International Business Strategy
RYANAIR

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RYANAIR STRATEGY

Ryanair strategy is close to the "virtual airline" business model (see Figure 1). This strategy appears much more effective for either new start-up airlines or existing growing airlines that are not encumbered with facilities and staff issues. By outsourcing most functions they can get the best and lowest cost deals.

Nevertheless, the cost leadership strategy is not the only distinctive characteristic of the Ryanair strategy. The company also applies a singular revenue model. In addition to flight/scheduled revenues, Ryanair uses an "add-ons" revenue strategy. These add-ons are becoming increasingly important to the company and, for example, what Ryanair describes as ancillary revenues grew faster than scheduled revenues in the year to March 2006. The airline increased ancillary revenues by 36% to €259m for a business that made total after-tax profits of €306m. When passengers get on the plane, further revenue is generated from food and duty frees. The latest product offering is an in-flight mobile phone service, charged at international roaming rates. The airline also makes money from selling hotel and car hire deals to ticket buyers.

Ancillary revenues are regarded as a lucrative source of revenue growth for Ryanair at high margins. In particular, great potential is invested in Ryanair.com, the company's website which has 15 million unique visitors a month. The relentless drive on costs has attracted the most controversy. The airline's pilots and cabin crew pay for their training and uniforms, staff are banned from charging their mobile phones at work and trade unions are not recognised.

Ryanair's often obscure destinations are underpinned by a solid, frugal logic. It seeks out airports that have lower landing charges than the major flight hubs. This boosts the margins from every journey and local authorities often offer attractive rates.

FUTURE EVOLUTION of the AIRLINE INDUSTRY

In the coming years, two different types of carriers should emerge: global network carriers and niche players. A global carrier would aim to provide a world-wide network of routes and destinations. The niche to focus on may be either geographical or a particular type of service (e.g.: focus on domestic services within a particular country, route-specific alliances, low-cost carrier, etc).

Nowadays and certainly in the future, cost monitoring has to be included in the airlines' corporate strategy. Cost reduction is a continuous and permanent requirement if airlines are to be profitable: labour being the largest single cost item will inevitably be the first key area for cost containment; introduction of e-commerce, online sales and automation for ticketing/checking should significantly reduce costs.

In parallel with this new cost policy, airline marketing should be refocused to give priority to increasing yield. This can only be done through a better understanding of the requirements of different market segments, through constantly improved and innovative products and services to reflect those requirements, and through the more effective use of customer relations management.

Airline service has become a commodity-like good, meaning that the price variable is a primary source of competition among participants. Nevertheless, pricing decisions are tactical rather than strategic. In essence, this means that although pricing decisions are easy to implement and reverse, competitors can easily imitate them, allowing the possibility of only a temporary competitive advantage at best. Competing principally on the basis of price has the potential to substantially reduce the firms' ability to operate profitably within an industry and to virtually preclude the possibility of generating customer loyalty.

RYANAIR GROWTH STRATEGY

Over the past five years, the average sustainable growth rate of Ryanair was about 20%. In other words, the growth that Ryanair can sustain without increasing its financial leverage is about 20%. Therefore, in my opinion, 20% should be the Ryanair target growth rate for the next five years.

<u>SCENARIO 1: Faster growth rate</u>

Advantages

- The evolution of the airline industry suggests that, in the following decade, Ryanair should face the risk of new entrants. This is explained by the fact that it is easy, in theory, to imitate the "virtual airline" business model. With a growth rate higher than 20%, Ryanair could invade new routes more quickly and therefore reinforce the company global position in the airline market. With a strong market position it will be more difficult and costly for other airlines or new entrants to challenge Ryanair effectively.
- As ancillary revenues increase more quickly than scheduled revenues, a quicker development of new routes could have a significant impact on future net incomes.

Disadvantages

If Ryanair grows at a rate of over 20%, the company will need to raise money from the market either via capital or debt increases.

- A capital increase could change the composition of Ryanair Board of Directors and therefore impact the current Ryanair strategy and management.
- If the company increases its debt, its fixed costs will increase affecting the cost leadership strategy of the company and therefore its profitability.

<u>SCENARIO 2: Slower growth rate</u>

Advantages

- The airline industry is a cyclical industry. During cyclical downturns, passenger growth falls and revenue decrease. Such market conditions do not encourage growth. Therefore to protect the company from these cyclical downturns, the company could adopt a growth rate lower than 20%.
- If the growth rate is smaller than 20%, Ryanair could focus more on the development of its ancillary source of revenues and less on the development of new routes. Even a small growth of ancillary revenues can have an high positive impact on Ryanair profits.

Disadvantages

- If Ryanair do not reach the 20% growth rate, this means that some assets are not used optimally in the development of the activity. In this case, these assets could produce returns below those generated by Ryanair having a negative impact on Ryanair ROEs.
- A slower growth rate could also be synonymous with slower growth of ancillary revenues as Ryanair will be present on less routes. Obviously this could significantly affect Ryanair net incomes as ancillary revenues represent 85% of net income.

FIGURES

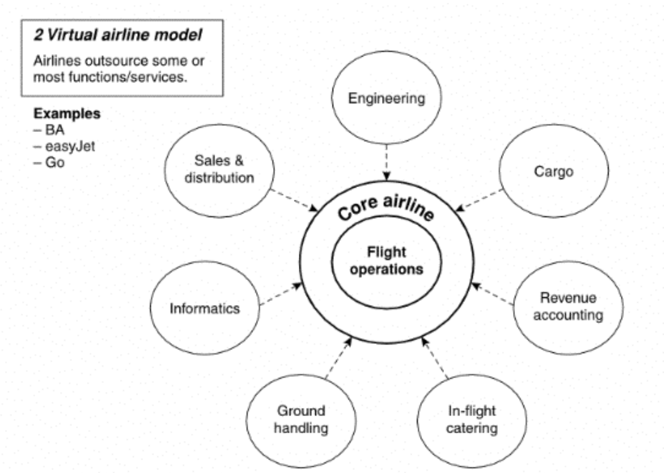

Figure 1: Overview of the virtual airline business models used within the airline industry.