



THE POST-COVID-19 FLIGHT PLAN FOR AIRLINES

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THE AIRLINE INDUSTRY HAS been hit extremely hard by the COVID-19 crisis—even harder, perhaps, than by the events of 9/11 and the 2008 global financial crisis put together. With unprecedented consequences, many airlines have grounded all, or almost all, of the planes in their fleet. Several are now flying passenger aircraft as freighters. Most of the commercial, network, and operations teams are still scrambling to repatriate passengers and decide which flights to keep. Meanwhile, executives are in touch with governments, employee representatives, and suppliers to formulate responses under very dynamic circumstances.

When flying through such turbulence, it's critical to focus on the horizon. Therefore, we propose a data-driven, action-oriented, and digitally supported “flight plan” to help airlines emerge stronger from the COVID-19 crisis.

Our flight plan for the new normal takes into account various air travel demand scenarios (which are in part a function of the

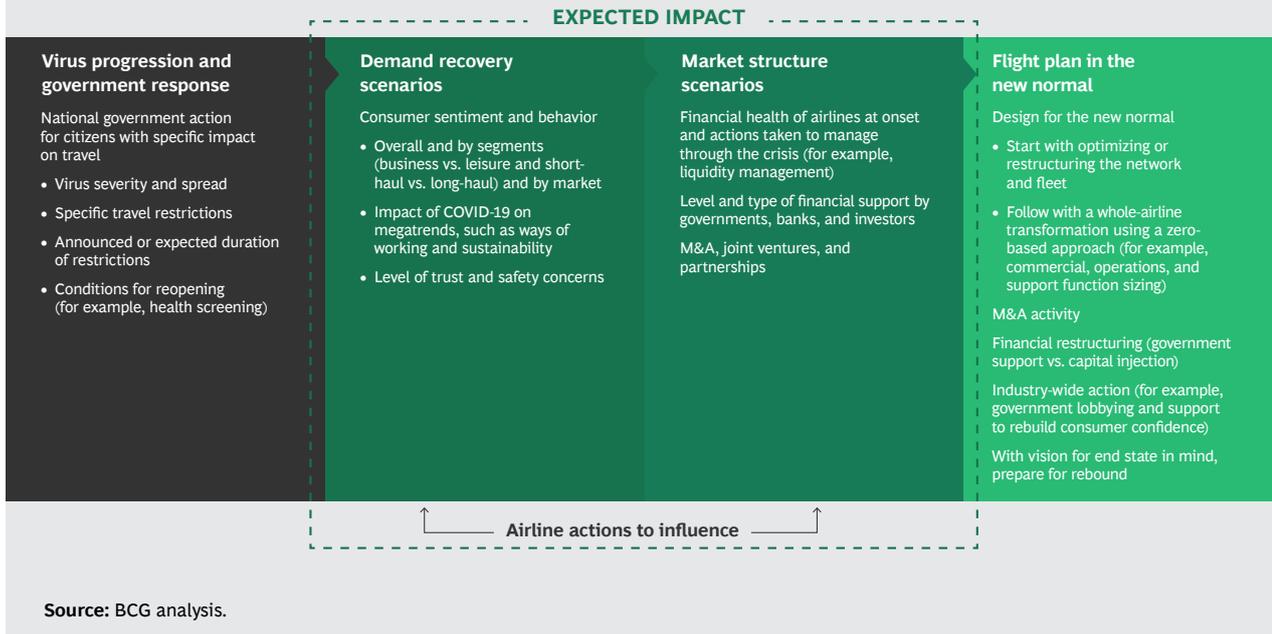
duration of the COVID-19 Crisis) and airline market structure scenarios (shaped by, for example, airline failures, government intervention, and consolidation). (See Exhibit 1.)

Duration of the COVID-19 Crisis

The most critical question today concerns the duration of the crisis in light of government responses and the progression of the virus. While we would all like to believe that the crisis will resolve within a matter of weeks, the reality is that we don't yet know how long it will last. What's more, the duration is likely to differ by region and by country.

So, for now, we are considering various scenarios and observing key indicators to learn which of those scenarios are most likely to occur. For example, we are tracking the spread of the virus by country and gauging the responses by governments, including the type and duration of travel restrictions and the specific conditions under which they might be relaxed. We are also

EXHIBIT 1 | Flight Plan to Succeed in the New Normal



monitoring indicators that measure consumer sentiment, such as internet searches. Also, we expect that governments might begin imposing specific limitations for inbound and outbound passengers, including requirements before boarding (similar to the security measures put in place after terrorism events), such as mandatory health screenings or certificates.

Demand Recovery Scenarios

Closely related to the duration of the crisis is the question of how quickly—and to what extent—air travel demand will recover. Data from previous crises, such as the SARS epidemic and the events following 9/11, shows how long it has taken the industry historically to return to precrisis levels. However, forecasts for the current crisis indicate that the duration and impact will be much more severe than any we've seen before. In mid-March, the International Air Transport Association (IATA) forecast a loss of \$252 billion in revenue—44% of 2019 revenue. As a result, the industry may have to manage structural demand changes (such as the state of the economy—depression, recession, and rebound) and megatrends (such as the dramatic rise in remote working, more locally oriented supply

chains, and a focus on sustainability). In addition, health concerns might initially curb passengers' inclination to fly.

We expect to see differences, in terms of duration and impact, between business and leisure travel for both short-haul and long-haul trips. For business demand, we expect a relatively quick rebound (in both short-haul and long-haul) as business travelers try to reestablish their businesses. However, the level of rebound will depend on the state of the economy and any long-term structural impact of remote working practices, which has yet to be determined and which will have to be assessed with consumer research. For leisure demand, we may see a distinction between short-haul and long-haul. For short-haul, we expect that many passengers will want to get away on trips after being housebound for weeks or months, once they are reassured that flying and traveling are safe again. Long-haul leisure usually takes more time to plan, so it is likely to rebound more slowly.

Our flight plan for the new normal must take these differences into account, especially when making network and fleet decisions, as well as planning for the initial rebound after markets reopen. For now,

we are tracking five potential scenarios: one, at this point, seems highly unlikely to occur; the other four are all possible, with the prolonged U-shape being the most likely, in our view. (See Exhibit 2.) We are also tracking the indicators necessary for any given scenario to become reality. This model allows us to forecast the demand outlook as accurately and dynamically as possible.

Market Structure

An important component of our flight plan involves assessing the market structure in the airline industry after the COVID-19 crisis. Which airlines will survive, and what will they look like? What will be the role of governments? Do we expect to see any consolidation?

Again, we must consider different duration scenarios. But we believe that, under any scenario, the industry will be forever changed, much as it was after 9/11 and the 2008 crisis.

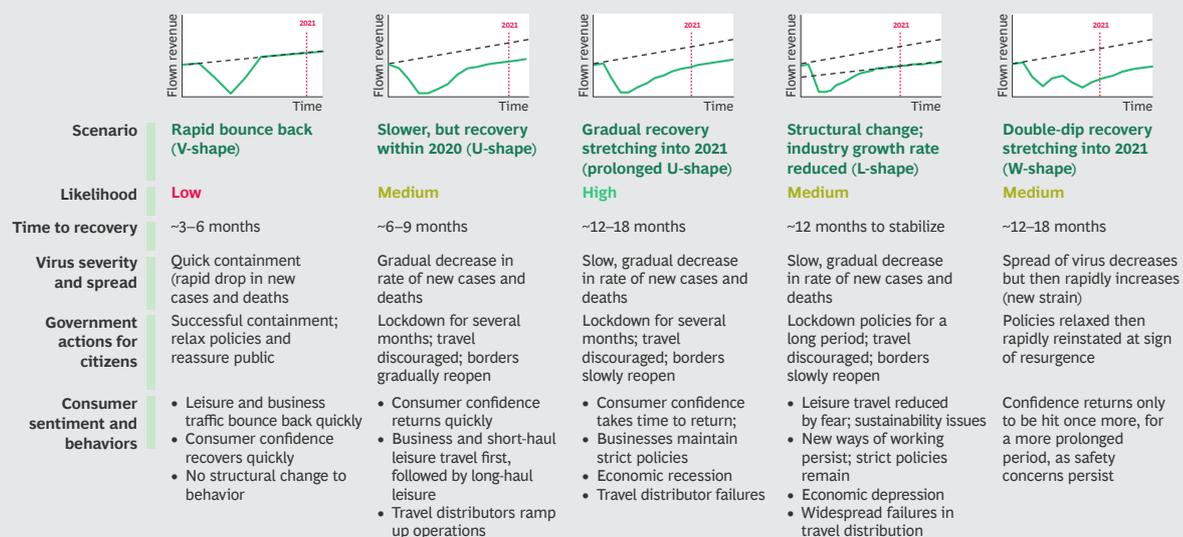
To predict the market structures that could arise given the different duration scenarios, we first take into account airlines' starting positions in terms of liquidity and balance sheet strength. Then, to predict viability,

we factor in potential government support as well as any given company's ability to adjust the cash-out.

Predicting which airlines that governments will choose to continue to support for more than a few weeks or months is complex. For example, it might be challenging to encourage governments to invest in airlines that are based in other countries—such as carriers that are part of airline groups. Governments may well want to support investment in their own country's airline while ensuring that they do not support (whether directly or indirectly) airlines elsewhere. They may also need to consider the question of fairness when multiple airlines in a particular country require support. And beyond government support and market concentration (as a result of some airlines failing because they could not gain support from governments or other investors), there might be some consolidation opportunities, particularly as the industry rebounds.

We expect the changes in regions, and the countries within them, to differ significantly, largely because of the variation in governments' responses to the crisis and the types and levels of support they offer. For example, in Europe, several countries have

EXHIBIT 2 | Five Demand Recovery Scenarios in a Highly Uncertain Future



Source: BCG analysis.

announced support for airline employees, which is helping companies to drastically reduce their employee costs. Similar support has been, or likely will be, offered (whether to employees directly or to companies) in the Middle East and some Asian countries. The US is offering a rescue package for all carriers that comprises a mix of payroll grants and loans.

We also expect airlines to differ within each region in terms of financial health, probability of benefiting from government support, and both willingness and ability to participate in consolidation or fragmentation.

In Europe, for example, several airlines that are part of an airline group were in relatively strong health as the crisis started. These companies are likely to receive government support because of their importance to the economy, and they could be the ones driving consolidation efforts. We also expect that smaller flag carriers, which have an important economic role beyond employability, will continue to receive either direct or indirect government support during the crisis, but we think that those airlines are unlikely to drive consolidation as buyers. Larger low-cost carriers (LCCs) were in strong health going into the crisis and may not require support (or, if they do, may need the support of multiple governments). For small airlines and tour operators, the level of support will depend to a greater extent on whether respective countries provide support to employees more broadly and whether those countries want or need to avoid favoring one airline over another.

We think that, in North America, there will likely be different outcomes for a wide variety of airlines—large network carriers (such as Delta Air Lines, United Airlines, and American Airlines), nationwide LCCs, smaller airlines, and independent feeders. (Compass Airlines is the first independent feeder to announce that it will cease operations; it will do so by April 7.)

Taking all these factors and hypotheses into account, we have defined three potential market structure scenarios. One is an

extreme version that could play out in Europe and Asia if the crisis continues for longer than expected. In that scenario, the industry regresses with a drastic reduction in the number of airlines, leaving a number of national carriers (with government ownership) and only the strongest LCCs.

A Successful Flight Plan for the New Normal

Armed with scenarios and data, and able to adjust for the nonstop flow of updates, our flight plan will help airlines succeed in the new normal. Though it is sufficiently dynamic to adapt to new circumstances, it offers stable guidance when it comes to fundamental, structural changes in the size and shape of an airline.

According to the flight plan, airlines should take the following actions:

- They should start by determining the optimal size and dimensions of their networks and fleet, and they should do so within the next few weeks. They should make big decisions—including which fleet types to recommission first and which routes are most likely to recover—on the basis of several demand and market structure scenarios and while optimizing for free cash flow. [Digital support tools](#) can provide network and fleet teams with the data-driven, granular simulations that help companies make the right big decisions on short notice.
- At the same time, airlines should consider M&A and consolidation opportunities. We expect that leading airline groups will be reviewing options, including potential divestitures and the sale or purchase of minority equity stakes.
- The next step is to resize and restructure the operating model and organization using a zero-based approach, which can be done in a matter of weeks. For example, BCG helped one global network carrier to redesign the entire organization—including process

redesign, organization size, and structure—in four weeks. The same approach can also be applied to procurement (in order to manage external providers) and technology. This work adds value that will remain well after the crisis is over.

- Airlines should also prepare for ramping up, once airports and countries reopen. Our work with several leading carriers reveals that the period of ramping up will be even more challenging and dynamic than the one for ramping down. Network redesign (which typically occurs from 4 to 13 times a year, with time to subsequently validate and hand over the schedule to resource providers) will now likely have to be done weekly. What's more, the time between developing and implementing the plan may be only a week or two—and will have to be accomplished despite the displacement of aircraft and staff. Designing this process,

and again leveraging digital tools to make the right tradeoffs, will be a major challenge that airlines will need to address as soon as possible.

- Finally, of course, finance teams will need to be closely involved to protect cash levels, capture revenues as soon as possible, and delay cash-outs as much as possible. Airlines should establish a project management office to manage cash until the environment stabilizes and regular financial processes and routines can be implemented once again.

THESE ARE TURBULENT times for airlines, yet the industry's response so far has been nothing short of impressive. Companies that take a data-driven, action-oriented, and digitally supported approach will have the best chance to emerge stronger from the COVID-19 crisis.

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