The global spend on air transport last year was almost $750 billion.

Even with more than three billion people flying annually, the industry also experienced an overall reduction in airfares of almost 4%. As a result, the pressure for you to realize true revenue growth has never been greater.

The industry is also seeing an increase in available seats to fill. As an example, according to Ascend Online Data, there were approximately 850 additional airplanes in commercial service in August 2014 compared with 2013, resulting in approximately 14 million additional seats for that month. That’s more pressure on you to manage revenue growth.

The airline industry is not for “the faint of heart.” Its volatility is affected by a number of variables, including regional and global economies, government actions/regulations and stability, large and influential labor groups, extensive investment in equipment, and even the weather has a major impact on the industry.
As 2015 comes to a close soon, we thought it was a good time to share with you our observations on the major challenges and opportunities that the airline industry faces.

1 The Economy

IATA recently shared some very interesting information, which I thought provided an excellent overview of where we are as an industry. Global GDP is expected to grow by 3.2% in 2015, up from 2.6% in 2014. This will be the first time that global GDP has broken over 3.0% since 2010 (when global GDP grew by 4.1% in a post-recession bounce back). Because many carriers are flying to/from different regions of the world, the industry needs to keep an eye on economic strengths and weaknesses across many of these regions. Here’s a quick regional glance of information provided by IATA:

North America: The strongest financial performance by far is being delivered by airlines in North America. Net post-tax profits are the highest at $13.2 billion (up from $11.9 billion in 2014). This improvement has been driven by consolidation, helping to raise load factors (passenger + cargo) to 65% this year, lower fuel prices and ancillaries, which together push breakeven load factors down below 60% next year.

Europe: European airlines continue to struggle as evidenced by the highest breakeven load factors among all regions (64.7%). European airlines compete vigorously in the continent’s open aviation area. But they are hampered by high regulatory costs, infrastructure inefficiency, and onerous taxation. As a result, and despite the industry in the region achieving the second highest load factor, financial performance has been poor. Net profits of $4 billion for 2015 (up from $2.7 billion in 2014) represent only $4.27 per passenger and a net profit margin of 1.8%.

Asia-Pacific: Airlines in the Asia-Pacific region are expected to achieve a net profit of $5.0 billion in 2015 (up from $3.5 billion in 2014) for a 2.2% net profit margin. Some strengthening of cargo markets, particularly important in this manufacturing region, plus lower fuel costs, are expected to drive the moderate improvement in 2014.

Middle East: Middle East airlines have one of the lowest breakeven load factors (58.6%). Average yields are low but unit costs are even lower, partly driven by the strength of capacity growth. Passenger capacity is expected to expand by 15.6% in 2015 (up from 11.4% in 2014). Post-tax net profits are expected to grow to $1.6 billion in 2015 (up from $1.1 billion in 2014). This represents a profit of $7.98 per passenger and a net profit margin of 2.5%.

Latin America: Latin American airlines have faced a mixed environment. Weak home markets have hampered performance, but a degree of consolidation and some long-haul success is expected to boost net profits to $1 billion in 2015 (up from $700 million in 2014). That would be a profit of $3.53 per passenger and a net profit margin of 2.6%.

Africa: Africa is the weakest region, as in the past two years. Profits are barely positive ($200 million in 2015, which is an improvement on the break-even performance in 2014), and represent just $2.51 per passenger. Breakeven load factors are relatively low, as yields are a little higher than average while costs are lower. However, few airlines in the region are able to achieve adequate load factors, which are the lowest among the regions by almost five percentage points. Performance is improving, but slowly.
Air Traffic and Competition
The good news is that more than three billion people are going to fly this year, so hopefully that means more people will fly with you than ever before. The challenge? That’s also a lot of people flying with your competition. Whether you compete against LCCs, ultra-LCCs, legacy network carriers, or even those that might be considered hybrid, you face significant pressure to consistently realize your true revenue growth and profitability potential.

Fuel Prices
The largest impact on airline profitability this year is the significant reduction in fuel prices. According to the U.S. Energy Information Administration, the price per gallon for jet fuel in August of this year is $1.45, less than half of what the cost per gallon was in August 2012. According to a special report by PwC, “Fuel Price Volatility: How Are Airlines Responding to the Challenge?” lower prices mean that globally, airlines will spend $70 billion less on fuel this year than in 2014. However, we might not know what the total impact is of reduced fuel prices until the fuel-hedging contracts that some airlines are still committed to end. The increases in airline profits will allow many carriers to invest in new aircraft, technology, and infrastructure; however, the industry does need to maintain discipline in their expenditures as fuel prices will rise at some point in the future. Exactly when nobody knows, but the rise will come.

Margins and Fares
According to IATA, industry profitability for 2015 should be around $25.0 billion in 2015. After adjusting for inflation, average return airfares (excluding taxes and surcharges) are expected to fall by some 5.1% on 2014 levels. The expected $25 billion net post-tax profit represents a 3.2% margin. On a per passenger basis, airlines will make a net profit of $7.08 in 2015. That is up on the $6.02 earned in 2014 and more than double the $3.38 earnings per passenger achieved in 2013.

Technology
According to the 2014 PwC Global Airline CEO Survey, 60 percent of airline CEOs are developing future strategies or have concrete plans for changes to their technology investment programs and 29 percent already have programs underway or completed. Advances in technology and the seemingly disappearance of borders provides a truly global audience for many businesses, and the airline industry is no exception. Right now, somewhere in the world, someone with a smartphone is shopping and comparing airfares. How do you make sure your fares and offers are the ones they will select? How do you make that experience consistent across all of your distribution channels? The right technology is a big part of the answer.

Customer Expectations
Related to the previous point on technology, your ability to manage your customers’ expectations relative to their shopping experience is more important than ever before. When you consider how your customers’ non-airline retail shopping experiences, especially what and how they purchase online, you realize that customers will expect to have a similar experience with your airline. And if they don’t, you will certainly not be meeting their expectations, which means they might just take their business elsewhere. As an example, how long does it take you to respond to a customer’s request for a
group booking? Hours, days, weeks, or seconds? If you can’t respond to them quickly, you’re leaving money on the table.

Global Conflict

It’s a small world out there. With impressive increases in aircraft range, many airlines are enjoying the flexibility and opportunity to expand their footprint across borders. Whether it is Air New Zealand’s new service from Auckland to Houston, Texas, or non-stop service on Emirates from Dubai to Los Angeles, the industry has done a great job making the world a smaller place. This global presence can also expose carriers to global conflicts that may affect their ability to expand, or even continue the service they may provide today. Carriers need to consider a balance of flying across global regions in order to insulate themselves from conflicts, or major international disasters. Think of the impact the industry saw with the outbreak of SARS in many areas of Asia just a few years ago. Or the impact to the industry based on conflicts in the Middle East, Africa, or other regions of the world.

NDC

The current distribution system is not keeping up with travelers’ shopping expectations. Our industry’s major distribution limitations, sometimes referred to here at PROS as “destructive distribution,” include the inability to differentiate your product and slow time-to-market; a lack of full and rich content for customers to access; and the inability to provide your customers with a transparent shopping experience. Along comes NDC (New Distribution Capability). This is a travel industry-supported program launched by IATA for the development and market adoption of a new, XML-based data transmission standard known as the (NDC Standard). So, what does that really mean? This standard will enhance the capability of communications between airlines and travel agents. The NDC standard will be open to any third party, intermediary, IT provider or non-IATA member to implement and use. The NDC standard will enable the travel industry to transform the way air products are retailed to corporations, leisure, and business travelers by providing benefits to airlines, travel agents, and travelers. While completion of the NDC might be a few years off, are you confident your distribution strategy is meeting your customers’ needs and allowing you to realize your true revenue growth?

Aircraft

According to Boeing, over the next 20 years there will be a need for 38,050 airplanes valued at more than $5.6 trillion. Approximately 40 percent of all new airplanes are being delivered to airlines based in the Asia Pacific region. Twenty percent will be delivered to airlines in Europe and North America, with the remaining 20 percent to be delivered to the Middle East, Latin America, the Commonwealth of Independent States, and Africa. Single-aisle airplanes comprise the largest share of new deliveries, with airlines needing approximately 26,730. These new airplanes will continue to stimulate growth for low-cost carriers and will provide needed replacements for older, less-efficient airplanes. In addition, widebody fleets will need an additional 8,830 new airplanes, which will allow airlines to serve new markets more efficiently than in the past.

Airport Growth

The need for more runways, more gates, and more capacity to handle more passengers are all concerns to airlines. A recent special report, the 2015 Arthur Little World Airport Report, indicates that these days
"it's an even better new normal" because this year there is growth across the board in every region. Global growth in traffic improved to 5.6% from 4.3% last year making this year one of the top performing years on record. We are seeing facilities being modernized from a perspective of passenger amenities in terminal to new international terminals being built, even at Houston’s traditionally “smaller” airport Hobby Airport to support international growth thanks to Southwest Airlines.

It’s an exciting time in the airline industry—and a time to realize your true revenue growth and profit potential. Have you put together your list of challenges and opportunities for the rest of this year and into the future? Do some of the challenges mentioned above resonate? Are there others to add? Focus on what you can control and influence, and keep your eye on the centerline … and it will be clear blue skies ahead.

About PROS

PROS Holdings, Inc. (NYSE: PRO) is a big data software company that helps customers outperform in their markets by using big data to sell more effectively. We apply years of data science experience to unlock buying patterns and preferences within transaction data to reveal which opportunities are most likely to close, which offers are most likely to sell and which prices are most likely to win. PROS offers big data solutions to optimize sales, pricing, quoting, rebates and revenue management across more than 40 industries. PROS has completed over 800 implementations of its solutions in more than 55 countries. The PROS team comprises more than 1,000 professionals around the world. To learn more, visit www.pros.com.