National University of Singapore

Source: *The Straits Times*, pB12
Date: 26 July 2021

Commentary

The airline sector and where travel is headed

Travellers seen at the Beijing Daxing International Airport on the first day of Labour Day holiday, in Beijing on May 1. Bain found that Asian domestic travel is starting to come back, largely driven by China. PHOTO: REUTERS

Focus now more on short-haul traffic but global vaccination efforts will drive recovery

Sherri Kimes

For The Straits Times

As vaccinations are under way globally, the global airline industry is also getting jabs of confidence.

Still, some parts are taking off faster than others and countries with a viable domestic market are faring better while business travel has taken a backseat.

The International Air Transport Association predicts that while budget airlines will lead the recovery, it will take until mid-2023 for the global airline industry to return to pre-pandemic levels.

In a similar vein, HSBC recently upgraded its rating of European low-cost carriers.

With closed or partially closed international borders in the near future, industry experts say that low-cost carriers serving local or regional markets may have an advantage over long-haul airlines.

Bain found that Asian domestic travel is starting to come back, largely driven by China. For example, during the extended May Day holiday, Chinese tourists made over 200 million trips. Both Asia to the United States and Asia to Europe flights are projected to be about 86 per cent of 2019 volumes by 2023. This does not bode well for full-service carriers that operate a high percentage of long-haul flights.

While budget carriers appear to have an advantage, they should still manage their finances well.

The competitive edge of serving domestic and regional markets may not be sustainable in the long term because the long-haul markets are expected to recover by mid-2023.

Border regulations can also change at short notice, making it necessary for airlines to find new revenue sources. For example, AirAsia has announced plans to look into grocery delivery.

WHAT DOES IT MEAN FOR AIRLINES?

People are also more likely to travel for leisure rather than business purposes in the near future.

McKinsey predicts that leisure travel is projected to recover by 2024, with a faster rebound in countries with stronger domestic tourism. On the other hand, it predicts that 20 per cent of business travel may not return.

Boston Consulting Group (BCG) forecasts that business travel will be down by 15 per cent compared with 2019, but points out that other forecasters are even more pessimistic.

BCG notes that how business travel recovers will vary by the type of interaction.

For example, internal meetings might be done online while customer-facing meetings could entail travel.

Corporate managers would scrutinise their budgets and wonder why travel, particularly international flights, which are more expensive, is necessary for internal meetings since Zoom or Microsoft Teams seemed to work perfectly well during the pandemic.

A reduction in business travel has serious implications for airlines such as Singapore Airlines (SIA) that have had a very profitable business travel market.

For example, should they reconfigure their planes or change their method of selling seats?

Given that consumer travel will take several years to recover, many airlines have increased their reliance on cargo flights. For example, strong cargo demand helped SIA to reduce its first-quarter losses.

It increased the frequency of passenger aircraft operating cargo-only flights and also maximised the use of its freighter aircraft so they could carry more cargo.

In addition, many airlines have reduced their capacity and, as a result, have been able to cut fuel and labour costs. Similarly, airlines such as SIA, Delta and United Airlines have reduced service levels, in part because of Covid-19 restrictions, but also in an attempt to lower costs. This has become even more important because of the increased cost of cleaning and hygiene procedures associated with the pandemic.

As you might expect, travel recovery will take a while. SIA's load factor – a measure of the passenger carrying capacity of an airline – was 14.9 per cent in May but an improvement compared with the 9.4 per cent in May last year.

Meanwhile, Cathay Pacific carried about 24,000 passengers in May, 99.2 per cent lower than May 2019 but up 30 per cent on May last year.

Many borders remain closed and are unlikely to completely open again for a while.

While domestic and intra-regional travel is expected to recover more quickly, particularly in areas with strong domestic tourism, it will still be some time before intra-regional travel returns to pre-Covid-19 levels.

WHAT DOES THIS MEAN FOR TRAVELLERS?

Besides flying preferences, one more notable change in the way people travel is where they stay. Vacation rentals have seen robust growth during the pandemic as consumers seek to have more control over their surroundings and health.

Vacation rentals are typically larger, can accommodate multiple people and are often more reasonably priced than hotel rooms. This, combined with the privacy and control that they offer, makes them particularly attractive to consumers.

Larger properties (four-bedroom villas and private houses) have had the strongest performance.

AirDNA research found that short-term rentals have been weathering the Covid-19 impact much better than hotels this year. Although it's still too soon to consider any upward trend a rebound, it is worth noting that alternative accommodations are showing more resilience.

Activities will change too. In a new normal, people will look for simpler activities in smaller groups. Buffets have largely disappeared or transformed into "a-la-carte" buffets during the pandemic, but are starting to make a comeback in the US and have been very well-received by consumers.

In the near term, tour operators and other agencies that facilitate mass tours will most probably need to reposition themselves and offer activities for smaller groups.

Once global travel recovers, the opportunities for larger tours will, as well. That being said, developing smaller and more specialised tours may provide an additional market segment and revenue stream for tour operators.

For now, pent-up travel demand is significant and low-cost carriers are well-positioned to lead the recovery since their focus tends to be more on domestic leisure and short-haul traffic.

Business and longer-haul international travel may not recover for a few years. As the worldwide vaccination drive continues, travel will return, perhaps at an even more robust level than pre-Covid-19. It's all a matter of when this will happen.

• The writer is a visiting professor in the department of analytics & operations at the National University of Singapore (NUS) Business School.

• The opinions expressed are those of the writer and do not represent the views and opinions of NUS.