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The Pricing Evolution in the Air Transportation Industry. Implication for the Romanian Tourism Sector in the Era of Globalization

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Abstract *The globalization process involves the liberalization of the services and the air transportation industry is responsive to this reality. There is a developing tendency for global alliances and strategies in major airline companies. The globalization implies extending service networks in the whole world. Currently we are witnessing lower prices for domestic and foreign airline flights with benefits for the tourists' business and leisure activities. The last minute offers and early booking prices provide a win-win situation, for the airline companies on one side and for the customers on the other side. The positive online reviews influence people buying decision because customers are more sensitive than ever to the services prices. Under this condition it is very interesting to see the evolution of pricing in the air transportation industry and the implication for the Romanian tourism sector.*

Key words Air transportation, price in air transport, ticketing

JEL Codes: Z32

1. Introduction

In an era of technology, information, travel and tourism, the demand for international and domestic flights in Romania has grown significantly. In order to meet the strong demand for airline services, important low cost carriers have started to offer flights services. The expansion of globalization has been facilitated by technological development and advances. Particularly there has been a revolution in communications based on information technology and internet and a constant increase in the efficiency of transportation. These have made it easier, cheaper and quicker to complete international businesses (Tribe, 2005). Globalization is sometimes thought of as a synonym for global business according to Tribe (2005, p.335). The global air transport has been undergoing wings of change in the last 30 years as a result of deregulation and liberalisation (Wei Min and Luk, 2009). Airline transportation is a particularly significant aspect of globalization. In the 2015 IATA's annual review stated the fact that "the airline industry had another strong year in 2014, solidifying a positive trend in profitability after huge losses during the

2008 and 2009 global economic recession. Net post tax profit for 2014 was \$16.4 billion, a 2.2% margin on revenues. This was the fifth successive year of profitability, and it builds on the \$10.6 billion profit and 1.5% profit margin in 2013". "Jet fuel averaged \$116.6 a barrel in 2014, down 6% on the 2013 average price of \$124.5 a barrel. And consumers benefited from cheaper travel, with the average return fare (before surcharges and tax) declining 3% in 2014 compared with 2013, after adjusting for inflation" (IATA's annual review 2015). As we know, in emerging economies, GDP growth has a bigger role on air transport demand, as each unit of GDP determines more air travel in emerging economies than in mature markets. In 2014, this trend in demand was supported by significantly lower airline fares in markets outside the United States because of falling *fuel prices* (IATA's annual review 2015).

The transformations in technology that helped aircraft engines to consume increasingly less fuel have led to lower fixed costs for air travel and consequently to lower prices for the air transportation. There was also an increase in aircraft deliveries in 2014, to 1,627 new aircraft. The in-service fleet rose to 26,051 aircraft, from 25,187 in 2013. Replacements for older aircraft were generally larger in size than their predecessors, adding yet more seats to the global market. Overall, the number of seats available in the fleet rose to 3.5 million, adding 5% capacity to the market globally" in conformity with IATA's annual review 2015.

Aviation can be an interesting reflector of the current economic climate. It is one of the first industries affected by any downturn and then one of the quickest to show signs of recovery. It is therefore encouraging to see some early signs of commercial passenger growth¹. Passenger numbers at UK airports increased for the third year in a row, with an extra 7.8 million people passing through UK airports in the calendar year 2013 (2012 - a total of 228 million passengers) according to Civil Aviation Authority Annual Report & Accounts 2014.

According to the U.S. Airlines 2016 Annual Results, the U.S. Airline onboard passengers were 136.2 million or about 2.3 million passengers per day². The key drivers of growth for the airline industry in 2016 include the rising of the employment, the personal incomes, the air travel affordability and the improved airline operations³. Traditionally consumers are extremely sensitive to price, and the airline ticket prices are no exception from this rule. Indeed, few authors are willing to attack this topic because it is delicate to deal.

¹ http://publicapps.caa.co.uk/docs/33/CAP1193_Annual_Report_2014_web.pdf

² <http://airlines.org/data/a4a-presentation-industry-review-and-outlook/>

³ <http://airlines.org/data/a4a-presentation-industry-review-and-outlook/>

Currently we are witnessing lower prices for domestic and foreign airline flights with benefits for the tourists' business and leisure activities. The last minute offers and early booking prices provide a win-win situation, for the airline companies on one side and for the customers on the other side. The positive online reviews influence people buying decision because customers are more sensitive than ever to the services prices.

"Computer versus computer" or the price wars between airline companies computers and consumers computers. Airlines use computers to decide prices, benefit from yield management application and flyers use computers to find the lowest price. From this struggle over the years the pricing evolution in the air transportation industry was important to observe and to follow.

Under this condition it is very interesting to see the evolution of pricing in the air transportation industry and the implication for the Romanian tourism sector.

2. Literature review

Air transportation is a complex socio-technical system and its function is to transfer passengers and cargos over long distances across continents and countries. The pass-through of airline cost changes strongly depends on the type of cost and market conditions. With increased demand of air traffic, air transportation affects national or international economies considerably (Wandelt and Sun, 2015).

The service process for airline services has always been considered a primary influence on service quality and customer satisfaction. However, in a service process that begins with the ticket booking process and involves onboard services, various factors may result in service failure (Kai-Chieh and Hsiao, 2016). When the service quality does not meet the expectations of passengers, they become dissatisfied. The price in relation to services represents an important quality indicator.

Thomas Bieger, Andreas Wittmer and Christian Laesser (2007) in their paper talk about the airline managers of the future, as they should be aware of customer value as an increasingly important factor for driving continued growth. The focus, the authors say had to be put on real needs of the customers instead of stated preferences.

The UK Civil Aviation Authority has continued work in 2014 for consumers to have access to better and more relevant information about *the price and non-price aspects* of their buying decision. The consumers should have accurate, comparable information when they need it. Airlines are already complying with transparency rules on compulsory charges, and card charges have either been discontinued or are disclosed to consumers. Preparation of guidance for travel agents and tour operators is also underway.

In their paper, entitled, *Disentangling the European airlines efficiency puzzle: A network data envelopment analysis approach*, Meryem Duygun, Diego Prior, Mohamed Shaban and Emili Tortosa-Ausina (2016) highlight the fact that in recent years the European airline industry has undergone critical restructuring, evolving from a highly regulated market to a dynamic, liberalized industry.

In a free market competition, airlines tried to improve their customer services. They began flight services in new routes and developed various airfare policies to ensure their survival. Various new airlines, including low cost carriers, entered the air transport market to satisfy diverse air transport demands. Low cost carriers have tried to reduce all kinds of cost-related elements to secure their operating profits (Young, 2016).

The price dispersion refers to variation in prices for the same service or product, such as an economy-class flight from point A to B. The sources of price dispersion are numerous; in the case of air transport, price discrimination and peak-load pricing are typically cited as key determinants of dispersion (Obermeyer *et al.*, 2013).

In their book, *Low Cost Carriers: Emergence, Expansion and Evolution*, Lucy Budd and Stephen Ison (2014) present the network structure of Low cost carriers (LCCs) their pricing strategies and competition with network carriers, including their effects on reducing average fares.

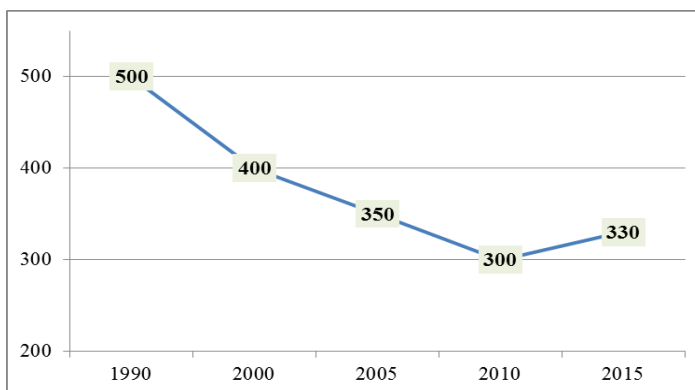
Low Cost Carriers (LCC) have undoubtedly revolutionized the aviation industry in recent years, and have become the dominant players in many markets. In response, full service carriers (or legacy carriers) have created new products, restricted and streamlined their operation and slashed costs, and often aggressively compete on airfares. As a result, low cost carriers can no longer rely solely on low airfares as the main driver of their business strategy in many markets, and have started to veer from the pure LCC model, exploring multi-channel distribution, allocated seating, and frequent flyer programs (Editorial Selected papers from the Air Transport Research Society World Conference, 2015).

Carl Koopmans and Rogier Lieshout (2016) show in their article that the airlines companies adapt their prices to demand (yield management), and cost changes will be passed through for less than 50% in prices.

In 2016, Hokey Min and Seong-Jong Joo pointed the fragility of the airline companies in the actual era of globalization. They brought to light the deregulations phenomenon that opened international airports and transcontinental routes to full competition. As we all know, in 2008 and 2009, the airlines companies were hit hard by increased taxation, instable yields, rising fuel prices, security hassles, and weak traffic volume. In order to survive to all this problems, the airline companies choose to consolidate their position forming strategic alliance and M&A (mergers and acquisitions).

3. The evolution of price in the airline industry

Once again the economic changes decide the fate of a sector activity, in this case the airline industry. In a few years, the globalization process allowed to the airlines companies to expand their market internationally, and to passengers to benefit from more flexible schedules, improved luggage handling and shorter travel times. According to the source Airlines for America the average round trip U.S. domestic airfares was \$500 in 1990, \$400 in 2000, \$350 in 2005 and \$300 in 2010, with an increasing trend for 2015.



Source: Airlines for America, <http://www.theatlantic.com/business/archive/2013/02/how-airline-ticket-prices-fell-50-in-30-years-and-why-nobody-noticed/273506/>

Figure 1. The evolution of the U.S. Domestic Airfares for round-trips (US\$)

The liberalization policy, representing the reduction of state control over airlines' internal and external operations and allowing free market competition, generated the fees and fares reduction.

The deregulation produced in the first place a speedy expansion of airline operations, and second a competitively priced for domestic and international air services. This policy led to an important growth in the number of passengers travelling, as well in the number of low cost carriers.

The increasing number of passengers has helped the low cost carriers to get sufficient return and profit. So, even if the LLCs cannot provide sophisticated services they have more and more passengers who want only a basic transportation function.

The concept of yield management is very important for the airline industry and represents the overall revenue that is to be obtained on each route. Yield can be defined as the air transport revenue obtained per unit of traffic carried or the total passenger revenue per passenger mile (Holloway, 2009, p.393). It is measured by comparing both the cost and revenue achieved per available seat mile. Comparing and balancing the proportion of full fares with those discounted both for economy or business class, the price of the airline ticket should be fixed ensuring that any drop in full fare will lead to an overall increase in revenue.

4. Implications for Romania's tourism regarding the prices of airlines

In the Romania airline market place there are airlines providing scheduled services and charter services. The charter services imply the fact that the aircraft is chartered to travel agencies and tour operators for a fixed charge and those travel agencies become in charge for selling the aircraft's seats. On the other hand, scheduled services operate on defined routes, internal or external, basis on schedule or timetable. The flight schedule for the regular flights is published and strictly respected. Creating alliance is in the benefit of the airlines because of their advantages such marketing facilities, low operational costs, sharing opportunities, all of this can lead to the price decrease. Regarding the airlines prices an important question arises: Why fares go down? *Because of the competition*. We know the fact that intensive competition in a sector of activity makes price sensitive issue.

For exemplifying the prices of airlines implications for Romania's tourism I will present the case of Dubai as a tourism destination for Romanians' tourists. The Romanian's tourists like Dubai and choose this destination for business and leisure. Until 4 and half years ago, TAROM had exclusivity for Bucharest-Dubai as a direct flight, without stopover. Holding monopoly position, TAROM was able to decide alone for many years the ticket prices for Bucharest-Dubai direct flights. A round-trip Bucharest-Dubai with TAROM in 2010 was around 650 euro, including fees.

In 2012, the low-cost airline *Fly Dubai*, owned by the Government of Dubai with Emirates, entered the Romanian market with four flights a week. A round-trip Bucharest-Dubai with *Fly Dubai* in 2012 was 450 euro, including fees. With zero stopovers *Fly Dubai* became a direct competitor for TAROM airline on this tourism destination. The low cost company Wizz Air also provided direct flights Bucharest-Dubai and Cluj-Dubai, which determined to lower the price of other airlines companies' operating Dubai destination.

In the present days (2016), we have air flights every day for Bucharest-Dubai and return line at 220 euro including fees⁴.

⁴ <http://www.tarom.ro/destinatii/dubai/>

08:10	→	14:35	 TAROM 67	- - - - S -	OTP-DXB
14:15	→	20:00	 flydubai 798	L - M J V - D	OTP-DXB
15:05	→	20:55	 Wizz Air 3255	L - - - V - -	OTP-DWC

Source: <https://www.google.ro/webhp?sourceid=chrome-instant&ion=1&espv=2&ie=UTF-8#q=bucuresti+dubai>

Figure 2. From Bucharest (OTP) to Dubai - United Arab Emirates direct flights

It is important to notice the fact that TAROM and Fly Dubai operates the flights to Dubai landing at Dubai International (DXB), the primary airport serving Dubai, United Arab Emirates, and Wizz Air operates the flights to Dubai landing at Al Maktoum International Airport (DWC), an international airport in Jebel Ali, 37 kilometers southwest of Dubai, United Arab Emirates.

Regarding the prices of a direct flight from Bucharest to Dubai and return, the Travel Commerce Platform–Travelport⁵ generated the following results using as filters pricing options (the lowest price) and itinerary options (no stopover): 383.82 euro with TAROM and 403.82 euro with Fly Dubai. As we can possible see in this special services request the departure was settled on 4 of June and the return on 11 of June and the flying time will be 5 hours and 40 minutes with TAROM and 5 hours and 15 minutes with Fly Dubai.

If we are using the same data for departure and return looking at the Fly Dubai official website⁶ we will pay 188 euro for the segment Bucharest- Dubai and 180 euro for the segment Dubai- Bucharest, a total of 368 euro (Inclusive of all taxes). A question arises? Why is it possible this difference between the prices generated with Travelport and Fly Dubai? Because of the special agreements signed by Fly Dubai with the GDS Travelport for the intermediation distribution, with a distribution cost around 30 euros. This distribution cost is integrated in the price generated with Travelport system. It is interesting to see these changes in prices depending of factors like: the type of flying (direct flight or flight with stopovers), the distribution channel (airline official website or the GDS portal), the moment when the ticket is bought (three months before or three days before), the landing point (the main airport or secondary airport), the airline seat, the economy or business class, and so on. These are the main reasons why the airline ticket price is not printed on it.

⁵ <https://www.travelport.com/>

⁶ <https://www.flydubai.com/en/>

A B C D E MYCONNECTION ON 39M3

APPLICATION TERMINAL HISTORY WINDOW PNR SEARCH SELL TOOLS HELP

1-FSBUH04JUNDXE +

>A

TTL OF 30 PRICING OPTIONS AND 105 ITINERARY OPTIONS RETURNED

FILTERS APPLIED

PRICING OPTION 1 TOTAL AMOUNT 383.82 EUR

ADT TAX INCLUDED

1 RO 67 T 04JUN OTP DXB 0810 1435 SA 73W TRTAE

FROM: HENRI COANDA ARPT, BUCHAREST

TO: DUBAI INTL ARPT, DUBAI

AIRLINE: TAROM-ROMANIAN AIR TRANSPORT

ARRIVES DXB TERMINAL 1

ELAPSED FLYING TIME: 05:25

2 RO 68 T 11JUN DXB OTP 1540 2020 SA 73W TRTAE

FROM: DUBAI INTL ARPT, DUBAI

TO: HENRI COANDA ARPT, BUCHAREST

AIRLINE: TAROM-ROMANIAN AIR TRANSPORT

DEPARTS DXB TERMINAL 1

ELAPSED FLYING TIME: 05:40

«BOOK» +TQ D R

PRICING OPTION 2 TOTAL AMOUNT 403.82 EUR

ADT TAX INCLUDED

1 FZ 798 M 04JUN OTP DXB 1415 2000 SA 737 MR1Y2R01

FROM: HENRI COANDA ARPT, BUCHAREST

TO: DUBAI INTL ARPT, DUBAI

AIRLINE: FLYDUBAI

ARRIVES DXB TERMINAL 2

ELAPSED FLYING TIME: 04:45

2 FZ 797 M 11JUN DXB OTP 0900 1315 SA 737 MR1Y2R01

FROM: DUBAI INTL ARPT, DUBAI

TO: HENRI COANDA ARPT, BUCHAREST

AIRLINE: FLYDUBAI

DEPARTS DXB TERMINAL 2

ELAPSED FLYING TIME: 05:15

«BOOK» +TQ D R

Source: Courtesy of Travelport

Figure 3. Searching direct flights from Bucharest-Dubai and return using global distribution systems (GDS)

Fly Dubai policy is all about low fares. Fly Dubai is dedicated to reduce the cost of air travel by decreasing operating costs. Important is the fact that the prices are all inclusive, with no extra charges or taxes added as “*With Fly Dubai’s fares, you only pay for the extras you choose*”. The Fly Dubai Company issue you with an electronic booking confirmation once your booking has been paid for.

✈️ 1. Bucharest (OTP) To Dubai (DXB)	✈️ 2. Dubai (DXB) To Bucharest (OTP)
Saturday 04 June 2016	Saturday 11 June 2016
Depart: 14:15	Depart: 09:00
Arrive: 20:00	Arrive: 13:15
Duration: 4hrs 45minutes	Duration: 5hrs 15minutes
Class of travel: Economy	Class of travel: Economy
Free to change fare ?	Free to change fare ?
Sector: EUR 188.00	Sector: EUR 180.00

Source: <https://flights.flydubai.com/en/passengers/new/>

Figure 4. Searching Bucharest- Dubai direct flight and return with Fly Dubai

Regarding the low cost company Wizz Air it is important to highlight that they are not integrated in the GDS because they consider not to be in their best interest to take part in these types of agreements.

Summary

Flight

lei858.00

Bucharest (OTP) →Dubai (DWC)

W6 3255 03/06/2016 15.05 - 20:55

1 adult

Fare

lei359.00

1 × Flight price

lei323.00

1 × Administration fee

lei36.00

Dubai (DWC) →Bucharest (OTP)

W6 3256 10/06/2016 21:30 - 01:50

1 adult

Fare

lei499.00

1 × Flight price

lei463.00

1 × Administration fee

lei36.00

Total in

EUR

€204.94

Source: <https://wizzair.com/en-GB/Passenger>

Figure 5. Searching Bucharest- Dubai direct flight and return with Wizz Air

Wizz Air considers their brand image recognition an important factor that allows them to sell through official website⁷.

⁷ <https://wizzair.com/ro-RO/FlightSearch>

Wizz Air is using preferential fares on their website in order to attract customers willing to land on a secondary airport and to pay additional costs of transfer. In the end, it is all about what customers need and want, and everyone has its place well established on the airline market. Searching Bucharest-Dubai direct flight and return with Wizz Air it can be notice the flying time, the departure and arrival points and the most important the total fare 204.94 euro.

In setting the fares for the airline tickets the low cost companies aimed primarily to cover all the fixed costs (like maintenance, crew, fuel, airport fees). The airlines do not print the price on the airline ticket because it depends of so many factors like the time of day when you choose to fly, the route, the number of seats left, the number of days' notice. So do not be surprised when you sit in the plane next to a passenger who paid 600 euro and you only paid 200 euro for the same flight.

In our quality of tourists we have the opportunity to decide when and with what company we want to fly. If we want to buy only the basic airline services or we need ancillaries' services and tailored offers. Nevertheless it is important to take into consideration if you want to do the trip on your own or consulting a travel agent. A travel agency can provide adequate counseling, manages overbooking problems, and provides personalized assistance through Romanian-speaking local guides. According to Sky Max Holiday Dubai⁸ it is in Romanian tourists best interest to work with travel agencies specialized in specific tourism destinations due to many reasons. First, travel agencies contract rates are much lower than the rates of online systems with at least 30-35%. Second, the travel agencies are able to sell accommodation with breakfast included in the price. Third there is that human contact between the travel agent and the tourist that provides a safety and security. Finally, the tourists are rescue from the stress of organizing the trip (regarding transportation, access facilities, transfer to and from the airport, accommodation, food and beverage, entertainment, visa formalities, currency exchange, insurance, sightseeing program, and so on).

5. Conclusions

Airline transportation is a particularly significant aspect of globalization. The expansion of globalization has been facilitated by technological development and advances. Particularly there has been a revolution in communications based on information technology and internet and a constant increase in the efficiency of transportation.

The airline fares depend on a multitude of factors like the level of competition and the route traffic density, the regularity of demand flow and the type of demand

⁸ <http://www.skymaxholidays.com/>

(business class and economy class), the estimated break-even load factor (the number of seats that must be sold to recover all fixed and variable costs).

The competition between the network carriers and low cost carriers permitted the transformations regarding the prices in the air transportation industry. All scheduled services operate on the basis of an advance reservations system, with the lowest fares being available on lines where the booking can be certified some time in advance of departure. These permit the airlines to assess its expected load factors with greater accuracy.

In the article are presented the implications of air transport liberalization over the airline companies' prices decrease. Intense competition in this market challenge airline companies to find solutions for cutting prices for airline flights.

The case study showed in the article wanted to highlight the Romanian tourists travel possibilities for Dubai tourism destination, comparing the prices of air tickets provided by three airlines Tarom, Fly Dubai and Wizz Air. If we take into consideration the direct flight Bucharest- Dubai and return at first look the lowest price is provided by the company Wizz Air. Then, we observe that the arrivals to and departures from Dubai are using an airport which is at a significant distance from Dubai and we have to take into account the costs of transfer that will occur. Low cost carriers Fly Dubai specialized in this travel destination is favorable if we purchase the airline tickets directly from their website because there we can benefit from the offers and buy at preferential fares. Also, Tarom comes with offers and service packages very attractive for Dubai.

In 2010, a round-trip with no stopovers, all fees included from Bucharest to Dubai was 650 euro, and in 2016 we have a round-trip with no stopovers, all fees included from Bucharest to Dubai at 220 euro. Matter-of-fact, in 6 years, from 2010 to 2016, the fare decrease with 450 euro in real terms, and with about 65% in percent.

The future of air transport will surprise us once again with the evolution of information and technology and will represent an important subject for further scientific research papers.

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<https://wizzair.com/ro-RO/FlightSearch>

<http://www.skymaxholidays.com/>