An Examination of Ryanair's Entry into the African Aviation Market

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The African aviation market promises to become one of the more dynamic markets in the coming decades for global airlines. Antony Wolfe examines rigorously the prospects of the African aviation market and assesses the likelihood of a European low-cost airline entry into the market.

Introduction

The Ryanair low-cost business model has been very effective in the European market. The airline cuts inefficiencies by keeping solely one type of aircraft across the fleet, flying point-to-point to small regional airports with quick 25-minute turnarounds. The resulting lower fares have been enhanced by the rise of the internet, which helped by cutting out expensive middlemen combined with minimal marketing. Increased competition in the sector will force airlines to streamline their costs and thereby lead to lower fares as airlines strive to capture market share.

This essay will look at airlines in the African aviation market and investigate the possible entry of Ryanair into the market. A low-cost carrier could provide competitive fares to the rising middle class in Africa, who will have more disposable income to spend on air travel in the future throughout this vast continent. Africa's sheer size and variable terrain makes air travel particularly suitable to the continent. Airline services here are driven by tourism, attracted by the first 2010 FIFA World Cup in South Africa for example, but civil unrest in regions such as Libya and Egypt in recent times will likely harm tourism for years to come. Travelling around the continent is an ordeal, even without factoring in the current poor level of infrastructure, relative to European standards. The key issue addressed in this essay composes of the advantages and disadvantages of Ryanair entering the African air market in the future, focusing solely on passengers. The time period here is very important; without a sizeable amount of investment into African aviation, the entry of Ryanair in the next decade looks unlikely.

Following the introduction, section two will study the current status of the African aviation market, section three will look at problems facing airlines entering the African market and section four will investigate the probability of Ryanair entering the African market. The conclusion sums up the African aviation market's prospects for the future.

Current Status of the African Aviation Market

The principal feature of the African aviation market is that it is in need of major development. While passenger traffic has increased dramatically in recent years "from 31.5 million in 2000 to 56.2 million in 2009" the fact remains that very few African airlines are profitable (Chingosho 2011). In 2010, the worldwide airline industry turned a profit of $16 billion but only $100m was made to African airlines (Chingosho 2011). This is due in part to the fact that Africa has a minuscule amount of air traffic measured in RPK (revenue per passenger per kilometre) in comparison to Europe, where Europe has about 16 times the value of Africa (Chingosho 2011). However what truly drives profit in the sector is not revenue gained per seat per kilometre, but the overall operating margin. The real measure of profitability is "the airline's ability to generate unit revenues which are higher than its unit costs" (Doganis, p. 7). According to Doganis, the majority of loss-making airlines around the world often fail to "match supply and demand adequately" (Doganis, p. 19).

Evidently inefficiencies abound in the market. High cost airlines are "a function of the nature of their operations" where they could cut costs, but in the absence of competition, have no incentive to do so (Doganis, p. 7). African skies are currently full of foreign airlines, especially in former French colonies where "Air France has a de facto monopoly" (Chingosho 2011). Chingosho notes that "the airlines in the North of the continent are the most successful"; which makes sense given their geographical proximity to the European market (Chingosho 2011). Many state-owned airlines such as Air Algérie receive large subsidies to maintain routes which may be beneficial from a social point of view but accrue little revenue, for instance "the provision of services to isolated and small domestic communities" (Doganis, p. 149). The high cost makes these services inefficient. To cut costs further, airlines need to keep only one type of aircraft to save on maintenance and training costs. For example in 1999 "Air Madagascar operated eighteen aircraft of six different types" (Doganis, p. 137). If the market for routes were competitive these practices would prove unsustainable.

There is progress in the market in the form of increased co-operation among African airlines. For instance, Egypt Air now has partnership agreements with 20 other airlines. Further collaboration between airlines is needed to stimulate growth and spread ideas for better practice. Continuing in this vein, AFRAA (African Airlines Association) provides a strong union for African carriers as it "represents 83% of total international traffic carried by all African airlines" (Chingosho 2010). There are economies of scale and other benefits from co-operating and sharing ideas on best practices in safety and other aspects. However, a brain drain out of the continent robs the aviation industry of highly-skilled workers. In addition to pilots and engineers, airlines regularly change CEOs. For instance Cameroon Airlines and Air Zimbabwe had "six CEOs in the period 2001-2007" (Chingosho 2011). This recurring phenomenon is disruptive for stability and growth.

The large numbers of small airlines in Africa are stumbling blocks to a fully competitive market. The majority are state-owned and thereby protected from competition. This stems from the desire of many nations to have their own flagship carrier and these nations therefore tend to prevent competition to that airline. Guttery condemns these "costly shows of patriotism" (Guttery, p. 1). This is portrayed by AFRAA's list of union members, where the majority of the list seems to be made up of small national airlines (www.afraa.org). In addition, states have varying degrees of taxes, charges and visas that prohibit the free movement of people and goods. Lower fares would be difficult to implement, but, as a starting point, governments should decrease taxes on aviation to encourage demand, as the industry is currently "over-taxed and over-charged" (Wings over Africa, Dec. 2012). In the future, a burgeoning middle class with increasing disposable income could then afford to spend money on airline travel instead of alternatives.

The African market should be competitive according to Baumol's description, where "entry and exit are completely free", where foreign airlines would enter and consumers would benefit from lower fares (Baumol 1982). But Chingosho states that 51.4% of the 660 city-pairs in Africa are served by "less than 5 flights per week" (Chingosho 2010). A solution to monopoly airlines on routes is to provide a Demsetz auction for competition to have "competition for the market where it is not possible in the market" for routes that may not have enough demand to support multiple airlines (Barrett, p. 29). The Yamoussoukro Decision, agreed by 44 African states in 1999, is a step in the right direction towards solving this barrier to competition.

The Yamoussoukro Decision aims to increase co-operation in the African aviation market. Its foundations were set in the Yamoussoukro Declaration of 1988 as it "commits its 44 signatory countries to deregulate air services, and promote regional air markets open to transnational competition" (Schlumberger, 2010). This accord includes the "liberalization of passenger and cargo services" as well as the exchange of fifth-freedom traffic rights, which comprise "the right of an airline from country A to carry revenue traffic between country B and other countries such as C or D on services starting or ending in its home country A" (www.africa-union.org) (Doganis, p. 336). This accord is pivotal to African aviation growth as it would provide competition for routes. However, not all African states are in agreement. The author of the report, Charles Schlumberger, states "ten countries have not signed" despite the World Bank report stating that "liberalized air transport would deliver improved safety, lower fares and increased traffic in Africa" (Schlumberger 2010). The full implementation of the Yamoussoukro Decision across all African countries would undoubtedly take away the clouds that block open skies for the continent.

Problems Facing Entrants to the African Market

The unease of doing business in Africa is seen as a barrier to trade for firms. A report by Barclays Bank Ireland titled Trade with Africa found that "respondents were wary of the continent as a business partner" with regards to corruption and a lack of infrastructure (Business World article, November 2012). Also, conflicts abound between or within states and future conflicts would almost certainly impact on revenues in regions affected by civil unrest. However, "62% believe opportunities will develop positively over the next decade" which embodies an opportunity for Ryanair to enter (Business World, Nov. 2012).

Fuel price increases have reduced profits across the industry. In 2011 the cost of fuel represented "29% of operating costs" (Chingosho 2011). This signifies an opportunity for Ryanair, who could possibly benefit from economies of scale from their existing operations in Europe. Ryanair would likely have a higher number of newer aircraft than African airlines, aircraft which don't guzzle as much fuel as older models. This drive for efficiency has not yet reached Africa, where industry margins were just "0.7%" in 2011, meaning any inefficiency will impact heavily on profit (Chingosho 2010).

A lack of infrastructure in Africa harms any drives for efficiency and also means there are problems of hub airport dominance, which Barrett calls "the most important obstacle to contestability" (Barrett, p. 23). A huge investment in infrastructure would be needed to build regional airports which the majority of African states would be unwilling to countenance. An additional setback includes the large amount of existing infrastructure and airspace that is normally reserved for military use. This problem is not just limited to Africa: for instance in 1989, there was an "average extra journey length of 10 per cent in Europe because of military zones" (Barrett, p. 37). A possible solution would be to auction the airspace to ensure this limited resource goes to the highest bidder, as Barrett states, "airspace is now scarce, and a system of property rights is appropriate" (Barrett, p. 37).

Safety stems from this lack of infrastructure and remains a priority for improvement in Africa. The safety standards of African domestic airlines are compromised, showing that the African "accident rate is more than 12 times higher" than the European equivalent (Schlumberger, 2010). In addition, "more than 25% are on the EU blacklist which continues to grow, with no country in Africa ever having been removed from the blacklist" (Wings over Africa, Dec. 2012). Perhaps the entry of non-African airlines could help show the best practices in safety standards drawn from their economies of scale. Other possible solutions include better marketing and increased safety training for employees. Nevertheless, this poor safety image begs the question: if African airlines and airports are deemed to not be safe, why would Ryanair or other carriers enter? These airlines are not going to invest in those facilities themselves. To attract foreign airlines, there needs to be a huge amount of investment in the aviation sector in Africa, which unfortunately does not seem likely to happen in the next decade.

The Likelihood of Ryanair's Entry

There are great prospects for air travel growth in Africa. Ryanair could provide low-cost air travel as the continent's "rapidly expanding middle class increasingly need goods and services which cannot be catered for domestically providing a golden opportunity for Irish businesses" (Business World, Nov. 2012). The cost structure of a low-cost carrier like Ryanair is different to the majority of African commercial airlines. According to Doganis, the main outlay of low-cost airlines are spent on direct costs such as "flight operations, maintenance and depreciation" that tend to exceed "60% of total operating costs" (Doganis, p. 87) but the airlines save a lot of resources in indirect costs including "ground expenses, passenger services and promotion" (Doganis, p. 88). Ryanair also have a relatively low marketing budget compared to other major European airlines, proving the airline does not waste resources inefficiently on advertising.

The opening of provincial airports could allow Ryanair to cut costs further. Following a successful cost-benefit analysis appraisal, potential projects could demonstrate that the time savings gained would offset the cost of the initial investment. For instance, in the Irish case, in 1989 Knock airport gained a huge increase in passengers and "generated time savings for the 170,000 passengers [...] to the value of £4.6 million" (Barrett, p. 36). An airport benefits the wider economy in the surrounding area, as the increased economic activity creates jobs and drives commercial growth. Schemes such as duty-free shopping entice consumers to spend in that country.

However Africa covers a lot more land mass than Europe. Domestic regional air services within some countries in Africa would include larger distances than Ryanair currently flies within Europe. The impact on fuel costs would hamper the company's ability to provide low fares. Nonetheless, certain countries within Africa could be used as strategic stopovers or hubs for refuelling due to the long distances. For example, Ryanair could use Morocco, where the airline has already established operations. Of course, the market may not need Ryanair if the market for charter airlines were to develop. In Europe's case, the increase in tourism prompted the increased supply of charter "which attained over 40 per cent of the passenger market within the region" (Barrett, p. 4). According to the Cascade Studies, these charter airlines charged much lower fares than the incumbents, finding that "actual charter fares were between 32 and 37 per cent of the scheduled airline fares" (Barrett, p. 4). If Ryanair chose not to enter, then perhaps charter airlines could meet the demand.

Ryanair would not be the first low-cost airline to enter the African market. Fastjet, built on the model of Easyjet in Europe, will commence flights "from Dar es Salaam in Tanzania at the end of the month for prices starting at $20" (Guardian Weekly, Nov. 2012). Bureaucracy means that progress is slow, but the Fastjet CEO Ed Winter (formerly of Easyjet) "has outlined a rough sequence for the markets which Fastjet plans to enter using the air operator's certificates of Fly540" (Air Transport World, Nov. 2012). Should the airline prove a success, it would send a clear signal to African governments, who would wish to facilitate more start-ups like Fastjet.

Conclusion: Future Prospects

There is huge market potential in Africa. Many airlines compete on routes out of Africa; therefore, it follows that the "best opportunities for growth and expansion for African airlines lie in the under-served African regional and domestic markets" that suits Ryanair's short-haul point-to-point model (Chingosho 2010). However, there are many challenges that would prevent Ryanair from entering in the near future. Africa spans a much larger area than Europe and there are big question marks over infrastructure and safety within the sector. The current conflict in Mali represents an example of the political fragility of many African states.

Over time, the aviation sector will develop and in the medium term it is possible to see the entry of Ryanair into the African market. Due to the size of the continent, Ryanair would initially enter only a portion of the African market, for instance expanding services from their existing operations in Morocco solely across North Africa, instead of taking on the entire continent. They could then develop their routes across the continent over time.

The foundations laid by the Yamoussoukro Decision will open up the African skies for more domestic start-ups like Fastjet. Airlines will streamline costs to cut fares in competition for the market share of the rising African middle class. Small national airlines will either fold or merge to survive in the competitive market. There are still barriers to competition to overcome. The continent-wide removal, or at least reduction, of barriers to the movement of goods and people, such as tariffs and visas, would undoubtedly stimulate the market for air travel for firms and consumer alike. Regardless, Africa's potential ensures the prospects for its future are bright.

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