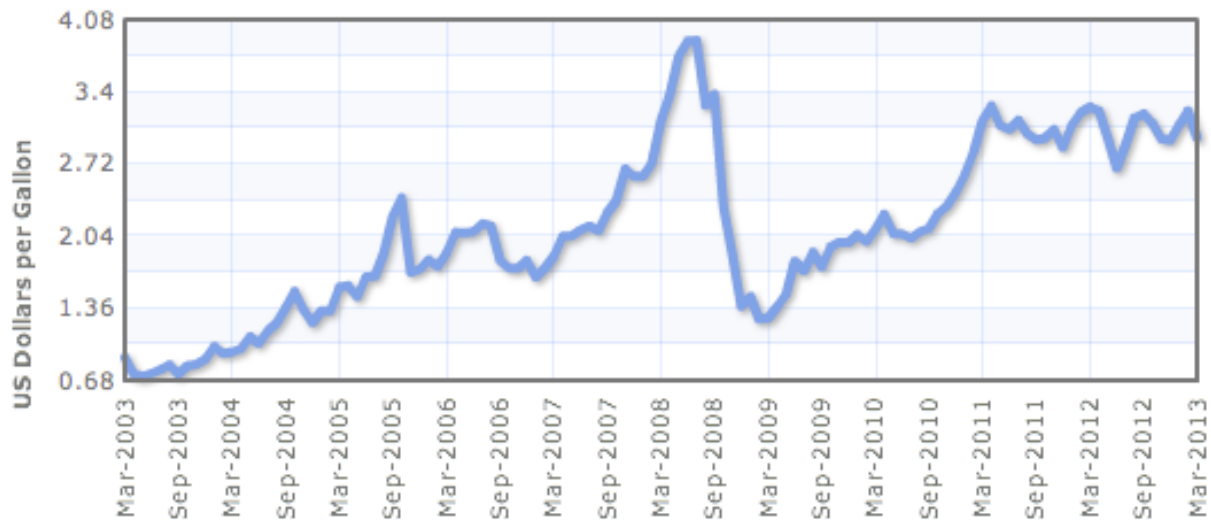
Threats

The main threats Ryanair faces come from competition, uncontrollable factors such as jet-fuel costs, and the policies enforced by the airline regulating bodies of the EU and Europe at large. Ryanair has excelled at developing point-to-point routes in geographic regions with potential prior to other low cost carriers. Yet, as low cost carriers continue to gain a market share and full service carriers continue to adjust their practices in order to compete with low cost carriers, competition for Ryanair will increase. Not only could this increased competition shift some of the consumer demand from Ryanair to other airlines, but Ryanair's buyer power could also fall – raising prices for slots at airports and reducing the support that they have received from less congested airports in the past.

¹⁵ <http://www.foxnews.com/world/2013/04/12/norway-leaders-threaten-boycott-ryanair-after-ex-employee-complains-about-work/>



The future jet-fuel prices will be a threat for almost all players in the airline industry. Not only are price levels a concern, but volatility in oil prices is also important – a trend that many analysts predict to increase over the next decade¹⁶. A graph of jet-fuel prices over the past ten years is below.



Other uncontrollable factors that serve as threats to the airline industry as a whole are economic shocks, as airlines are hurt when the economy is worse, and natural disasters that may disrupt the ability for airlines to fly in certain regions. Airlines can offset risks of sudden and extreme volatility with fuel hedging, for which Ryanair spent €320 million to hedge 90% of its fuel¹⁷, but the future of oil prices are a threat regardless.

¹⁶

<http://www.netadvantage.standardpoor.com/NASApp/NetAdvantage/showPublication.do?dataPosition=0&SPID=1558>

¹⁷ http://www.ryanair.com/doc/investor/present/quarter4_2012.pdf



STRATEGIC RECOMMENDATIONS

Before providing recommendations, let us consider possible trends going forward in the airline industry. When the industry was nationalized, airlines had exclusive rights to certain routes and could thus charge prices far above competitive levels. Airlines subscribed more to the hub and spoke model, allowing for less profitable routes because airlines made greater profits on main routes and placed higher value on customer loyalty. With increases in competition resulting from deregulation, low cost carriers have emerged on the scene with great success, flying more exclusively profitable routes at lower prices. As customers have shifted to fly with low cost carriers, full service network carriers have had to restructure, allocating more aircraft toward profitable routes and cutting labor costs. As the industry progresses, we will likely see a convergence towards a lower cost model than before regulation. However, governments will work to protect airlines that fly less profitable routes because of concerns for tourism and business, therefore regulation will be a key concern for airlines going forward as well.

Align Ancillary Fees with Costs

Ryanair is able to charge lower ticket prices than every other European airline because it does not include many services for free, leaving the choice up to the consumer as to which services to purchase. Ryanair makes twenty percent of its revenue from ancillary fees, and they are vital to the company's success. However, Ryanair has two genres of ancillary fees: fees that arise to account for the costs of a specific good or service and fees that take advantage of a consumer's desperation. While ancillary fees for services rendered or goods purchased are the catalysts for cheap ticket prices and should be expanded, fees that capitalize on consumer's desperation harm public perception and should be eliminated.

Examples of practical ancillary revenues are fees for baggage handling, in-flight refreshments and food, carry-on luggage, partnership deals with complementary companies, and flight changes. These fees are either partnerships with businesses and mutually beneficial (as in a Ryanair credit card) or are fees that account for the costs of services rendered by the airline. If Ryanair can expand these fees and continue to cut costs, their base ticket prices will stay low while making additional revenue for the airline. If a standing section is deemed safe, then such a move could be both profitable for



the company and helpful to consumers seeking ultra low cost tickets. Or, for example, charging a fee for minors flying without parents is appropriate because it increases work for flight attendants. Ryanair must continue to find innovative cost-cutting measures in order to retain their competitive advantage in offering the cheapest flights available.

Certain Ryanair fees vastly overinflate actual costs, and work only because the consumer is in a desperate situation. For example, Ryanair charges €70 to reprint a lost ticket. In 2012, Ryanair was forced to eliminate its “unlawful” debit card fee¹⁸ of €6 for online booking. Such fees, despite making money for the airline, are some of the main drivers behind the intense criticisms against Ryanair. Long-term, these fees are less likely to produce profits considering customers’ likely future aversions to flying with the airline. Eliminating “rip-off fees” may detract some ancillary revenue, but will ultimately protect Ryanair’s image and help retain customers if other airlines can produce more competitive prices.

Retain Large Market Share Amongst Low Cost Carriers

Ryanair’s recent purchase of 175 new Boeing jets increases its fleet by more than 30 percent. If demand can meet that supply increase, Ryanair will significantly increase its market share, especially amongst low cost carriers. Given the growth of consumer demand, even during Europe’s cyclical economic downturn, Bridges believes consumer demand will meet Ryanair’s expansionary hopes. The European airline industry is primed for consolidation. Increasing their fleet substantially will keep Ryanair as one of the foremost leaders when consolidation does occur; assuming they survive to reach that juncture.

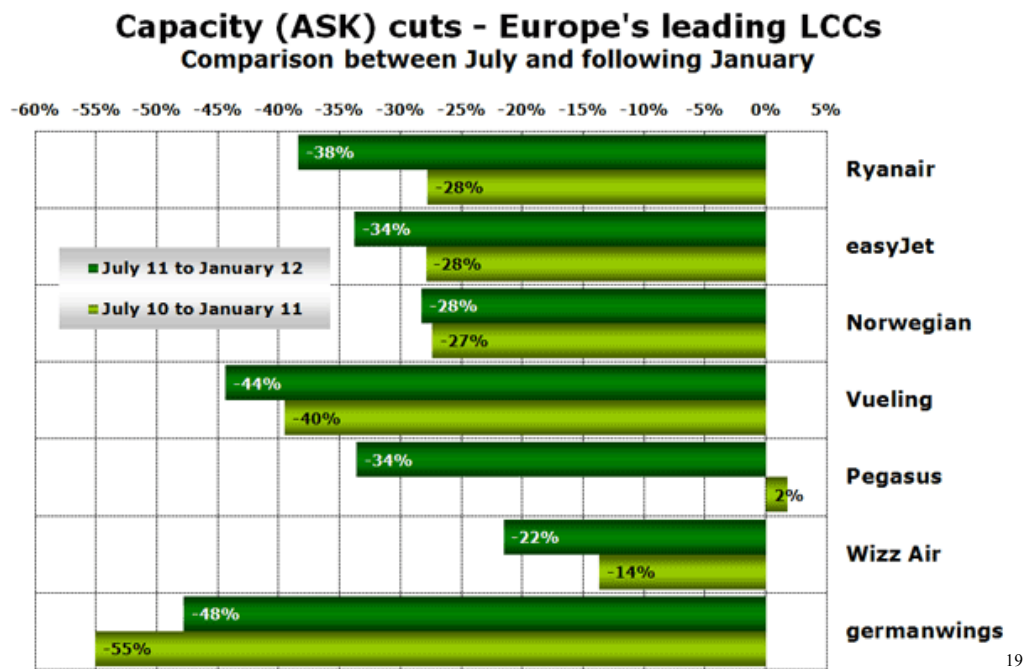
Utilize Fleet During Winter Months

Given that they have increased their potential market share drastically with their recent deal with Boeing, Ryanair should take some measures to insure against the large cash outflow, especially given the volatile and inflammatory nature of jet-fuel prices and the fragility of the current European economy. Ryanair has already insured against the volatility of fuel prices with ample hedging, but may want to take additional measures. Bridges recommends exploring potential renters for aircraft during winter months. Given the high costs of fuel, Ryanair grounded almost 40% of its aircraft in

¹⁸ <http://www.dailymail.co.uk/news/article-2240390/Anger-Ryanair-finally-scrap-unlawful-6-debit-card-fee--introduce-6-website-admin-fee-day.html>



January 2012. The graph below shows the capacity cuts (in available seat kilometers) across Europe's low cost carriers from July to the following January.



This strategic move increased load factors during the less busy winter months. However, this also resulted in 80 aircraft going unused for Ryanair. If they could rent the aircraft out to warmer regional airlines, than they could continue profiting from those planes. If those aircraft are incapable of getting to warmer destinations far away, perhaps they could rent out their planes to a full service carrier who could then rent out its larger aircraft to airlines in regions farther away. Given the tumultuous economic circumstances and the high costs of fuel, renting (rather than buying) aircraft may be an appealing prospect for southern hemisphere based airlines wishing to increase fleets during their summer months.

¹⁹ <http://www.anna.aero/2012/07/04/grounding-planes-in-winter-improves-profitability-the-new-network-planning-reality-explored-among-europes-airlines/>

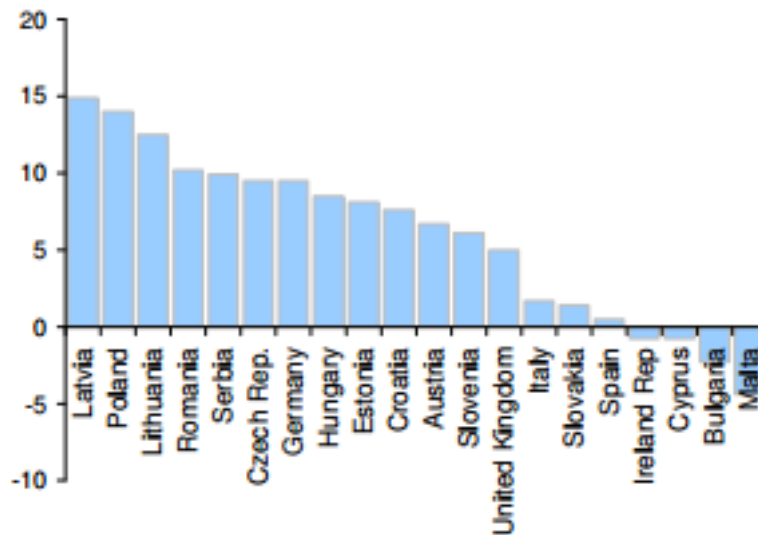


Expand to Eastern Europe

Bridges highly encourages Ryanair to continue rapid expansion into Eastern Europe. 12 of the 13 fastest growing countries by air travel in Europe were either part of Scandinavia, the Baltics, or Eastern Europe.

Foreign visits to select destinations

2012, year-to-date*, % change year ago



Source : TourMIS

*date varies (Mar-Jun) by destination

20

A large portion of Ryanair's competitive advantage is its early expansion into uncongested space. As the first-mover, Ryanair gets favorable deals with airports, dominates airports that will later increase in value, and seizes larger shares of consumer demand for point-to-point routes. Specifically, Bridges recommends expanding into Hungary, where Ryanair currently does not fly; and expansion in Lithuania, Latvia, and the Czech Republic, where Ryanair operates in and out of only one airport.

Conclusion

Ryanair has excelled at seizing the birth of the ultra low cost airline market in Europe. Their leadership has given them tremendous competitive advantages, enabling the airline to maintain low costs, high profits, and rapid expansion. However, as the European airline industry will continue to

²⁰ <http://europetravel.net/wp-content/uploads/2012/10/europe-visitors.bmp>



converge – an occurrence that ensued after the initial broadening of the industry post-deregulation – Ryanair must maintain its competitive advantage amongst airlines to maintain profitability. Through continued strategic cost cutting techniques, rapid expansion, and a large market share amongst low cost carriers, Bridges believes Ryanair will remain the lowest cost carrier in Europe. However, as other airlines approach Ryanair’s low prices, Ryanair will have to improve its image in the public eye in order to retain passengers. Regulation and fuel prices will be additional challenges that Ryanair must navigate, but given their unrelenting leadership amongst European airlines, Bridges believes Ryanair will continue to lead the European airline industry for years to come.



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