

# A CONCEPTUAL FRAMEWORK OF THE LOW COST CARRIER - AIRPORT RELATIONSHIP DEVELOPMENT IN SOUTHEAST ASIA

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## ABSTRACT

The purpose of this study is to explore the relationship development between Low Cost Carriers (LCCs) and airports in Southeast Asia. LCCs are growing rapidly in Southeast Asia and their development inevitably involves establishing relationships with airports. As LCCs continue this impressive growth rate in the future, it is not difficult to foresee that there will be more and more relationships establish between LCCs and airports which make it a valuable topic to be studied. International air service is one of the major characteristics of LCCs in Southeast Asia. Traditionally, international airlines and airport relationships have been confined to bilateral air service agreement (BASA). Besides, that most of the airlines are national carriers while most of the airports are government owned and controlled in Southeast Asia. Therefore the traditional airlines-airport relationship in Southeast Asia is between two governments' organizations and confined to BASA. However, most of the the LCCs in Southeast Asia are privately owned commercial organization. Therefore the LCC-airport relationship is between a commercial and a government organization. As a result, the knowledge of the traditional airlines-airport relationship cannot be applied to the LCC-airport relationship. However, the issue of the LCC-airport relationship development has seldom been addressed by previous researchers. This study aims at filling this research gap. This study will borrow the idea of the Interaction Model (IMP Group, 1982), power imbalance, mutual dependence (Pfeffer and Salancik, 2003) and mutuality (Ford, Hakansson & Johanson, 1986) to explore and explain the LCC-airport relationship in Southeast Asia. This research will first study what factors lead a LCC and an airport to start up a relationship, and how these factors affect their relationship development. Whether and how power, dependence and mutuality will affect their relationship will also be studied.

**Keywords:** Low cost carrier (LCC), airport, relationship

## INTRODUCTION

Low cost carriers are growing rapidly with an approximately 27% global increase in seat capacity in the year of 2005/2006 (OAG, 2006). In Southeast Asia, the seat

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\* Any remaining errors or omissions rest solely with the author(s) of this paper.

capacity increased by 57.6% (OAG, 2006) in the same period. The development of LCC inevitably involves establishing relationships with airports. As LCC continue this impressive growth rate in the future, it is not difficult to foresee that there will be more and more relationships establish between LCCs and airports which make it a valuable topic to be studied.

As LCCs have developed rapidly, many researchers have paid increasing attentions to them such as analysing their geographical network (Dobruszkes, 2006), their development and life cycle (Francis, Humphreys, Ison & Aicken, 2006), and competitive advantage (Gillen & Lall, 2004). The relationship between LCCs and airports has captured the attention of several scholars, such as Barbot (2006), Francis, Humphreys and Ison (2004), Francis, Fidato and Humphreys, (2003). Their studies were mainly about discount on airport charges and the importance of non-aeronautical revenue. However, the issue of LCC-airport relationship development has seldom been addressed by previous researchers. This study aims at filling this research gap.

The study make reference to the idea of the Interaction Model (IMP Group, 1982), power imbalance, mutual dependence (Pfeffer and Salancik, 2003) and mutuality (Ford, Hakansson & Johanson, 1986) to explore and explain the LCC-airport relationship in Southeast Asia. It will first research the factors which lead a LCC and an airport to start up a relationship, what factors and how these factors affect their relationship development. Besides this, whether and how power, dependence and mutuality will affect their relationship will also be examinde.

## **PROBLEM STATEMENT**

LCCs in the USA mainly provide domestic services. The 3<sup>rd</sup> package of liberalization created a single market in Europe, therefore air services within the Single Sky become domestic routes. However, there is no single market agreement in Southeast Asia, and almost all the air services between countries in Southeast Asia are regulated by bilateral air service agreements (BASAs). As a result, international air service becomes one of the major characteristics of LCCs in Southeast Asia. Altogether they fly to approximately 100 foreign destinations from their origins.

Most of the international air services in Southeast Asia are regulated by BASAs. These give airlines rights and responsibilities to fly to airports agreed to by the two involved governments. Airports also have rights and responsibilities to accommodate airlines appointed under BASAs. Airlines and airports only exercise the BASAs which are negotiated and agreed by the 2 involved governments. Besides, airlines are mainly national carriers while airports are mainly government owned and controlled in Southeast Asia. Therefore, the traditional relationship between international airlines and airport in Southeast Asia is between two government organizations and confined to BASA.

However, the relationship between LCCs and airport is totally different. In Southeast Asia, most of the LCCs are privately owned commercial organizations and need to make every effort to ensure a return for their stakeholders. Although LCCs in Southeast Asia are also regulated by BASAs as the national airlines, LCCs do not have the responsibility to fly to all the foreign destination airports agreed to in BASAs. Instead, LCCs have the flexibility to make commercial decision on which airports to fly to, provided that the airports are agreed in BASAs. On the other hand, most of the airports in Southeast Asia are still government owned and controlled which may not aim at commercial benefit only. As a result, the LCC-airport relationship is between a commercial and a government organization. LCCs and airports will strive for their own interests which may create barriers in their relationship. Arguments between LCCs and airports are not unusual nowadays, such over as discounts on airport charges and LCCs threatening to fly to another airport. However, these are new experiences for airports in Southeast Asia because these are not happening in the traditional airlines-airport relationship. The knowledge of the traditional airlines-airport relationship can no longer be applied to the LCC-airport relationship.

Building up a relationship with one airport means developing an additional route to a LCC while building up a relationship with one LCC means tapping a source of income to airports. Obviously, their relationship has significant implications for future development of both parties. Since the knowledge of the traditional airlines-airport relationship cannot be applied to the LCC-airport relationship, this research attempts to construct a conceptual framework for exploring the development of the relationship between LCC and airport.

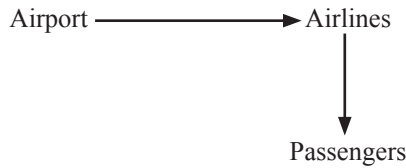
## **OBJECTIVES**

- To identify the prerequisite conditions that allow LCCs and airport to start up a relationship;
- To identify the factors that lead the LCCs and airports to start up a relationship;
- To identify the factors that influence the development of an LCC-airport relationship;
- To examine how these factors influence the development of an LCC-airport relationship;
- To identify the role of government in the LCC-airport relationship;
- To examine how the LCC-airport relationship in turn affects their business development; and
- To construct a conceptual framework for understanding the LCC-airport relationship development in Southeast Asia.

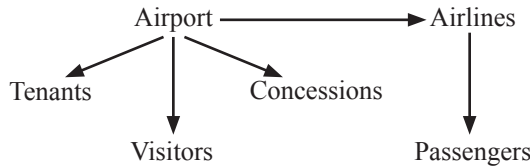
## LITERATURE REVIEW

### Relationship between LCCs and airports

Traditionally, the contract between airlines and airport stated the conditions of use of airport facilities and services in exchange for the aeronautical fees paid by the airlines (Graham, 2003). This was a simple dyadic buyer-seller relationship (Albers, Koch & Ruff, 2005). As shown in Figure 1, airports viewed airlines as their primary customers (Francis et al., 2004; Graham, 2003). Passengers were viewed as part of airlines business and airports had very little intention to obtain revenue from passengers (Francis et al., 2004). As a result, airports relied heavily on aeronautical revenues.



**Figure 1** Airline-airport relationship: traditional model (Francis et al., 2004)



**Figure 2** Airline-airport relationship: new commercial model (Francis et al., 2004)

Francis et al. (2004) argued that the airline-airport relationship was gradually becoming more complex as airlines are increasingly cost minded for the sake of their own financial performance, as a result, aeronautical charges are under increasing scrutiny from airlines (Graham, 2003). This situation is more apparent in the case of LCC.

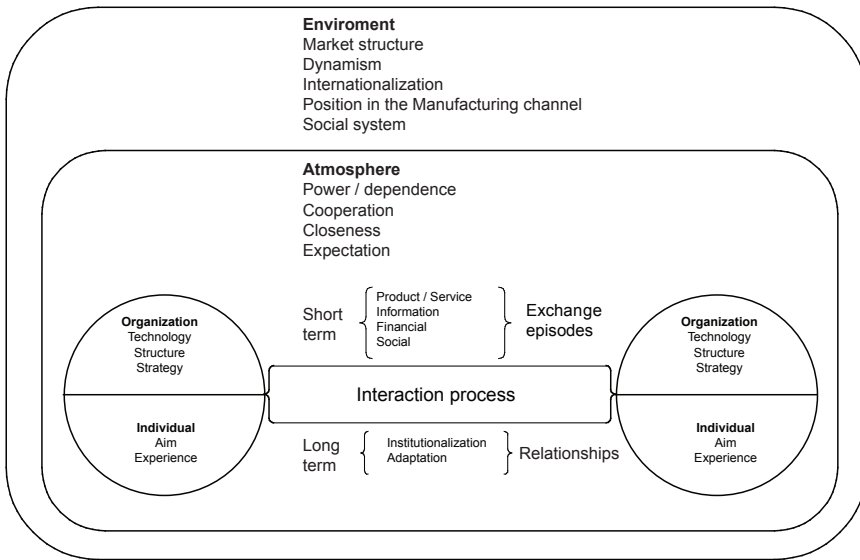
Many LCCs are attempting to negotiate a better deal in aeronautical charges from airports. Some airports, particularly those under-utilized airports, are willing to offer discounts to LCCs (Barett, 2004) or even waive their landing fee for the first few years (Graham, 2003). In order to compensate the loss of aeronautical charges, airports must tap new source of income, while non-aeronautical incomes from concessions, tenants and visitors are the most readily available source of revenues to airports (Francis et al., 2004). However, all of the non-aeronautical incomes depend heavily on passenger throughput. As a result, the airport management is linking up their operating revenues to LCCs' ability to increase traffic flow. A concept of risk sharing is emerging into LCC-airport relationship

which is rather new in aviation management. Since most of the airports in Southeast Asia are still government owned, controlled or subsidized, it is questionable if these airports are willing or allowed to share business risks with LCC, even if they are under-utilized. Government influences should not be overlook in Southeast Asia. It seems that the LCC-airport relationship in Southeast Asia can be described as a buyer-seller relationship with strong government influence.

**Buyer – seller relationship**

The interaction Model (IMP Group, 1982) depicted a comprehensive picture of buyer-seller relationships as shown in Figure 3.

The Interaction Model



**Figure 3** The Interaction Model (IMP Group, 1982)

The Industrial Marketing and Purchasing (IMP) Group (1982) as well as some other researchers, such as Dwyer, Schurr & Oh (1987), Ford, Hakansson & Johanson (1986), Brennan, Turnbull & Wilson (2003), viewed the exchange between industrial buyers and sellers as an ongoing process with many individual exchange episodes. IMP Group (1982) also argued that industrial buyers are not generally responding to marketing mix variables manipulated by the sellers. Instead, the interactions between individual buyers and sellers are important to their relationship because both the buyer and seller are active in the relationship. The interaction model emphasized that there are not many buyers and sellers in the industrial market and they know each other very well and realize the movement of each other. Moreover, both the buyer and seller have the same task to search a

suitable counterpart, to make a request or offer and to try to control the transaction process. In this sense, the Group (1982) claimed that the characteristics, actions and reactions of both the buyer and seller have to be analyzed simultaneously in order to understand their relationship.

These arguments may also apply to the LCC-airport relationship. Firstly, the transaction between LCC and airport is rather long term which involves interaction and negotiation for a period of time. The purchase of airport services by LCC is not in the form of single discrete transaction, instead, a contract between LCC and airport normally last for a few years. Secondly, similar to the industrial market, there are not many LCCs and airports in the aviation market. They also know each other very well and are aware of the others movement in the market. Thirdly, both the LCCs and airports will also take the initiative to search for a suitable counterpart and attempt to control the transaction. It seems that the Interaction Model (IMP Group, 1982) can well suit the LCC-airport relationship. However, the Interaction Model (IMP Group, 1982) purely studied the relationship between commercial organizations in the industrial market. The LCC-airport relationship in Southeast Asia is probably between a commercial and government organization. Therefore, this study will only use the Interaction Model (IMP Group, 1982) as the starting point to construct the conceptual framework of the LCC-airport relationship in Southeast Asia.

There are four groups of variables in the IMP model, which are the organizations involved, elements and process as of interaction, environment where the interaction takes place and atmosphere affecting and affected by the interaction. The model attempts to explain the buyer-seller relationship in industrial market with these 4 groups of variables (IMP Group, 1982). However, this model cannot explain what factors lead the two parties to build up a relationship with each other. This paper suggests incorporating the concept of resources and capabilities in order to explain why a LCC and an airport wish to develop a relationship with each other.

## **Resources and Capabilities**

Organizations interact with each other because they seek to gain from each other, have a function for each other (Ford, Hakansson & Johanson, 1986) or need each other the resources. (Pfeffer and Salancik, 2003). Capability refers to what an organization can do for its counterpart or what function the organization can carry out for its counterpart (Ford, Hakansson & Johanson, 1986).

Probably, organizations will evaluate their counterparts' resources and capabilities in the pre-relationship stage. If an LCC or an airport finds that the resources and capabilities possessed by their counterpart are valuable, they may want to develop a relationship with this counterpart. It seems that resources and capabilities are the fundamental reasons why organizations want to establish a relationship with each other. Therefore, this research is going to incorporate the concept of resources (Pfeffer and Salancik, 2003) and capabilities (Ford, Hakansson and Johanson, 1986) into the conceptual framework.

## **LCC's requirements of Airports**

LCC is willing to start up a business relationship with an airport only if the airport can provides what it needs. Previous researches suggested some requirements such as low airport charges (Barbot, 2006; Barrett, 2000; Graham, 2003; Francis, Humphreys & Ison, 2004; Warnock-Smith & Potter, 2005), quick turnaround time (Barrett, 2004; Gillen & Lall, 2004; Warnock-Smith & Potter, 2005), spare airport capacity, convenient slot times (Warnock-Smith & Potter, 2005), single-storey airport terminals (Barrett, 2004; Francis et al., 2004), quick check-in, good catering and shopping at airport, good facilities for ground transport, high potential demand for LCC services and no gold-plating facility (Barrett, 2004).

Interaction only makes sense if the organizations can gain from their counterpart (Ford, Hakansson & Johanson, 1986) and they can provide what their counterpart needs (Pfeffer and Salancik, 2003). Therefore what the airports need from LCCs should be considered simultaneously.

## **Airports' requirements of LCCs**

Previous researches, such as Barrett (2004) and Warnock-Smith & Potter (2005), only studied what LCCs required from airports. The airports' requirements on LCCs are rarely studied. From Francis et al.'s studies (2003 & 2004), two factors may be taken into account, which are sustainability of the LCCs in the airports (Francis et al., 2003) and LCCs' ability to increase passenger throughput, hence the non-aeronautical revenue can be increased (Francis et al., 2003; Francis et al., 2004).

However, most of the airports in Southeast Asia are government owned and controlled. When governments decide policies for their airports, they may not solely consider the benefit of the airport. Instead, the government may take the benefit of the whole society into account including the benefit of their own flag carrier, tourism development of their country, and economics development. For the sake of the whole society, the government may scarifies the benefit of the airport. The Singapore government stated clearly that 'unused traffic rights will be allocated among competing users in a manner that optimizes national interests' (Straits Times, 2003). Obviously, airports and LCCs cannot develop relationships with their own desires, but they are very much affected by government's views on national interest and airport benefit. Therefore, government influences on airport should be taken into account in LCC-airport relationship development in Southeast Asia.

The above sections briefly reviewed what resources and capabilities LCCs and airports need from and provide to each other as well as government influences. This implies that LCCs and airports are interdependent. However, the influences of government becomes variables in their relationship.

## **Power Imbalance & Mutual Dependence**

Organizations are not self-contained (Buchanan, 1992; Pfeffer & Salancik, 2003). All organizations coexist in an environment and depend on the external sources for necessary resources. It is always true that while airlines need airport facilities for operating flight services, airports need airlines to buy their services at the same time.

However, the question is if the LCC and airport depend on each other at the same level. If not, then one party will have power over the others because power resides implicitly in the other's dependency (Emerson, 1962). The difference in power between the LCC and the airport will form a power imbalance (Casciaro & Piskorski, 2005; Emerson, 1962) between them. The power advantage party may exert influences on the interaction process in order to gain benefit from the power disadvantaged side.

Mutual dependence is the sum of dependence (Casciaro & Piskorski, 2005; Emerson, 1962) of the two organizations. When the dependence of the LCC and the airport on each other is high, their mutual dependence is high, and vice versa. Lawler and Yoon (1996) suggested that a more balanced power relation together with greater mutual dependence will promote relational cohesion.

In the Interaction Model (IMP Group, 1982), power-dependence was viewed as the outcome of the relationship. However, assuming that every organization possesses its own resources and capabilities before developing any relationship with any organization, their inherent resources and capabilities as well as what resources it needs from its counterpart determine the power and dependence between them. IMP Group (1982) also suggested that the inherent resources of an organization and its power determine its basic position in the interaction process. Therefore, it comes to a logical inference that power and dependence are the factors affecting the interaction process, rather than the product of a relationship.

## **Mutuality**

Mutuality rests on whether the two organizations share common goals or interests and the way they handle their divergent goals (Ford, Hakansson & Johanson, 1986). Mutuality means how much a company is willing to give up its own goals in order to increase the positive outcome of others, hence its own ultimate benefit can be enhanced (Ford, Hakansson & Johanson, 1986) or how much either party is prepared to sacrifice for the sake of the relationship (Johnsen & Ford, 2001). For instance, if the organizations emphasize on mutual goals and interests, such as simplifying the production process, then the organizations will show an interest in each others' well-being and look for a longer term gain (Ford, Hakansson & Johanson, 1986). However, if an organization has a very limited extent of mutuality with its counterpart, this organization will focus on its self-interest and short term opportunism, such as discount negotiation (Ford, Hakansson & Johanson, 1986).

Ford, Hakansson & Johanson (1986) stated that 'mutuality can only be demonstrated over time'. However, this study is going to argue that LCCs and



airports will consider mutuality from the pre-relationship stage because this study believed that the potential of mutuality will affect the LCC's and the airport's intention to develop a relationship with each other. Besides, this study also believed that mutuality will affect the way that the LCC and the airport interact with each other.

### 1 The Conceptual Framework

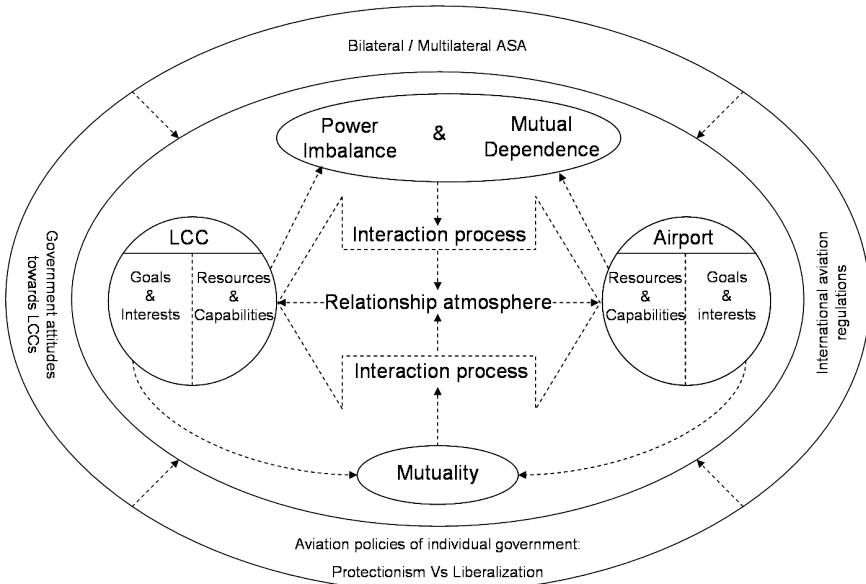


Figure 4 The Conceptual Framework

The whole aviation industry, as well as LCCs and airports, are framed by three levels of control, which are international aviation regulations, BASA / Multilateral Air Service Agreement (MASA) and national government aviation policies. LCCs cannot fly to any foreign destination airport according to their own desire. This research suggests that the three levels of control together with local governments' attitudes towards the development of LCC formed the prerequisite conditions for starting up a relationship between a LCC and an airport as shown in Figure 4.

After examining the prerequisites, the conceptual framework will study why the LCC and the airport start up a relationship with each other and how their relationship is developed. For a relationship to be worthwhile both the interacting parties must be able to gain from each other and be able to form something meaningful together (Ford, Hakansson & Johanson, 1986) which cannot be formed by either party individually (Hakansson & Snehota, 1995). This point of view inevitably leads to two fundamental questions. Firstly, what resources and capabilities that a LCC and an airport can offer each other? Secondly, what goals

and interests do they want to achieve from the relationship? Therefore, the concept of resources, capability, goals and interest are incorporated into the conceptual framework.

With the consideration of their resources and capabilities as well as their goals and interests, this study is going to incorporate the concept of power imbalance, mutual dependence and mutuality into the conceptual framework to examine whether and how these three factors affect the development of LCC-airport relationship. Besides, this research will explore whether there are other factors that will affect the relationship development between LCCs and airports.

The IMP Group (1982) suggested that the relationship atmosphere is the product of the interaction process and also the starting points for future interaction. However, how the future interaction would be affected was not specified. This research will study how the relationship atmosphere affects LCCs and airport's future interaction and business development with each other.

## **METHODOLOGY**

This research is an exploratory study which aims at constructing a conceptual framework of the relationship between LCC and airport. As an exploratory study, an inductive research model will be adopted. A multiple case study approach will be used in this research.

The unit of analysis is defined as the development of a dyadic relationship between LCC and airport. The process of developing a relationship between one LCC and one airport represents one case. Since the development of a relationship is a temporal issue, a timeframe is needed to define the beginning and the end of the case. The beginning of the case will be the time when a LCC or an airport start to evaluate each other as a potential counterpart. The end of the case will be at the time when the LCC and airport are being interviewed because the interviewees can trace back their actions and reactions taken overtime, they cannot predict precisely what they and their counterparts are going to do in the future. Therefore the information on the cases is only available up to the time that they are being interviewed.

Data will be collected from primary and secondary sources. A set of semi-structural questions will be designed for conducting personal interviews with executives from LCCs and airports. Secondary data will be a cross-referenced to primary data in order to process triangulation. After data collection, within-case analysis will first be carried out to gain an in-depth understanding on each case before cross-case comparison can be processed. Besides, a pilot interview will be conducted in order to refine the research design.

## CONTRIBUTION

This study attempts to make academic and industry contributions.

Academic:

- This research attempts to fill the research gap in the LCC-airport relationship development issue.
- Airlines in Southeast Asia are gradually undergoing privatization which will be more cost sensitive (Graham, 2003), the airline-airport relationship will then tend to be similar to the LCC-airport relationship. The understanding of LCC-airport relationship development can be a starting point to further study the privatized airlines-airport relationship in future.

Industry:

- The knowledge about the way the LCC-airport relationship is developed and what factors affect them is particular useful to route development of LCCs and airports which need to develop business with LCCs.

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