NAVIGATING RELENTLESS PRESSURE
AVIATION MARKET REPORT, ASIA
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MARKET SNAPSHOT

Competition in the Asian aviation industry remains intense. Traffic and capacity growth have continued to outpace other major aviation markets in line with faster economic development in the region. However, profitability gains remain elusive in an environment marked by pricing pressure and fuel price volatility.

New entrants and new business models are encroaching on the legacy airlines’ traditional sources of revenue, gaining share in intra-Asia markets and, to a lesser extent, key long-haul markets. Additionally, the “super connectors” concentrated in the Middle East have impact on traffic patterns between Europe and markets in Asia and Africa.

These competitive pressures are forcing legacy airlines to address key aspects of their business such as their network structures, growth rates and cost competitiveness. The combination of regulatory barriers and higher degrees of government ownership are slowing the efforts to address these issues while competitive pressures continue to build.
COMPETITIVE LANDSCAPE

In the past decade, profit performance of Asian airlines has changed from leading the industry to a lagging position, as measured by the International Air Transport Association (IATA).

Figure 1. EBIT margin development by key regions

Source: IATA Industry Economic Performance review, June 2018
INTERNATIONAL COMPETITION

One of the more significant sources of margin erosion has been the rise of three large Middle East carriers—the ME3. Emirates, Qatar and Etihad have strategically targeted traffic between Europe and Asia, which was once a source of profit for the largest Asian airlines. In the past 10 years, the ME3 have grown their widebody fleets by 10 percent per year, a rate that is four times faster than the Asian majors. In parallel with the aggressive capacity growth, the ME3 have built sophisticated hub structures designed to divert major intercontinental traffic through the region.

Today the ME3 carry more passengers than all Asian network carriers combined. These competitive dynamics have had a dramatic impact on yields. As measured in US dollars, yields have fallen at a compounded rate of 6.2 percent per year since 2012.

*Figure 2. Airline passenger traffic and yields*

*Source: Innovata, Airline financial reports*
CUSTOMER EXPERIENCE IMPACT

Passengers benefit from the increasingly competitive landscape in Asia, enjoying advantages such as:

**Lower fares.** Supply and demand influences fares more than input prices. With such abundant supply of capacity, fares are dramatically lower today (20 percent) than they were three years ago.

**Greater choice and transparency.** There are more ways for carriers to sell to customers. Fast-growing distribution channels (e.g. online aggregators) improve price transparency for customers. Carriers are attracting customers to their direct channels with innovative, tailored branded fares, and they are offering more packaged holiday products with airfare and hotels.

**More destinations.** New markets and destinations are becoming available to customers as LCCs and other operators expand their networks.
VIEW FORWARD

Competitive threats affecting Asian airlines will continue for the foreseeable future. Yield pressures, along with the recent rise in fuel prices, will reveal weaknesses within Asian aviation business models. Responding to continued competitive threats while delivering sustainable returns on capital will require near-term responses and long-term structural change.

In the near term, the continued re-optimization of networks and revenue management practices will be essential for major airlines seeking to improve profitability. Additionally, a focus on transforming cost structures to achieve parity or better, as compared to other leading international competitors, many of which have spent the last decade lowering their cost structures in the face of competition. Leading competitors are focused on these activities, indicating that more work is required.

To achieve long-term and sustained financial performance, Asian carriers will need to seek a more rational competitive structure and balance capacity growth decisions against market demand. Asian aviation significantly lags North American and European rivals in its degree of consolidation. Consolidation in the other major aviation markets has proven beneficial to both balancing supply and demand, as well as unlocking great cost-efficiency opportunities.

Progress will require proactive management of pan-Asian government affairs, regulatory and anti-trust frameworks. Successful solutions will involve consolidation through M&A activity and/or liquidations of competitors as well as deepening international partnerships through increasingly sophisticated joint venture frameworks.

Structural changes will move slowly, yet consumer expectations will evolve at speed and continue to increase in scope. At the same time, the market presents an unparalleled opportunity to invest in and leverage technology to transform customer experiences and business performance. Dynamic airlines are already making great strides:

1. Creating frictionless and personalized travel experiences that leverage technologies such as artificial intelligence, deep customer analytics and internet of things.

2. Investing in digitalizing operations to create step changes in operational efficiencies including in support functions such as finance, human resources and information technology.

3. Collaborating with partners across the travel ecosystem to own the end-to-end travel experience and create / capture new value from the customer.
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