



The carrier-within-a-carrier strategy: An analysis of Jetstar



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ABSTRACT

The carrier-within-a-carrier (CWC)—or “airline-within-an-airline” (AWA)—approach has become an integral part of many airlines’ marketing strategies in the Asia–Pacific region where several full-service national airlines operate low-cost/low-fare subsidiary airlines. The CWC approach is a response to competition from low-cost carriers based on product differentiation, i.e., a ‘two brands’ business strategy aimed at defending market share. Most CWCs were established after 2001 as a response to deregulation and liberalization and generally adhere to the principals of low-cost/low-fare carriers. Typically, CWCs enter markets through new, point-to-point services and operate short-haul routes (one-to 2-h flying times) that might have been abandoned by full-service airlines (FSAs), whereas at other times they simply compete directly with FSAs on price. This paper analyses Jetstar, a subsidiary of Qantas, which has transitioned from a domestic CWC to an international medium- and long-haul carrier. In addition to its domestic Australian operations, Jetstar operates between Australia and the Asia–Pacific region and has established partnership arrangements operating within Asia, including Jetstar Asia (based in Singapore), Jetstar Vietnam and Jetstar Japan. Jetstar also has operations in New Zealand. The theoretical framework applied in this paper is based on the strategic windows concept, in which opportunities arise and a window opens, and Tregoe and Zimmerman’s (1980) ‘driving forces’ model, in which nine attributes are listed and certain of these are exemplified by Qantas’ strategy. The methodology adopts a case study approach that draws upon content analysis and ‘events in the making’ and features interviews with key respondents. The findings show that Jetstar disproved earlier criticism of the CWC strategy and further demonstrate that by careful planning, strategy and execution, Jetstar has been able to grow its capacity, maintain high load factors, increase revenue and (more importantly) increase profitability at a time when many airlines are consolidating or withdrawing services because of losses.

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1. Introduction

Global aviation has been reshaped by powerful forces, including deregulation, liberalization, open-sky policies, the Internet, a rising middle class in many Asian societies with the desire to travel, modern fuel-efficient aircraft, new business models and more liberal collective bargaining agreements among low-cost airlines, unions and employees. The emergence of low-cost carriers (LCCs) is now well established in nearly all aviation markets (Gross and Lück, 2013); these LCCs typically operate as variants derived from the pioneering Southwest Airlines (USA) and Ireland-based Ryanair, which in 2009 was Europe’s largest airline in terms of passenger numbers and market capitalization (Ryanair, 2009). The Centre for

Asia Pacific Aviation Studies (CAPA, 2005) identified five key features that have attributable to the growth of low-cost carriers in aviation markets:

1. Rapid demographic and economic progress in many countries;
2. Current aviation market opportunities (and threats to the survival of conventional models);
3. Congested, high-cost hub airports alongside underutilized regional airports and growing difficulties in raising capital for new infrastructure;
4. Broader government policy objectives to stimulate tourism and trade outside of capital cities; and
5. Opportunities for soft liberalization that allow international access to smaller airports behind national gateways with limited risk to national flag carriers.

The aim of this paper is to analyze the Qantas/Jetstar growth strategy with particular emphasis on Tregoe and Zimmerman

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(1980) 'driving forces' model, in which nine attributes are listed and certain of these are exemplified by Qantas' strategy. In particular, this paper focuses on how these driving forces have contributed to Jetstar's performance in terms of profitability. Qantas is currently in the midst of a transformation strategy that includes discontinuing loss-making routes and efforts to better position Jetstar in Asia. The Qantas Group is under intense competitive pressure in all the markets in which it competes and announced an underlying pre-tax loss of AUD \$252 million for the half-year ending 31 December 2013, which represents its worst fiscal performance since the airline was privatized in 1994 (Taylor, 2013). This performance has led the Australian Parliament to discuss a possible change in the Qantas Sales Act 1992, including the possibility of increasing foreign ownership.

The structure of the paper is as follows. The literature review discusses the limited number of studies of the carrier-within-a-carrier (CWC)—or "airline-within-an-airline" (AWA)—approach, in which researchers have identified the difficulties involved in establishing two separate airlines on different business platforms that share the same parent airline. The method adopted in this research is a case study approach that employs content analysis and data from newspaper articles, aviation publications and Qantas' semi-annual and annual reports. Semi-structured interviews were also carried out with Qantas' CFO and a director from the CAPA — Center for Aviation. The case study developed in this research describes Jetstar's route expansion, its rapid growth and market extension into Asia and its financial results. However, the study has several limitations, such as the difficulty of dissecting Jetstar's different operations, which are aggregated for reporting purposes.

2. Carriers-within-carriers (CWCs)

Several researchers have questioned whether full-service airlines (FSAs) might create distinct business streams on a single integrated production platform. Lindstadt and Fauser (2004) and Gillen and Gados (2008) assess the problems associated with mixing business models and suggest that AWAs use different operating parameters requiring a different type of culture that eventually results in a poor strategic fit with the parent airline's business model. Graham and Vowles (2006) posit that CWCs represent a strategic response to the growth of low-cost airlines that had tapped into the price-conscious leisure market. Several airlines that previously established subsidiary airlines have now re-absorbed those subsidiaries and created an 'economy lite' product that offers a certain number of seats on specific flights 'down the back' that require payment for food, refreshments and in-flight entertainment.

The emergence of low-cost/low-fare airlines is now well established in diverse aviation markets, including South America, Asia, North America and Mexico, the Middle East, Europe and Africa. These airlines operate idiosyncratically, that is, each airline adapting to its own markets and characteristics. Moreover, the CWC strategy has become increasingly popular in the Asia-Pacific region, in which up to 12 airlines are subsidiaries of parent airlines (Gross and Lück, 2013). This development has occurred in response to what CAPA (2012) described as 'soft' liberalization.

The low-cost airline industry, which accounts for 17% of global airline passenger traffic (IATA, 2013), has been described as a concept, as a phenomenon and as a business strategy. Jarach (2004, p.24) discusses the 'low-cost phenomenon' by contrasting the operating environment and outcomes between what he termed "LCCs on the attack and national airlines on the defence" and defined LCCs as having a "simplified value proposition to a wider market potential". Alamdari and Fagan (2005) acknowledge LCCs as

a concept but then more fully describe the sector as an evolved business model that is being reworked and adapted to suit various types of operating environments in different markets. Moreover, these and other authors have observed that the original low-cost model has been modified over the years and that LCCs were tending to follow a product differentiation strategy as opposed to the cost leadership principles on which the original model was based (Hansson et al., 2003; Daft and Albers, 2013). A number of 'hybrid' low-cost models now operate in different markets in which CWCs also operate, which suggests that the LCC business model is not static but shifts according to the dictates of market and financial conditions (Lohmann and Koo, 2013). Jarach (2004, p.25) noted that low-cost airlines act as "flexible, dynamic and innovative players, eroding the advantages of network carriers". Alternatively, the CWC strategy might also be considered market cannibalization because passengers sometimes take advantage of a lower fare by switching from a parent airline to its subsidiary.

The CWC concept is used by more than 20 of the world's leading airlines, and approximately 58% of the world's CWCs are based in the Asia-Pacific region (Pearson and Merkert, 2014). However, the rise of the CWC strategy has received little academic attention. Pearson and Merkert (2014) provide a synopsis of past CWCs and, more importantly, evaluate the performance of CWCs presently operating in Europe, Asia and South Africa. Their study emphasized four key areas that contribute to the success or failure of a CWC: (1) ill-defined strategies and the need for decisive leadership, (2) late market entrance and the need to achieve market dominance, (3) excessive management control and insufficient dissimilarity from the parent airline, and (4) higher costs and less efficiency vis-à-vis LCCs. This synopsis compared the CWCs' yields (cents per seat kilometer earned) and load factors with those of their parent airlines. However, these measures do not assess profitability or return on capital.

With respect to Qantas, the case that is the subject of this study, its strategy exemplifies what Stahl and Grigsby (1997) define in the strategic management literature as a pattern or apparent behavior that emerges from a series of actions, i.e., a position or match between an organization and a product-market area, such as a product differentiation strategy. The Qantas Group complies with Stahl and Grigsby (1997) product-market area and product differentiation strategy in which one airline—Jetstar—covers the diverse market with a variety of airline products and routes that reflect different service levels (Homsombat et al., 2014). More specifically, Tregoe and Zimmerman (1980) established a framework for strategy and nine possible 'driving forces' (i.e., products offered, market needs, technology, production capability, method of sale, method of distribution, natural resources, size and growth, and return and profit) in this framework, although they urged executives to base their strategic decisions on a single 'driving force'. However, as opposed to having one dominant driving force, as suggested by Tregoe and Zimmerman (1980), strengths are required across a diverse number of driving forces to compete effectively. Mintzberg (1994) argues that strategy emerges over time as intentions collide with and accommodate changing realities. One might start with a perspective and conclude that it calls for a certain position, which is to be achieved by way of a carefully crafted plan, with an eventual outcome and strategy reflected in a pattern that is evident in decisions and actions over time. This pattern in decisions and actions defines what Mintzberg (1994) called 'realized' or emergent strategy. A plan is crafted (e.g., segment routes according to the predominant type of traffic and lower unit operating costs), and the outcome is determined over time through revenue and profit growth, route expansion and a focus on cost reduction strategies.

The 'planned approach' emphasizes a long-term, highly systematic and deterministic process of strategic planning that aims to

achieve the best fit between the organization and its environment. In Quinn's (as cited in [McKiernan, 2006](#)) 'logical incrementalism' approach, the author claimed that strategic management involves guiding actions and events toward a conscious strategy in a step-by-step process. Quinn's guiding actions are taken one step further by [Markides \(1999\)](#), who describes strategy formation and implementation as an on-going, never-ending integrated process that requires continuous reassessment and reformation. Thus, Qantas' planned strategic approach is consistent with the strategic management literature wherein its strategic window opportunities have evolved rationally in response to changes in the environment, such as the intensity of competition, pressure to reduce costs, labor market changes, aviation liberalization and technological advancements.

The principle of market segmentation consists of dividing a total market into manageable components such that the organization might concentrate its resources on those segments in which it decides to compete and, more precisely, to serve those markets' needs. The airline industry typically segments its markets into business and leisure customers and requires leisure customers to book and pay in advance and to apply conditions that penalize any changes to the booking that business customers are loathe to be locked into. Thus, the Jetstar product is aimed at leisure and price-conscious travelers. However, Qantas' strategy has been to segment its market according to routes; thus, when a particular route carried predominantly leisure travelers, the Qantas full service product was withdrawn and replaced with the Jetstar product.

3. Method

The data used to conduct this case study was derived from newspaper articles, aviation publications, annual and semi-annual airline reports, and IATA and Official Airline Guide (OAG) web-site information in the public domain, in addition to interviews with senior executives of Jetstar and the Sydney-based CAPA. Relevant material collected during the 2004–2013 period helped generate a case study based on content analysis or, according to [Yin \(1994\)](#), on 'situations in the making' over a period of time. Content analysis provides a solid foundation of evidence-backed research and can chronologically record the strategic decisions of firms and their outcomes at different points in time. Studies on the aviation industry rely extensively on strategic and statistical analyses and typically employ 'case building' (which locates such research in the 'existing theory' category) rather than 'theory building' as the basis for developing an explanation. Specifically, the case study approach offers a bounded system within which to examine the research problem ([Gummesson, 1991](#); [Blaikie, 2000](#); [Stake, 1995](#)). Thus, the approach is well suited to illuminating a decision or set of decisions and explaining why such decisions were made, how they were implemented, and with what results ([Yin, 1994](#)). In essence, case study analysis is 'outcome evaluation' ([Stake, 1995](#)) and features what might be termed a 'face-value credibility' that can provide evidence or illustrations that certain readers can readily accept. For this study, the driving forces model developed by [Tregoe and Zimmerman \(1980\)](#) has been applied to initiatives and developments undertaken by Jetstar.

4. Background on the Qantas/Jetstar Group

The Qantas Board created Jetstar in May 2003 with the decision to establish a 'two brands, carrier-within-a-carrier' segmentation strategy (Qantas Press Release, 31 May 2003). The motivation for the decision was threefold. First, there was the need to compete with the rapidly rising Virgin Blue (currently Virgin Australia), an LCC that then featured a lower cost structure as measured in cents

per flown kilometer ([CAPA, 2005](#)). Virgin Blue's first commercial flight was on 29 August 2000; since that time, it has eroded the Qantas market share ([Roberts et al. 2011](#)). Second, Qantas' high cost structure was affecting its yield with respect to routes on which leisure travelers predominated because such travelers frequently seek the lowest fare. Third, Qantas was locked into legacy industrial-relations agreements that restricted labor market adjustment, flexibility and work conditions, which enabled a more flexible and agile Virgin to hold a 20–25% cost advantage over Qantas ([Bussell, 2010](#)). Finally, international expansion followed; in a mature Australian market, Qantas sought to expand into Asia, which was relatively late in opening its markets to increased competition and start-up airlines. The Jetstar brand now operates outside Australia in Southeast Asia, Japan and New Zealand and plans to commence business soon in Hong Kong ([Fig. 1](#)).

Jetstar's creation was initially met with skepticism from aviation writers and commentators. For example, Steve [Creedy \(2003\)](#), aviation writer for *The Australian*, observed that, "low cost airlines do not sit well with full service, network airlines", perhaps basing this conclusion on the well-publicized British Airways and KLM failures with LCC subsidiaries ([Harrison, 2001](#)). To establish the new carrier, Qantas expended considerable resources, i.e., close to AUD \$70 million ([Qantas, 2004](#)).

In the domestic market and on many international routes, Jetstar replaced former Qantas services. However, on some domestic routes in Australia, Qantas and Jetstar both offer services. Initially, Jetstar operated the so-called leisure routes on which the passenger traffic consisted of tourists or travelers visiting friends and relatives (VFR). For example, Jetstar flew to eight Queensland destinations (from Coolangatta at the southern tip of the Gold Coast to Cairns in Far North Queensland). However, in 2012, Qantas decided to re-establish mainline services between Sydney and the Gold Coast to satisfy business travelers who resented the 'no frills' Jetstar concept and to compete with Virgin Australia, which had decided to abandon the low-cost model and go upmarket.

Before engaging in its market extension strategy to Asia, Jetstar flew the A330 between Brisbane and Christchurch; in a departure away from most LCCs that operate only single-aisle aircraft, Jetstar introduced the twin aisle, 301-seat aircraft on routes between Australia and Asia and to Hawaii ([Qantas, 2005](#)). On 6 August 2007, [Australian Aviation Express \(2007\)](#) reported, "Jetstar to be the key vehicle for Qantas expansion into Asia". Many of the routes that Jetstar services are former Qantas routes. According to the Bureau of Transport, Infrastructure and Regional Development ([BITRE, 2012](#)), Jetstar was at that time ranked the third-largest carrier of outbound Australians traveling internationally. Simultaneously, Qantas took advantage of liberalization moves in Asia and established a majority shareholding in Jetstar Asia, which was based in Singapore. Jetstar Asia and Valair were two airlines under the holding company Orange star that were launched in 2004 as a partnership between Qantas (49%), two Singaporean businessmen (32%) and the Singapore government's investment company Temasek Holdings (Private) Limited (19%). Jetstar distinguished itself from its competitors by flying to destinations within a 5-hour radius from Singapore, whereas its competitors flew only to destinations within a 4-hour radius. This approach was considered the most ambitious start-up plan compared with any of the company's Asian rivals and would have given it the widest international coverage.

However, services to certain destinations that were previously announced (Shanghai, Jakarta and Surabaya) were not initiated. Flights to Shanghai could not be undertaken because China's aviation authority did not allow foreign budget airlines to fly to both Shanghai and Beijing. Flights to Indonesia were not feasible because the Indonesian government embarked on a policy of protectionism, which shifted Jetstar's attention to Cambodia. Next,

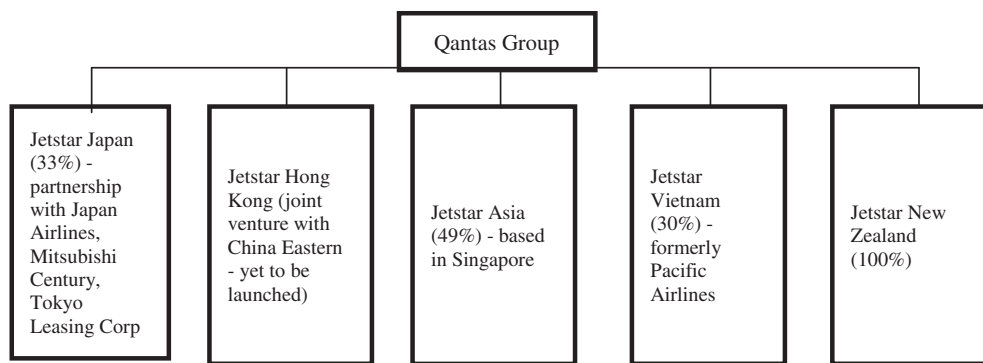


Fig. 1. Jetstar brands and proposed brands operating from bases outside Australia. Compiled by the authors.

Jetstar went against Tiger in head-to-head competition regarding a Phuket (Thailand) route that commenced on 25 October 2005. However, as a result of inconsistent demand and better opportunities elsewhere, Jetstar suspended the Phuket flights on 27 March 2008. By the end of December 2008, as Jetstar Asia was losing cash and its investors were struggling to finance the airline, Qantas decided to merge Jetstar Asia and Valuair into one refinanced entity.

On 16 April 2008, the company announced that it had achieved profitability for the year ending 31 March 2008. By June 2011, the company was carrying 2.7 million passengers annually, which represented an increase of 18% from the previous year. Revenue passenger kilometers (RPKs) increased by 39.7% following the launch of long-haul flights from Singapore to Auckland and Melbourne using Airbus A330 aircraft. Jetstar Asia has a fleet of 19 A320 aircraft and is headquartered at Changi Airport (Qantas, 2013 Annual Report).

In 2005, the new company received a cash injection of more than SGD 50 million in fresh capital, which was mostly provided by Qantas. Valuair's shareholders, including airline-industry veteran Lim Chin Beng, owner of Malaysia's Star Cruises and *Asiatravel.com*, became minority shareholders in the merged company, Orange Star, with Qantas owning 42.5% of Orange Star. Shortly thereafter, the company experienced more corporate shake-ups. Thus, over its relatively short life, there have been several senior management changes, and the new ownership structure of Orange Star consists of Westbrook Investments (51%) and Qantas Group (49%), under the banner of Newstar Holdings.

In 2013, Jetstar slowed expansion of its fleet and its available seat kilometers (ASK) from Singapore after a period of rapid capacity growth for all the country's major LCCs that intensified competition and affected its profitability. However, seat capacity has continued to grow rapidly as Jetstar Asia has increased its emphasis on short-haul Southeast Asian markets—particularly Malaysia (Fig. 2)—while decreasing its focus on medium-haul flights to North Asia, on which capacity has been shrinking, particularly to mainland China. Jetstar has made many schedule changes, adding or dropping destinations at short notice. Fig. 2 shows the weekly seat capacity of Jetstar Asia, whose short-haul Singapore-Kuala Lumpur route is its strongest.

Additional Asian expansion for Jetstar included Vietnam with a 30% shareholding in Pacific Airlines, which was later renamed Jetstar Vietnam. In 2012, Qantas established its Jetstar operations in the Japanese market in partnership with Japan Air Lines, Mitsubishi and Century Tokyo Leasing Corp. Qantas next sought to enter the Chinese market by establishing Jetstar Hong Kong and partnering with China Eastern Airlines. However, plans to have the operation running by the end of 2013 have been thwarted by regulatory

issues. Qantas has been unable to establish a footprint in the Chinese People's Republic, and its only current access to the country's growing outbound market to Australia involves code-share agreements with various Chinese airlines.

Jetstar Japan has great opportunities to take advantage of open skies between Japan, Korea and China and has significant growth potential (Creedy, 2014). Jetstar Japan is the largest LCC serving 10 domestic routes and flying up to 72 services a day with 18 A320 aircraft deployed. The low penetration of LCCs in North Asia was one of the reasons Jetstar targeted Japan; however, several predecessor LCCs have failed, including Air Asia, which withdrew from a joint venture with All Nippon Airways (mainly over its strict refund/ticketing policy), and Tiger, which was unable to obtain approval to launch an LCC in Korea. However, Steve Creedy portrayed a different perspective of Jetstar Japan by indicating that the budget carrier was struggling to raise passenger loads and faced delays in gaining access to Kansai International Airport, in addition to requiring a cash injection of AUD \$118.6 million from two of its three main shareholders—Qantas and Japan Air Lines (Creedy, 2013a).

Despite outwardly attractive markets with growth potential, Jetstar is competing against other LCCs in fierce and crowded markets, particularly in Southeast Asia, where it has a market share of approximately 8%, which is nearly identical to the market shares of Tiger and Air Asia. However, the company faces several challenges with respect not only to maintaining its short-haul operations from its Singapore hub but also to linking its Southeast Asia and North Asia strategies. Together with Jetstar Japan and a shareholding in Jetstar Vietnam (formerly Pacific Airlines), Qantas has been challenged by competitors on several fronts, which is straining the airline's finances and resources. Qantas has a sound cash-liquidity position; according to its 2012/13 Annual Report, liquidity stood at AUD \$3.4 billion for the year ending 30 June 2013. However, its Asian operations have been costly, and its Asian start-ups are not earning returns on its capital investment.

5. Jetstar driving forces

In their strategic management framework, Tregoe and Zimmerman provide the basis for defining a company's strategic profile. Whereas the framework does not exhaust all the possible contributors to understanding an organization's strategic vision, it has been used primarily as an important and simple tool to determine the future product and market scope that defines a business (Nourse and Roulac, 1993; Isorait, 2006; Hoogstra and Schanz, 2008). This paper uses the driving forces from Tregoe and Zimmerman (1980) to analyze Jetstar's past and future strategies for the business. Table 1 summarizes certain elements

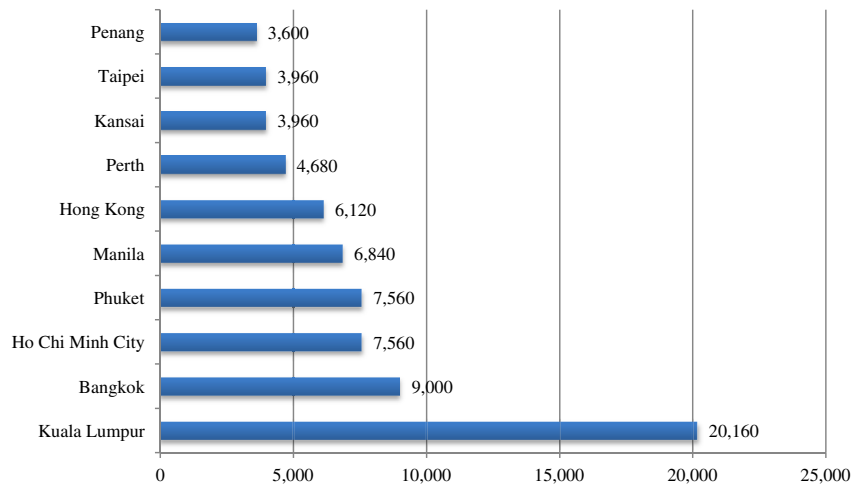


Fig. 2. Weekly seat capacity offered by Jetstar Asia from its hub in Singapore.
Source: Centre for Asia Pacific Aviation, 2013.

implemented by Jetstar, whereas the following subsections analyze some of Jetstar's key driving forces in more detail. As asserted by Tregoe and Zimmerman, a business might use one or more of the driving forces as a determinant for what it does.

5.1. Products and markets

Apart from the Brisbane-Christchurch service, another Trans-Tasman service was added in October 2009 with Jetstar operating between Auckland and the Gold Coast. Trans-Tasman routes between Australia and New Zealand operate under an 'open-skies' policy (Vowles and Tierney, 2007). In 2008, Qantas considerably revamped its Japan/Australia services, particularly those into Cairns, although the Gold Coast Airport (the only major low-cost airport in the country) was a major beneficiary from schedule changes securing services from Japan. In March 2010, Jetstar took over the Qantas code-share service with Air Pacific between Sydney and Nandi (Fiji), which was partly a reaction to Virgin's entry to the route.

Jetstar's expansion into international markets further exemplifies the application of strategic windows and a market extension strategy—taking a domestic product and extending it into an international market without substantial change (Fletcher and Brown, 2007) in seeking a competitive cost advantage against its rivals. Qantas has faced difficulties in matching the costs of its competitors, particularly Asian carriers, which has forced Qantas to review all its international operations and to stem its losses (see 'Capabilities' section for a discussion of labor costs). In mid-2009, Jetstar took over Qantas Jet Connect domestic services in New Zealand in a move that was designed to reduce costs and bring an LCC into New Zealand's domestic market, although by serving only four airports: Auckland, Wellington, Christchurch and Queenstown. Moves to align and integrate some services with its parent owner began in September 2009 when Jetstar began a code-share agreement on Qantas flights to Mumbai, India (Australian Aviation Express, 2009).

During his interview, Jetstar's CFO stated that although Jetstar had been handed routes from its parent owner, the new carrier nevertheless had to establish its brand and organizational culture in a highly competitive market among Asian carriers. The promotional message was clear and simple: a destination, price and offers to stimulate demand. Jetstar's CFO stated that Jetstar appealed more to the younger set of travelers but that it would be a mistake

to suggest that the product did not attract older travelers looking for a competitive price. Jetstar backed its decision with well-developed research and planning and a well-formulated marketing strategy. Although Australians comprised the largest share of its international customers, the Japanese predominated in the routes between Australia and Japan. Jetstar was particularly successful in Japan—a country in which Qantas had experienced some difficulty on the Japan–Australia route due to its high cost base—and a substantial shift to Jetstar services enabled the Qantas Group to compete in an important inbound market for Australia.

In 2008, Jetstar dropped plans to initiate operations into southern Europe based on the expected delivery of the new Boeing 787 Dreamliner (Smith, 2008); however, several factors have conspired against this expansion, including the following:

- the global financial crisis and the debt-ridden economies of Greece and Italy;
- Jetstar's concentration on growth opportunities that have presented themselves in the Asian market that are better suited to the Jetstar model; and
- parent owner Qantas entering into a five-year alliance agreement with Emirates Airline beginning on 1 April 2013, which provides Qantas passengers with better access to over 35 European cities by hubbing transfer passengers through Dubai.

When asked about services to southern Europe, Jetstar's CFO indicated that it was no longer a priority, and without ruling out such services, he said that China was the core of its pan-Asian strategy with capacity from the airline's Asian hub, Singapore. When questioned about operating wide-bodied aircraft with 300 seats, Jetstar's CFO indicated that increasing turnaround time is required but that increasing operational efficiency and aircraft utilization was the key (see, for example, the 'Capabilities' section below and the poor performance of Jetstar on delayed departure and arrival times).

5.2. Capabilities

Jetstar's early beginnings involved Boeing 717 aircraft into Tasmania taken over from the integration of the failed Impulse Airlines into Qantas in 2001. Upon its formation, Jetstar ordered a fleet of 15 Airbus A320s, which gave the airline a slight strategic advantage over Virgin because the A320s had more seats than the Boeing 737s

Table 1
Tregoe and Zimmerman's driving forces related to the Qantas/Jetstar strategy.

| Driving forces | | Elements implemented by Qantas/Jetstar |
|----------------------|------------------------|---|
| Products/ Markets | Products offered | Two brands strategy: Jetstar is a 'no frills' budget airline. Customers pay for ancillary charges. |
| | Market needs | Tourists, leisure travelers and VFRs: low fares, basic service, and point-to-point operations. |
| Capabilities | Technology | Jetstar has widely embraced new technology, such as automated check-in and airborne wireless. |
| | Production capability | One aircraft type for domestic routes. |
| | Method of sale | Purchase/lease new aircraft—save money on maintenance. |
| | Method of distribution | Encourage online bookings directly, i.e., bypassing travel agents (commission saving) and high use of Internet. |
| Results | Resources | Internet now extending to social media. |
| | | Less reliance on travel agents. |
| | | Adopt policies to avoid harm to the environment. |
| | Size and growth | Has developed own cadet flying school to draft qualified pilots into airline. |
| | | Domestic and international expansion within the first five years. From an initial 14 aircraft to over 40 aircraft at present that have carried more than 40 million passengers. |
| | Return and profit | Major contributor to the Qantas Flying Brands. |

and baggage could be containerized rather than loosely stowed in the baggage hold, which enabled faster unloading. More significantly, Jetstar's operation mirrored well-established and successful LCCs, including Southwest (USA) and Ryanair (Europe). Over-arching Jetstar's growth is that it has been able to grow its business by largely replacing or complementing Qantas' mainline services—particularly to tourist destinations. By early 2013, Jetstar was operating routes to 19 Australian domestic destinations, including 14 destinations along the Australian east coast (Whyte and Prideaux, 2008).

As with the A320s, Jetstar is seeking a competitive advantage by ordering 15 B787-8s to add to its fleet. In comparison with the A330-200, the B787-8 offers a number of operational benefits, including a 9.33% longer maximum range, an 8.51% faster cruise speed (for the long-range version) and a 68.4% shorter takeoff field (<http://planes.findthebest.com/>). The lighter and more fuel efficient B787-8 was delivered in 2013; by March 2014, it has been used in international routes between Australia and Indonesia, Thailand and New Zealand. The five-year delay in securing the first Dreamliner reduced the possibility of Jetstar having an earlier competitive advantage (Creedy, 2013) and led to changing plans regarding flying to Europe. The overall fleet strategy for Jetstar to acquire/lease newer airplanes also means lower maintenance costs (Lück and Gross, 2013).

Another way in which Jetstar has made strategic use of technology is by developing a hybrid model of distribution channels typically not adopted by stand-alone (non-AWA) LCCs. As part of the interviews undertaken for this research, Jetstar's CFO indicated that the airline opted to establish a selective distribution strategy rather than rely wholly on Internet bookings as most LCCs do. Thus, taking advantage of Qantas commissionable bookings, Jetstar's inventory is also made available to certain travel agents, which is a way of capturing segments that book predominantly through intermediaries. To achieve these types of bookings on a worldwide scale, Jetstar Group (including Jetstar Australia and New Zealand, Jetstar Asia, Jetstar Pacific and Valair) signed a deal with Amadeus, the most popular retail application for travel professionals (Factiva, 2013).

In addition to the use of technology, Jetstar has also made use of alliances, code-shares and interline agreements that are normally

adopted by FSAs to maximize their production capabilities. This strategy was adopted not only with Qantas on select international and domestic flights but also with other partner airlines and in groundbreaking alliance agreements. For example, on 7 January 2010, the Australian media reported a major cost-saving agreement between two of Asia's largest LCCs, Jetstar and Malaysia's Air Asia (Easdown, 2010). The announcement highlighted the potential cost savings in operating costs; the carriers would pool their expertise and buying power to generate and share synergy benefits of up to AUD \$300 million within 16 months of the agreement taking effect. Jetstar stated that the cost benefits would arise from jointly operated passenger and ramp handling services, shared inventory and shared replacement parts for the two carriers (Australian Aviation Express, 2010). An important difference between this agreement and most airline strategic alliances is that its emphasis is on the technical, engineering and operating characteristics of the airlines rather than on a joint marketing strategy. Although the Jetstar–Air Asia alliance may be different than typical airline alliances (there is no equity arrangement) and code-sharing arrangements adopted by FSAs, it suggests that LCCs may seek to emulate major airlines with loose forms of cooperation and consolidation. Another example occurred in 2011, when Jetstar formally entered into a marketing agreement with the oneworld alliance, which includes major carriers such as British Airways, American Airlines, Cathay Pacific, Finnair, Iberia, Japan Air Lines, Malaysia Airlines and LAN (Creedy, 2011); this alliance offered the carrier opportunities to code-share and—more significantly—to obtain feed traffic from other oneworld members. In a departure from the practice of most LCCs that operate independently and have avoided interline partners, Jetstar has eight interline partners, including three in the South Pacific and three in the Middle East.

5.3. Results

Until 2011/12, Jetstar's Australian operations achieved positive results, whether measured as growth, capacity, number of passengers carried, RPKs generated, revenue or profitability. In FY2008, Jetstar tripled its underlying earnings from AUD \$43 million to AUD \$121 million (pre-tax) on an 18.1% increase in revenue to AUD \$1.131 billion, partly as a result of route expansion but also due to cost containment and low cost per ASK. In FY2009, the company earned after-tax profits of AUD \$107 million and a capacity increase of 27.8% (Jetstar, 2009). In the ensuing year (2010), Jetstar's profit increased to AUD \$131 million (Jetstar, 2010). In 2011/12, Jetstar recorded a profit of AUD \$203 million with revenues rising by 18% and clearly marked the significance of Jetstar to the profitability of the "Qantas Flying Brands". In addition, Jetstar was able to reduce its unit costs to record low levels by achieving a 2% reduction. Ancillary revenue, i.e., revenue over and above basic fares (which is a key factor for LCCs), generated an average of AUD \$31 per passenger. This figure represented an increase of 20% from the previous year.

Jetstar's results are not segmented, which makes it difficult to analyze its operational and financial performance in different markets. The Qantas 2011 Annual Report states that Jetstar EBIT (earnings before interest and tax) amounted to AUD \$169 million, which represents an increase of AUD \$38 million (29%) over the previous year. Jetstar Asia's capacity increased by 46% in that same year. In addition, the Qantas 2012 Annual Report states that start-up losses that were incurred to position Jetstar for success in Asia amounted to AUD \$50 million and that the sustainability of Qantas brands over the long term depended on achieving its cost of capital. However, in Qantas' most recent statements concerning its profitability, there is concern about the slide in Jetstar's performance, which has sharply declined, resulting in a loss of AUD \$16 million

for the half year ending 31 December 2013. Given that Qantas domestic's profit fell from AUD \$218 million to AUD \$57 million because of extra capacity and soft economic conditions, it can be assumed that Jetstar also took a hit in the half year (even with 17% of the market) but also incurred substantial losses on international services and with its Jetstar Asia operation.

We posed a number of semi-structured questions in an in-depth interview with the Centre for Asia Pacific Aviation Studies' Executive Chairman, Dr. Peter Harbison, regarding these matters. Dr. Harbison stated it was becoming clear from Qantas' announcements and financial reports that the airline's international business was under pressure from the effects of rising costs – mainly in fuel – and static or falling yields, in addition to competitive pressure from airlines with a lower cost base. Dr. Harbison indicated that Qantas would have to rely more on Jetstar for its growth and retention of market share to survive the threat not only from Middle Eastern (Gulf State) airlines but also from the emerging Chinese airlines. Dr. Harbison opined that Jetstar would enter more collaborative arrangements not only with Qantas but also with other carriers where there were similar synergies and benefits that might accrue to both partners through scheduling, handling, marketing and particularly distribution.

When questioned about cost differentials between an FSA and an LCC, Dr. Harbison stated that modeling performed by his organization suggested that there were areas in which savings can be made but that the differential for long-haul operations compared to short-haul operations was smaller. He identified that some savings in direct operating costs might be attained in areas such as crew costs, ground handling and contracting out services, particularly if new-generation, fuel-efficient aircraft are in operation. Dr. Harbison believed that Jetstar learned much from the introduction of its services to Asia and that this experience would provide the platform for further long-haul expansion.

6. Conclusions

The development and growth of Jetstar conform to well-established frameworks of strategic management literature and exemplify the application of the strategic windows concept. From its inception to its present position, the CWC strategy implemented by Qantas has proven earlier critics of such a model wrong and has proven to be successful in domestic and international markets. Jetstar's development and growth is consistent with Tregoe and Zimmerman (1980) nine possible driving forces and McKiernan (2006) four key frameworks: the planned approach, logical incrementalism, outside-in analysis and inside-out analysis. Jetstar fulfills at least two of these frameworks and arguably all four.

First, from an analysis of the external environment and the forces within that environment, a planned approach has been applied by Qantas in route entry strategy, product differentiation and cost containment. The Jetstar model is a simple proposition: a low-fare market position achieved through a direct sales model, self-service and user-pay offerings, a simplified fleet and a lean and accountable culture. The planned approach emphasizes a long-term, highly systematic and deterministic process of strategic planning and aims at achieving the best fit between the organization and its environment. In this regard, the demand for a no frills type of domestic airline service became apparent following the rapid rise and market acceptance of Virgin Australia.

Second, logical incrementalism has been applied in the manner in which Jetstar has emerged from being a purely domestic carrier into an international carrier by first testing the waters with a market extension strategy across the Tasman and then graduating to wide-bodied aircraft flying to Asia and Hawaii. The expansion of Jetstar services to international destinations is consistent with

McKiernan (2006) logical incrementalism based on segmentation principles and combating aggressive competitors with lower costs than Qantas. International expansion has been based on the concept of a market extension strategy, i.e., what works domestically can be applied internationally, and Jetstar has undertaken the transition from domestic to international business almost seamlessly. Jetstar's growth over a 5–7-year period has been rapid but has responded to changing competitive and market conditions and various new opportunities arising from aviation liberalization and capacity increases to bilateral air agreements. Jetstar has demonstrated its flexibility and agility to be able to identify new opportunities in different markets, whether in Australia, New Zealand or Asia in both short-haul and medium-haul markets and to implement plans and strategies.

Third, the outside-in analysis and inside-out analysis could be said to apply, as Jetstar executives evaluate markets and new opportunities based on the strategic capabilities of the airline matched to the strategic window of opportunities presented. Jetstar has displayed flair, imagination, agility and flexibility and has demonstrated how it applies the strategic windows concept. Although it built much of its own capability and resources, the carrier has the benefit of a well-established strong parent owner that has the engineering, technical, planning, financial and marketing resources to support its subsidiary airline. Jetstar also conforms to Treacy and Wiersema (1997) in their study of the discipline of market leaders. The Qantas Group, with approximately 62% market share, is a clear market leader in the Australian domestic market, although it is under increasing competitive pressure from Asian and Gulf State airlines in its international business; however, the group (Qantas and Jetstar) is the market leader for all outbound travel from Australia (BITRE, 2012).

Although Qantas has defied the earlier critics of the CWC strategy, the strategy shows signs of weakening the Qantas brand and cannibalizing Qantas mainline services. CAPA (2013) reported that Jetstar might overtake Qantas on international routes, which have been subject to restructuring to discontinue loss-making routes. Despite these difficulties, the CWC strategy has been well established in the Asia–Pacific region by several leading airlines, including Air India, Asiana, Cathay Pacific, Japan Airlines, Singapore Airlines, and Thai International. Moreover, although the strategy has certain limitations, FSAs can use the “two brands” product differentiation strategy both to attack and to defend market shares. Despite past failures in some markets, the CWC strategy is less likely to fail in the Asia–Pacific region compared with an independent LCC when there is a strong, experienced parent owner with resources that include technical, engineering, operational, marketing and financial skills. Furthermore, strategic window opportunities will continue to be generated by market changes, such as further aviation liberalization, rising incomes and a growing middle class that is and will be seeking new travel opportunities.

In conclusion, there is room to broaden the analysis and discussion of the CWC strategy and to more closely examine those airlines in the Asia–Pacific region to learn more about which strategies are being adopted and what types of financial results are being realized. However, it would be wrong to suggest that a CWC strategy is a panacea for all major airlines. Each airline must assess its own network and markets, the extent of its competition and its costs, in addition to the industrial relations regime that impacts costs; nonetheless, much can be learned from the Qantas experience with Jetstar.

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