

## **RYANAIR (2005): SUCCESSFUL LOW COST LEADERSHIP**

**Thomas M. Box, Pittsburg State University**

tbox@pittstate.edu

**Kent Byus, Texas A&M University – Corpus Christi**

kbyus@cob.tamucc.edu

### **CASE DESCRIPTION**

*The primary subject matter of this case concerns strategic management in the airline industry in Europe. Secondary issues examined include international marketing, operations management and business ethics. The case has a difficulty level of four or five and the case is designed to be taught in one ninety minute class session. It is expected that students will need to devote three to four hours of outside preparation for the class discussion.*

### **CASE SYNOPSIS**

*Ryanair is a twenty-year old international air carrier based in Dublin, Ireland. It is now the largest low cost airline in Great Britain and Europe and has modeled its operations (since 1991) on the very successful Southwest Airlines Low Cost Leadership model. Ryanair's CEO – Michael O'Leary – is an accountant by training, but a combative entrepreneur by inclination. He has angered trade unions, government officials and competitors with his "bare knuckle" tactics but has achieved dramatic growth and profitability in the very competitive airline industry.*

*As of the end of the year 2004, Ryanair was flying 25 million passengers annually with a staff of less than 2500 personnel. Ryanair flies only Boeing 737s and is rapidly transitioning to the newest 737 models – the 737-800. Challenges to the airline at the end of 2004 included escalating fuel costs, intensity of competition and the sometimes less than favorable attitude of the regulatory bodies in Great Britain, Ireland and the EU.*

### **INTRODUCTION**

On Thursday, May 26, 2005 Ryanair Holdings, PLC (Ryanair) celebrated its 20<sup>th</sup> birthday in a central Dublin hotel with a birthday cake and a party. At the celebration, Ryanair's CEO – Michael O'Leary – confidently predicted that Ryanair would overtake British Airways by carrying 3.5 million passengers a month in 2005. He went on to say, "The very fact that a Mickey Mouse Irish airline can start in a field in Waterford 20 years ago, and in 20 years, overtake the world's self-styled, self-proclaimed favourite airline is testament to the demand for low-airfare travel around Europe." (Business Ticker, 2005)

### **EARLY HISTORY OF RYANAIR**

Ryanair was founded in July, 1985 by Cathal and Declan Ryan with the financial backing of their father, Tony Ryan. The elder Ryan had, for many years, been Aer Lingus' leasing manager and had gone on to found Guinness Peat Aviation which eventually became the largest aircraft leasing company in the world. Ryanair began operations with a staff of 25 and a single 15-seat Bandeirante turbo-prop flying between Waterford and London. In 1986 Ryanair received permission from the regulatory authorities to begin flying four flights a day on the Dublin-London route with two 46-seat

BAE748 turbo-props. In doing so, they challenged the high cost monopoly of British Airways and Aer Lingus with fares that were set at half the prevailing fare of £209. Ryanair's strategy (initially) was to offer simple, low-cost fares and exemplary customer service. In 1986 (the first full year of operations) they flew 82,000 passengers and began negotiations to acquire their first jet aircraft and additional routes.

During the later part of the 80s Ryanair continued to compete vigorously with British Airways and Aer Lingus while adding additional routes and jet aircraft. By the end of 1989 Ryanair had 6 BAC-111 jets and 3 ATR 42 turbos. In 1990 Ryanair suffered a £20 million loss and was forced to completely restructure. A new, brash CEO – Michael O'Leary – was brought in to manage the turnaround and the Ryan family invested an additional £10 million. O'Leary, at the suggestion of Tony Ryan, visited Southwest Airlines in Dallas, TX to learn the fundamentals of Low Cost Leadership in the airline industry. Southwest, of course, was by far the most profitable of the American carriers and their business model was quite different than the traditional flagship carriers.

Gulf War I (Desert Storm) broke out in January of 1991 and airline traffic around the world collapsed. Despite the decline in overall airline traffic, Ryanair made a profit of £293,000 for the year and carried 651,000 passengers with a total workforce of 477 people. In May 1991, Ryanair switched its London base from Luton Airport to Stansted Airport in Essex. By 1999, Ryanair had added a number of European destinations, had switched the aircraft fleet to Boeing 737s and carried over 5 million passengers – profitably.

## INTO THE 21<sup>ST</sup> CENTURY

In January 2000, Ryanair introduced Europe's largest travel website – [www.ryanair.com](http://www.ryanair.com). Within three months the site was recording 50,000 bookings per week. The web site also facilitated car and hotel rentals, rail services and travel insurance at low prices. In September, the first new base since 1991 was established at Glasgow Prestwick (Scotland) and three new Boeing 737-800s were stationed there. The base provided Scots customers direct flights to Paris, Frankfurt, Dublin and London. In 2000, Ryanair carried over 7 million passengers with a workforce at year end of 1,262 people. Ryanair had, by the end of 2000, formalized its business model to include:

- All Boeing aircraft (primarily 737-800s)
- No "free" amenities such as snacks and drinks.
- Non reclining seatbacks.
- Quick flight turnarounds – averaging 45 minutes.
- An in-flight magazine that was really a catalog for food, beverage and a multitude of duty free products – sold at a considerable profit by the cabin attendants.
- Minimum baggage allowances.

In 2001, Ryanair opened its first European base at Brussels' Charleroi Airport with five more new Boeing 737-800s. Service was provided from Charleroi to Dublin, London, Glasgow, Shannon, Venice, Paris and Carcassonne (France). The agreement at Charleroi was negotiated with airport authorities at a considerable savings in landing fees and gate charges in addition to subsidies for Ryanair. Despite the cost advantages, many predicted failure for Ryanair because the airport is located about 65 km from the capital (Brussels). This, however, was not the case. In August, the airline carried more than 1 million passengers – more than the total passengers carried in the year 1993. The terrorist attack of September 11<sup>th</sup> marked a downturn in airline traffic around the world and an enormous upward spike in the cost of oil – leading to substantial increases in operating cost for all airlines. Ryanair carried over 9 Million passengers in 2001 with a staff of 1,477 at year end.

Frankfurt (Hahn) was selected as the second European base in 2002. It was necessary to prevail in the German courts to overturn Lufthansa's high price monopoly of German aviation and customers responded enthusiastically. During this year, Ryanair increased an order at Boeing from

45 to 125 737-800s with an option for an additional 125 aircraft. In 2003, Ryanair acquired Stansted-based Buzz Airlines from KLM and as a result of the acquisition, got access to an additional 11 French regional airports. By 2004, Ryanair was the largest low cost airline in Europe flying almost 25 Million passengers with a staff (at year end) of only 2,288.

### **RYANAIR'S VISION AND MISSION**

Ryanair does not publish a formal vision or mission statement, but in accordance with Jack Welch's advice, "Strategy is simply finding the big aha and setting a broad direction..." Michael O'Leary's broad direction – communicated in public statements -- is to simply continue to be the largest Low Cost Leader in the European airline industry and to carry 50 million passengers by 2009. Implementing this vision is a function of many individual tactics including an absolute dedication to low cost performance in every element of the value chain, quick gate turnarounds, non-union operations, performance-based incentive compensation plans, standardization on one type of aircraft and flying (in most cases) to secondary airports which provides significant savings for Ryanair.

### **BUSINESS ETHICS**

Despite its remarkable success, Ryanair and particularly Michael O'Leary have been criticized on a number of issues. One of the areas of concern is human resource management. Ryanair is a non-union operation based in Dublin, Ireland. Ireland, of course, is a strongly pro-union environment. Taoiseach (head of the Irish government) Bertie Ahern described O'Leary's orientation toward labor as "tooth and claw capitalism" during the baggage handler's strike at Dublin Airport in 1999. In addition, compensation for pilots and flight attendants is comprised partly of salary and partly based on efficiency issues such as number of flight segments flown and, for flight attendants, amount of revenue generated from sales of items in the in flight magazine.

O'Leary has been a harsh critic of government officials in Ireland and Europe. He is particularly disdainful of officials at Aer Lingus ([www.aerlingus.com](http://www.aerlingus.com)) – Ireland's publicly owned airline and officials at the airline authority (Aer Rianta). As a result of the fees imposed by the Irish government, Ryanair has actually reduced the number of flights in its home country over the last four years.

A recent criticism of Ryanair was its refusal to supply wheel chairs for disabled passengers at Stansted airport. The airline argued that this provision was the responsibility of the airport authority and that 87 of the 93 airports that they fly to provide wheelchairs for those requiring them. In 2004, a judge ruled that the responsibility should be shared by the airline and the airport owners.

Perhaps the most significant (potentially costly) criticism of Ryanair was the deal they negotiated for landing rights at Charleroi. In February, 2004, the European Commission ruled that 4 million of the 15 million in incentives paid to Ryanair constituted illegal state aid. In October, Ryanair agreed to put 4 million in an escrow account pending its appeal of the ruling.

### **OPERATIONS**

In 2004, Ryanair achieved a number of important milestones. They launched two new European bases (Rome and Barcelona) and added 73 new routes bringing their total to 150 routes. They took delivery of 18 new Boeing 737-800s and acquired a competitor – Buzz Airlines from KLM. In July 2003, they carried a record number of passengers – 2 million --and for the year out carried British Airways in the UK/European market. At the end of the year they had 2300 employees and an industry leading 10,049 passengers per employee.

## FINANCIAL DATA

<b>Table 1: Income Statement (all amounts 000)</b>		
	Year 2004	Year 2003
Total operating revenues	1,074,224	842,508
Total operating expenses	(803,373)	(579,034)
Operating profit	270,851	263,474
Profit for the year after adjustments	206,611	239,398
Source of data: Ryanair (2004) Annual Report		

<b>Table 2: Balance sheet information (all amounts 000)</b>		
	Year 2004	Year 2003
Fixed assets	71,994	71,994
Current assets	533,859	526,910
Total assets	605,853	598,904
Other liabilities	35,172	35,172
Equity	570,681	563,732
Total liabilities and equity	605,853	598,904
Source of data: Ryanair (2004) Annual Report		

## INDUSTRY COMPETITORS

Aer Lingus Group Plc (AL) is owned (85%) by the Irish government. They fly about 7 million passengers per year to 50 destinations in Ireland, the UK, the US and Europe. In 2004 they generated \$1,236, 900,000 in revenues with 3,906 employees. AL began flight operations in 1936 with De Havilland biplane, flying between Dublin and Bristol, England. In 1958, AL bought Aerlinte Eireann and began Atlantic service to New York City. The airline grew rapidly until 1993 when revenues and profits eroded substantially. A restructuring plan was introduced and the Irish government invested an additional 222.2 million in equity. Following the financial crisis related to the September 11, 2001 terrorist attacks, AL implemented a survival plan which included a staff reduction of over 2,000 employees, a pay freeze and sales of non-essential assets. The airline also adopted a new lower fare strategy which has resulted in significant increases in revenue and profits.

British Airways Plc (BA) is a very large, full service airline based in Hammonds worth, England. It traces its history back to 1919 when its predecessor, Aircraft Transport and Travel, launched air service from London to Paris. Today, BA flies to 154 destinations in 75 countries with a fleet of 300 aircraft. In 1998, BA invested \$25 million in a new, low cost airline subsidiary named Go. Go was headed by an American woman, Barbara Cassinni, and had an eventful five year history till it was sold (in 2003) to Stelios Haji-Ioannou, owner of easyJet, for \$375 million. Interestingly, the market cap of BA is slightly less than the market cap of Ryanair – a much smaller airline.

easyJet Plc (EJ) is primarily owned by Stelios Haji-Ioannou and began operations in 1995 when Stelios – as he likes to be called – was 28 years old. EJ began as a low cost airline, although it does offer some amenities not offered by Ryanair. In 1998, Stelios founded easyGroup to extend the low cost concepts used at easyJet. easyGroup is invested in hotels, car rentals, internet cafes, credit cards and is constantly exploring additional opportunities. EJ flies 100 Airbus aircraft to 70 destinations and expects to fly 30 million passengers in 2005 in Europe and the UK.

Other competitors include Sir Richard Branson’s Virgin Express, Lufthansa (Germany’s flagship airline), Air France and the 60, or so, small airlines in Europe that have been created since the EU deregulated the airline industry in 1998.

### **CONCLUSION**

It was March 17, 2005 – the start of the four day national holiday honoring St. Patrick, Ireland’s patron saint--and Michael O’Leary was stretched out on a couch watching an old rugby match being replayed on the telly. On a yellow legal pad, O’Leary had jotted down issues that needed consideration at Ryanair: fuel prices, expansion to Eastern Europe, his future at Ryanair and the regulatory battles with Irish politicians and the EU.

### **REFERENCES AVAILABLE UPON REQUEST**