



## US Aviation Post-COVID-19: Scenarios and Implications – Installment 2 of 3



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# Context

This Is Not	This Is
<ul style="list-style-type: none"> <li>▪ <u>A quantitative exercise</u> based on rigorous analysis of data. There are no charts or graphs to prove any particular point</li> </ul>	<ul style="list-style-type: none"> <li>▪ <u>A qualitative exercise</u> based on               <ul style="list-style-type: none"> <li>▪ An understanding of what tends to happen in the aftermath of shocks</li> <li>▪ A broad assessment of reasonably-assumed economic and airline industry effects from COVID-19</li> <li>▪ Widely-reported decisions airlines have already made</li> </ul> </li> </ul>
<ul style="list-style-type: none"> <li>▪ A <u>prediction of “the” future</u>; a point-solution; a guide to or replacement for standard <u>strategic planning</u></li> </ul>	<ul style="list-style-type: none"> <li>▪ An aid to <u>scenario planning</u>, to begin to prepare and best position your organization for possible future states</li> </ul>
<ul style="list-style-type: none"> <li>▪ <u>A static assessment</u>; a once-and-for-all exercise</li> </ul>	<ul style="list-style-type: none"> <li>▪ <u>A fluid assessment</u>. As new information arises, we will reassess and revise our thinking and conclusions</li> </ul>

The best strategy tends to be the one that provides the most options and flexibility in the moment

# Definitions

*Note: Because our aviation expertise is US domestic, this material is intentionally US-centric [but we do possess passports]*

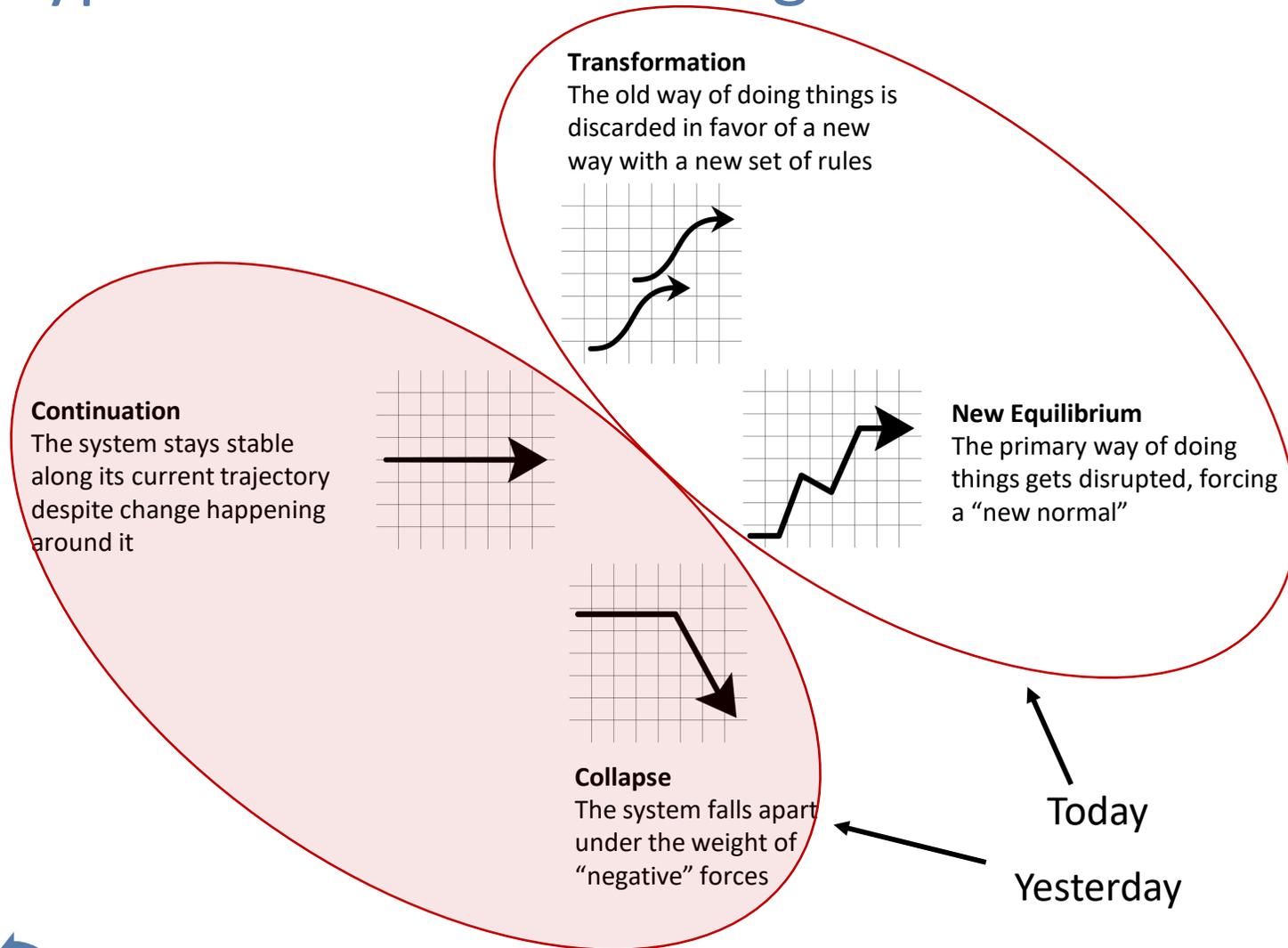
## **Terms already used in the industry:**

- Incumbent Carrier – Established National Carrier, Network Carrier, Regional Carrier, or Ultra Low Cost Carrier already flying at some meaningful scale
- National Carrier – Alaska, jetBlue, Southwest
- Network Carrier – American, Delta, United
- Regional Carrier – Airline flying aircraft of 75 or fewer seats, either:
  - Under the brand of a Network or National Carrier
  - Under its own brand
- Ultra Low Cost Carrier (ULCC) – Allegiant, Frontier, Spirit, Sun Country

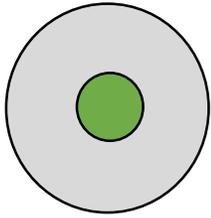
## **Terms we'd like to think we coined (but probably didn't):**

- Evolutionary Carrier – a Nascent Carrier that creates market share by acting much like an Incumbent Carrier with respect to aircraft type, layout, airport space use characteristics, and customer interface. Differentiates itself (or proposes to) based on some combination of market selection, pricing, and incremental product improvements
- Nascent Carrier – Non-Incumbent Carrier that fills (or intends to fill) a void in the marketplace and brings/keeps passengers in the national system who otherwise would choose alternatives to flying. Either:
  - Already flying but with relatively few aircraft and routes
  - Not yet FAA-certified. Proposed or, perhaps, still just a twinkle in someone's eye
- Revolutionary Carrier – a Nascent Carrier that creates a new market with a business model distinct from that of Incumbent Carriers. In addition to market selection and pricing, differentiates itself (or proposes to) based on some combination of radically different aircraft type, customer interaction, airport space use, product, technology, and overall experience

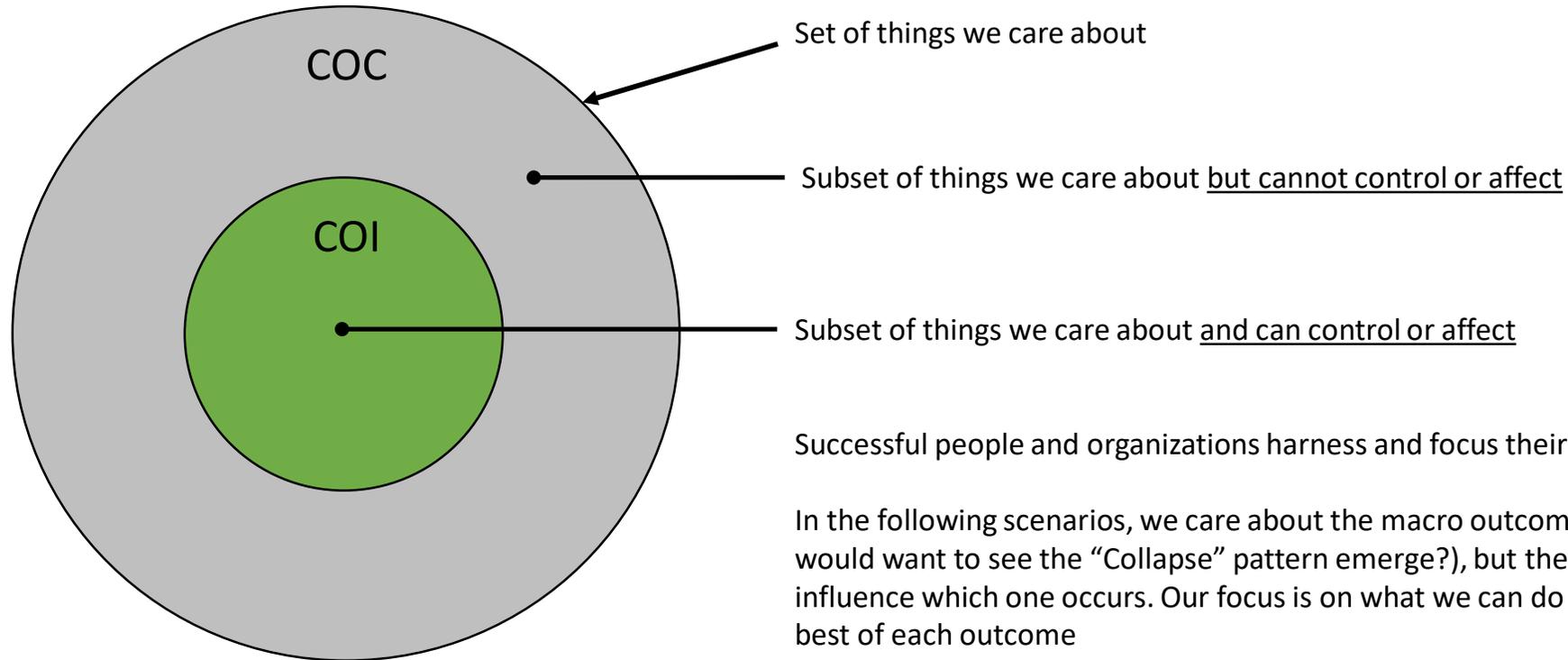
# Typical Patterns of Change



- These are patterns based on historical evidence
- No one knows at this point which path(s) our world, the US, or aviation will take after COVID-19
- Aspects of multiple paths may hybridize or succeed each other



# Circle of Concern (COC) vs. Circle of Influence (COI)



Concept adapted from Franklin/Covey



# New Equilibrium - Concept

The primary way of doing things gets disrupted, forcing a “new normal”

## Chaotic Beginnings

When a system begins to experiencing this “outside change”, the first reaction is usually very chaotic. People don’t know how to react, making the outcome uncertain

## New Stability

If a system undergoes the New Equilibrium Pattern, there is disruption which usually reveals vulnerability in the system. This instability brings opportunities for profit and innovation, for building resilience, and for self-evaluation



## Examples

### Post 9/11 Airport Security

After the 9/11 attacks, there was a time of great instability in the airport industry. Systems began changing rapidly and asynchronously. New technologies and products came to market, new jobs created and many profited. Now, nearly 20 years later, global airport security measures have fundamentally shifted but have mostly settled into a new, stable rhythm

### Tylenol Tampering

After several instances of medication tampering, some thought we would never be able to trust medicine on the shelves. However, the advent of tamper-proof or tamper-evident seals restored consumer confidence in off-the-shelf medication



# New Equilibrium - Applied to US Aviation

The primary way of doing things gets disrupted, forcing a “new normal” [Assessed probability: moderate and rising]

## What You Would Have To Believe

- Disease follows expected path
- Substantially clarity about forward economic trajectory by, say, June 30, 2020
- Social distancing to some degree as the new norm
- Short term demand recovery to, say, 60% of previous levels
  - A significant reduction, but...
  - ...Not to point of system collapse
  - Unevenly experienced based on how well (or poorly) airlines and airports adapt and communicate



## Implications - Airlines

- Most Incumbent Carriers stabilize at the smaller base and then flex with GDP. Some cease to exist. Regional partners of Network Carriers hit especially hard
- Discretionary/lower income demand substantially rejected by Network Carriers
- Passengers resist return to crowded seating layouts
- Unit costs increase, and revenues from prior sources decrease
- Stable ULCCs and Evolutionary Carriers vie to backfill secondary and point-to-point markets and retain passengers in the commercial aviation system who would otherwise choose alternatives. Stable National Carriers may play in this space also. If no carriers are successful...
- ...Possible airline re-regulation



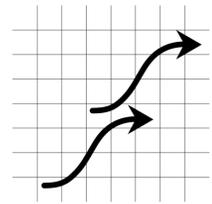
# New Equilibrium - Applied to US Aviation

The primary way of doing things gets disrupted, forcing a “new normal” [Assessed probability: moderate and rising]

## Implications - Airports

- Substantially all airports lose some service long-term
  - Strategic markets & some hubs fare a little better, though some hubs will lose that status
  - Smaller and non-strategic markets fare worse to varying degrees. Substantial risk to
    - RJ-only airports
    - Ultra-short-haul city pairs
- Fear of crowds and international traffic subsides but not completely
  - Passenger preference for smaller domestic airports and less crowded hubs when feasible
  - Opportunity for new commercial airports if adjacent to strong airline demographic areas or able to drive destination demand
  - Unit costs increase
  - Airline and non-aeronautical revenues decrease
  - Airport cost per passenger to airlines increases
  - Evolutionary Carriers use facilities much as incumbent carriers do
  - Passengers expect, possibly demand, rigorous health measures
    - Real-time symptom check and location tracking to backtrack exposures, linked to traveler profile with visual and/or computer-scannable code at Security and Boarding to confirm eligibility to fly
    - Increased cleaning of airports’ public spaces and airplanes via more aggressive use of chemical methods. Purell dispensers everywhere, if you can keep them
    - Greater space bubbles inside airports (holdrooms and concessions spaces in particular)





# Transformation - Concept

The old way of doing things is discarded in favor of a new way with a new set of rules

## Transformational Innovation

Often transformation happens when a new process or technology allows people to do things through a better medium. This intersection of a timeless need and new solution can force transformation within a system

## The Former Things Recede

The PRIMARY difference between a Transformation Pattern and the New Equilibrium is that New Equilibrium keeps the same basic structures or systems intact, while Transformation forces the former system to go away, moving from mainstream to niche and artisanal



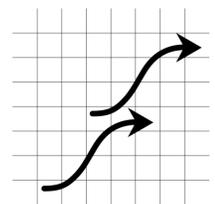
## Examples

### Digital Communications and the Internet

For much of human history, long-distance communication was accomplished by hand crafted letters delivered by people. With the invention of the Internet, communication can happen to nearly any part of the globe, nearly instantaneously. Letter writing has become novel, when it used to be mainstream

### Horseless Buggy

Henry Ford famously said, “if I’d asked the public what they wanted, they would have asked for a faster horse.” The automobile has fully transformed transportation, city planning, logistics, and trade. Horse riding has moved to a niche hobby



# Transformation - Applied to Aviation

The old way of doing things is discarded in favor of a new way with a new set of rules [Assessed probability: moderate and rising]

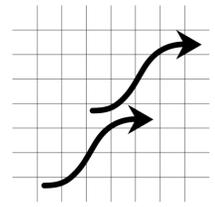
**What You Would Have To Believe [Substantially similar to “New Equilibrium” except where highlighted]**

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## Implications - Airlines

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- Discretionary/lower income demand substantially rejected by Network Carriers
- Passengers resist return to crowded seating layouts
- Unit costs increase, and revenues from prior sources decrease
- **Revolutionary Carriers** create new models to retain passengers in the commercial aviation system who would otherwise choose alternatives. If they are not successful...
- ...Possible airline re-regulation



# Transformation - Applied to Aviation

The old way of doing things is discarded in favor of a new way with a new set of rules [Assessed probability: moderate and rising]

## Implications – Airports [Substantially similar to “New Equilibrium” except where highlighted]

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  - Airport cost per passenger to airlines increases
  - **Revolutionary Carriers use facilities completely differently from how Incumbent Carriers do**
  - Passengers expect, possibly demand, rigorous health measures
    - Real-time symptom check and location tracking to backtrack exposures, linked to traveler profile with visual and/or computer-scannable code at Security and Boarding to confirm eligibility to fly
    - **Disinfection of airports’ public and offices spaces with proven, medical-grade, non-chemical technology**
    - Greater space bubbles inside airports (holdrooms and concessions spaces in particular)



# To Be Continued April 9

- April 9 – Installment 3 of 3: The most likely scenario and how to prepare for it starting right now

# About



We're an aviation management consulting firm focusing on helping our clients drive customer demand for their brands. We provide commercial and marketing strategy, organizational health, facilities strategy, and airline/airport relationship consulting to airports and airlines

Based on two decades in commercial, marketing, and airports leadership positions at Southwest Airlines, and then over eight years of management consulting, Sky Synergy developed and applies NextGenASD<sup>(SM)</sup>, a methodology that identifies and then addresses the root issues that can stand in the way of airline growth at an airport

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We're marketing and research professionals with a passion for helping companies understand their customers' motivation and preferences at a deeper level, now and in the future

**OUR APPROACH IS BASED UPON THREE GUIDING PRINCIPLES:  
HINDSIGHT, INSIGHT AND FORESIGHT**

This helps us paint a complete picture of your business - where it started, where it is now, and where it's headed.

**Hindsight** establishes historical context and understanding of the field;

**Insight** illuminates consumer trends and key ideas;

**Foresight** prepares our partners to react to changes in the ever-evolving market.

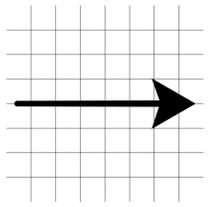
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# Appendix

Slides from Part 1





# Continuation - Concept

The system stays stable along its current trajectory despite change happening around it

## Often Called the “No Change” Future

This future speculates what would happen if outside change did not affect it

## Least Likely Option

Because change is always happening around us, the Continuation Pattern is usually the least likely scenario

## Comfortable but Unreliable Plans

Strategic plans based on the Continuation Pattern are very comforting because we believe what happened yesterday will happen today and tomorrow. However, plans that assume nothing will change can be blindsided when change almost inevitably occurs



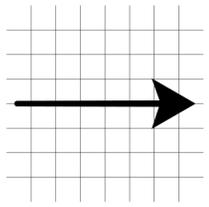
## Examples

### Spiritual Rituals

Many of the major world religions have practices and rituals (prayer, washing, holidays and festivals, etc.) that remain basically the same despite changes around them

### Trading Time for Money

For most people in developed economies, those of the working class spend much of their lives trading time for money. The *type* of work may be changing, but the system of trading time for money has not



# Continuation – Applied to US Aviation

The system stays stable along its current trajectory despite change happening around it [Assessed probability: low and dwindling]

## What You Would Have To Believe

- Economic and industry disruption are short-lived, based on
  - Any of the following
    - COVID-19 cure and vaccine in mass use in a matter of weeks; or
    - Disease shown to be far less contagious and deadly than Italy and NYC headlines made it seem; or
    - Governments adopt, and people accept, a “damn the torpedoes” mantra prioritizing economic health over personal health
  - AND public assesses low risk of follow-on pandemic
- Passenger demand and airline capacity recover quickly, à la post-9/11, to 90% pre-COVID-19
- People haven’t already come to prefer their customized Zoom backgrounds to face-to-face interaction



## Implications

- US aviation industry looks substantially similar to, but slightly smaller than, pre-COVID-19
  - Some larger planes (e.g., A380s, 767s) and regional airlines take a disproportional hit
  - Some planned, seasonal reductions in airlines’ future schedules at typical flu season peaks
- Airport facilities and airlines’ fleets see lower utilization, but not to the point of significant business model change
- Scaled-down business as usual for the most part at some point in 2020
- Labor force reductions accomplished without permanent layoffs by early retirement packages and generous time-off-without-pay options
- Everyone breathes a sigh of relief (but not on anybody)
- Ramping back up will bring staffing, equipment, and facility challenges of its own



# Collapse - Concept

The system falls apart under the weight of negative or opposing forces

## Bursting the Bubble

Though not always, the Collapse Pattern can often happen suddenly, causing major system breakdowns. Usually this sudden crash happens when people are assuming the Continuation Pattern and ignoring early signs of Collapse

## Not Always a Bad Thing

It is easy to think of this pattern as always negative, but it is important to remember that there are times when the Collapse Pattern is a best-case scenario, like when unjust political systems implode, or a concerted effort contains and eradicates a disease like smallpox



## Examples

### Falls of the Third Reich and of the Soviet Union

Both collapses led to greater individual freedom and less persecution (though Russia still a work in progress with uncertain outcome)

### Collapse of Film Cameras

The digital camera was initially invented by Kodak, but because it was expensive to use for storing images, it was initially shelved. By 2002, miniaturization and other technologies had already put small cameras in phones, not only collapsing the film camera industry but also digital point-and-shoot devices

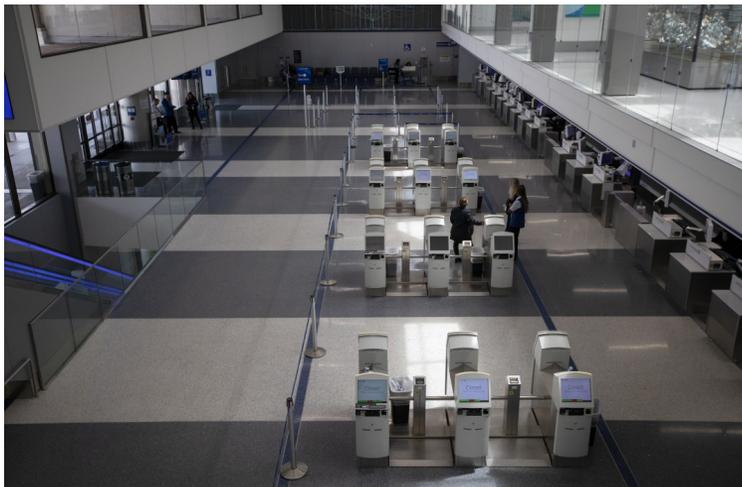


# Collapse - Applied to US Aviation

The system falls apart under the weight of negative or opposing forces [Assessed probability: low but rising]

## What You Would Have To Believe

- Significant and prolonged economic disruption from
  - Longer than expected duration of COVID-19 and social distancing measures
  - Higher end estimates of transmission rates and/or mortality rates are realized
  - COVID-19 runs its course as expected, but implacable fears remain or repeated pandemics occur
- Government, industry, and individual efforts to reduce fear and attract passengers back are impractical or ineffective
- Airline forward bookings for post-Labor Day remain at a fraction of pre-COVID-19 levels



## Implications

- Virtual meetings and staycations assume dominant position, supplanting physical presence
- Most airports lose significant service. Airlines radically consolidate hubs
- Mass airport and airline extinction; permanent idling of associated people and assets
- Remaining airports find it more difficult to issue debt after defaults elsewhere. Cost of borrowing (interest rates and/or reserve requirements) increases
  - An optimist might point out the low likelihood, in this scenario, of airports' having to bond much anytime soon anyway; but that wouldn't exactly make him suddenly popular
- Prospective airlines can't raise capital, hire laid off employees, or redeploy fallow assets
- Almost-certain airline re-regulation
- Remaining airlines and airports focus on improving interaction and connection with remaining passengers and employees
- Innovative airports discover ways to profit from alternate uses of fallow facilities and land