SkyWest External and Internal Assessment Report
U.S. Regional Airline Industry
U.S. REGIONAL AIRLINE INDUSTRY - EXTERNAL ANALYSIS

1) PESTEL Analysis:
   a. Political Factors
      • Sept. 11 terrorist attacks increased fear of flying and decreased revenue for majors
      • Foreign expansion restricted by the 49% ownership limits placed on US carriers
   b. Economic Conditions
      • 2008-09 Recession caused consumers to cut down on discretionary spending
      • IATA noted that weak travel markets caused by recession typically lasted 3 years, thus travel was not expected to grow more than 4% until 2011
      • Recession’s strong impact on credit, making it hard for airlines to acquire new aircraft
      • Increasing fuel cost caused financial troubles for major airlines, fuel made up 10-20% of overall airline cost in 2008 and 35-40% in 2009
   c. Sociocultural Forces
      • Airline employees represented by labour unions - acrimonious relationship between labour unions and airlines leading to strikes and huge financial losses
      • Airplane travel considered discretionary spending for leisure and business customers
   d. Technological Factors
      • Introduction of faster, more efficient commuter jets expand regionals service areas
   e. Environmental Factors
      • Seasonal fluctuations – increased travel during summer months, while cancellations and delays during the winter months primarily due to weather
      • Regional carriers limited geographically to one region, mostly affected by bad weather, and routinely cancelled to make room on the runway for majors
   f. Legal/Regulatory Factors
      • Post 9/11 – FFA, TSA, DOT increased government intervention by increasing security regulations, which led to additional costs for the airlines
      • Dept. of Transportation’s regulation to provide oxygen for passengers estimated to cost between $262m and $577m to airline industries for over 10 years

Summary: The analysis provides a broad perspective of factors that drive the airline industry. Airlines are widely impacted by regulations and restrictions related to international trade, tax policy, ownership limits from foreign governments and environmental issues like war and terrorism. Regulatory and political factors also drive changes in economic conditions like surges in fuel prices and affect sociocultural conditions creating volatility between labour unions airlines.

2) Dominant Economic Features Analysis
   a. Market Size and Growth Rate
      • Airline carriers divided into 3 types: network, low-cost, and regional - each operated under different business models
      • IATA predicted revenues of worldwide passenger traffic falls by 3% to $394B from $425B (2008), cargo revenues fall to $54B from $59B
   b. Number of Buyers
      • IATA – worldwide passenger would fall by 3% to $394B from $425B in 2008
      • Regionals’ passengers historically business travelers
      • 95% of regional airlines revenues from contracted fees per departure with majors
c. **Buyer Needs and Requirements**
- Travel by both leisure and business travelers were considered discretionary
- Increasing concern for safety after terrorist attacks
- Increasing number of business travelers using low-cost carriers resulting in major airlines’ market share drop of 60% while a 20% increase for low-cost carriers

d. **Number of Rivals**
- Top 5 major airline competitors: United, U.S. Airways, American, Continental and Delta-Northwest (Delta and Northwest merged)
- Top 5 Independently owned regional carriers: SkyWest, Mesa Air Group, Republic Airways, ExpressJet, Pinnacle Airlines
- Low-cost: Southwest, JetBlue, Ted (United) and Song (Delta)

e. **Scope of Competitive Rivalry**
- Increased mergers meant limited growth/partnership opportunities for regionals
- Low cost carriers increased in market share (20%) among business travelers

f. **Product Innovation**
- Bombardier turboprop and regional jets allow regional carriers to operate more efficiently and provides better comfort to passengers
- Regional airline growth attributed to development of smaller regional jets that could be flown on routes that majors had previously serviced

g. **Product Capacity**
- Planes are required to operate under capacity, increasing cost per passenger

h. **Pace of Technological Change**
- “Hub-and-spoke system used by Network Carriers operated large portion of flights
- “Point-to-point” flights used by low-cost carriers

i. **Vertical Integration**
- Major carriers’ low-cost lines flying routes traditionally contracted to regionals (United’s Ted & Delta’s Song)
- Regional carriers acquiring major carriers to expand operations and increase revenue stream (ie. Republic Airways Holdings acquisition of majors – Frontier and Midwest)

j. **Economies of Scale**
- Regional subsidiaries operated separately, but combined functions in finance, treasury, IT and admin to realize economies (ie. SkyWest and ASA)

**Summary:** A notable feature derived from the analysis is the level of competitiveness that low-cost carriers bring within the airline industry. This factor has influenced buyers’ needs and requirements and increased the demand for low-cost carriers by 20%, and dropped business market share for other competitors by 60%. In response, network and regional carriers re-strategized to also incorporate low-cost lines within their business function.

3) **Porter’s 5F Analysis**

a. **New Entrants (Moderate)**
- Major carriers responded to loss of revenues from low-cost competitors by starting their own low-cost airlines (United’s Ted & Delta’s Song)

b. **Threat of Substitute Products or Services (Insufficient Information)**

c. **Bargaining Power of Customers (High)**
- Increasing number of business travelers began to travel on low-cost carriers. As a result, major airlines’ market share dropped to 60% while low-cost increased by 20%
- Business and leisure travels are highly discretionary
• Airlines still obligated to operate partially loaded flights

d. Bargaining Power of Suppliers (High)
• Fuel costs made up 35-50% of an airline's operating costs
• 95% of regional airlines’ business is supplied by major carriers
• Pressure on major carriers to cut costs forces regional partners to accept lower fees
• Regional airlines must maintain high levels of customer service to partner with majors
• 40% of airline’s expense comprised pay for airline workers/professionals

e. Intensity of Competitive Rivalry (High)
• Fierce competition among regionals and low-cost carriers for partnership with majors
• New routes being offered are often bid out by major carriers
• Increased mergers meant limited growth/partnership opportunities for regionals
• Major carriers decide distribution of routes and have preference toward subsidiaries

Summary: The airline industry is a competitively unattractive industry, and is not a conducive industry to earn good profits. First, fierce rivalry among regional carriers exists as several regional carriers vie for partnership with only a few major airlines. Regional carriers also have little control over revenue growth since major carriers primarily supply their business. Lastly, rising fuel cost, suppliers and consumers have considerable leverage and greatly impact a company’s ability to grow in revenue.

4) Driving Forces Analysis

a. Changes in an industry’s long-term growth rate
• IATA worldwide passenger traffic fall by 3% ($425bn to $394bn) for 2008
• Post 9/11 incidents translated to fear of flying causing revenues to decline for majors
• Demand is declining - business customers decreased by 60%
• Travel markets not expected to revert back to pre-recession numbers until 2011
• Consolidations of majors limit regionals’ growth opportunities

b. Regulatory influences and government policy changes
• Post 9/11 incidents resulted in increased security, adding additional cost to airlines
• Legislation requiring carriers to provide oxygen for passengers increase regional airlines costs by between $262m - $577m (Air Carrier Act, 1986)
• Airline employees represented by labour unions - acrimonious relationship between labour unions and airlines leading to strikes and huge financial losses

c. Changes in Cost and Efficiency
• Fuel costs, 10-20% of airline costs in 2008, changed to 35-50% in 2009
• Pressure for majors to cut costs forces regional partners to accept lower fees
• Increased travel during summer months while decreased flights during the winter

Summary: Change in an industry’s long-term growth rate, regulatory policies and changes in cost and efficiency are the key drivers that affect the airline industry’s level of attractiveness and competitive condition. Factors such as the recent recession and post terrorist attacks have decreased the overall demand for airline services making it a highly competitive industry. Mandatory regulations (ie. scope clause, increased security, etc.) and rising fuel costs increased operational costs for industry players thereby weakening their ability to maximize profit.
5) Strategic Group Map Analysis:

Summary: The strategic group map shows that in 2008, amongst five largest independently owned regional airlines, SkyWest is ahead of its competitors in terms of market share, geographical scope, and quality. Geographical scope is defined by the total number of cities flown, and quality is assessed according to market data that compares percentage of on-time flights, number of mishandled baggage reports, denied boarding due to oversold flights, and total number of passenger complaints.

6) Framework for Competitor Analysis:

<table>
<thead>
<tr>
<th>Key Success Factor/Strength measure</th>
<th>SKY WEST, INC</th>
<th>Mesa Air Group</th>
<th>Republic Airway Holdings</th>
<th>Expressjet Holdings</th>
<th>Pinnacle Airlines Corp</th>
</tr>
</thead>
<tbody>
<tr>
<td>Customer Service</td>
<td>0.2</td>
<td>9</td>
<td>1.8</td>
<td>7</td>
<td>1.4</td>
</tr>
<tr>
<td>Safety (accidents)</td>
<td>0.2</td>
<td>10</td>
<td>2</td>
<td>8</td>
<td>1.6</td>
</tr>
<tr>
<td>Operational efficiency/Timeliness</td>
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<td>8</td>
<td>0.8</td>
<td>7</td>
<td>0.7</td>
</tr>
<tr>
<td>Strategic Partnership with major</td>
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<td>6</td>
<td>1.2</td>
<td>9</td>
<td>1.8</td>
</tr>
<tr>
<td>Range of Operations (geographical)</td>
<td>0.1</td>
<td>7</td>
<td>0.7</td>
<td>8</td>
<td>0.8</td>
</tr>
<tr>
<td>Financial Management</td>
<td>0.1</td>
<td>7</td>
<td>0.7</td>
<td>6</td>
<td>0.6</td>
</tr>
<tr>
<td>Employer/Employee Relationship</td>
<td>0.2</td>
<td>9</td>
<td>1.8</td>
<td>6</td>
<td>1.2</td>
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<td>Cost Differentiation</td>
<td>0.2</td>
<td>6</td>
<td>1.2</td>
<td>8</td>
<td>1.6</td>
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<tr>
<td>Overall weighted competitive strength rating</td>
<td>1</td>
<td>10.2</td>
<td>9.7</td>
<td>10</td>
<td>9</td>
</tr>
</tbody>
</table>

Rating Scale (1=Very Weak, 10=Very Strong)

Summary: The best performing company within the regional airline industry was SkyWest Inc. SkyWest has a strong customer service, good reputation for safety and harmonious relationships with employees. Pinnacle Airlines Corp. had the lowest score due to their unsafe practices that killed 49 people in 2009. Republic Airway Holdings followed SkyWest with an overall score consisted of an average score for their strength ratings. Lastly, ExpressJet and Mesa Air Groups scored lower as they both had bad financial management scores.

7) KSF Analysis:

a. Customer service
   - Regional airlines must maintain high levels of customer service to partner with majors
   - The Complaints per 100,000 passengers boarded per year varied within the competitors and reflected on the regional airlines’ customer service

b. Cost Differentiation
   - Business travellers choosing to travel on low-cost carriers - business market share for major carriers dropped to 60% while low-cost carriers increased by 20%
c. Strategic Partnership/Alliances
• Regional Airlines mainly operated through partnerships with the major airlines
• Major Airlines rolled back operations and outsourced more of their routes to the regional airlines, which gave regional airlines a larger market share
d. Safety (accidents)
• 9/11 attacks on US decreased demand for airline services in 2000
• Regional airlines perceived as less safe because they used smaller planes
e. Operational efficiency/Timeliness
• Four of the worst on-time records for bumping customers held by regionals carriers
• Regionals notorious for worst carriers in baggage handling and flight cancellation
f. Range of operations (geographical)
• Regional Airlines were limited geographically to one region
g. Financial management/Cost management (low operational costs)
• High operational cost from rising fuel cost (35% to 50%) and mandatory legislation ($2M and $5M over 10 years) - realizing economies of scale becomes important
• Pressure on major carriers to cut costs forced regional partners to accept lower fees
• Bankruptcy filings of major carriers may risk regional partners to also follow suit
h. Employer-Employee relationship
• Most airlines are represented by labour unions; acrimonious relationship with employees/ions lead to strike and huge financial losses for airlines

Summary: Distinguished key success factors are customer service, cost differentiation and strategic partnership alliance. Excellent customer service places regional carriers in a better position for partnership with major carriers. It also opens up opportunities for repeat business among clients. Cost differentiation is important since flights are considered discretionary spending. Lastly, strategic partnership is key within the regional industry because network partners are the primary supplier of business for regional airlines.

8) Overall Summary Conclusions of Relevant Findings:
• Macro-environmental conditions incur huge losses form major carries, recession, terrorist attacks, overexpansion, bloated flight schedules, high fuel cost, low-cost carrier pressure
• IATA – worldwide passenger would fall by 3% to $394B from $425B by 2008
• 95% of regional airlines revenues from contracted fees per departure with majors
• Business travelers are flying low-cost, resulting in a decrease of 60% business market share for major carriers and 20% increase for low-cost airlines
• Airline employees represented by labour unions - acrimonious relationship between labour unions and airlines can lead to strikes and huge financial losses
• Travel considered discretionary; discretionary spending minimized due to recession
• Fear of flying from recent terrorist attacks; increased security rise in operational cost
• Rising operational cost from fuel costing airline up to 35-50% of operating costs; legislations (ie. Air Carrier Act, 1986) costing airlines between $262M - $577M
• Mergers threaten regionals’ growth opportunities – route options are minimized
• Regional airlines subject to a number of operating constraints and are fared poorly in Airline Quality Report for problems caused by major carriers
• SkyWest’s reputation of being well-run enabled them to enjoy respectable profits even when other competitors produced flat earnings; they also successfully revived ASA
### SKYWEST INC. – INTERNAL ANALYSIS

#### Percentage of Scheduled Flights Arriving on Time

<table>
<thead>
<tr>
<th>Carrier</th>
<th>AVG</th>
<th>CAGR</th>
</tr>
</thead>
<tbody>
<tr>
<td>American Eagle</td>
<td>73.4%</td>
<td>24%</td>
</tr>
<tr>
<td>Atlantic Southwest</td>
<td>70.6%</td>
<td>-1.73%</td>
</tr>
<tr>
<td>Comair</td>
<td>72.2%</td>
<td>-3.20%</td>
</tr>
<tr>
<td>Express Jet</td>
<td>76.4%</td>
<td>37%</td>
</tr>
<tr>
<td>Mesa</td>
<td>76.1%</td>
<td>1.07%</td>
</tr>
<tr>
<td>Pinnacle</td>
<td>80.9%</td>
<td>7.65%</td>
</tr>
<tr>
<td>SkyWest</td>
<td>81.2%</td>
<td>29%</td>
</tr>
<tr>
<td>Industry</td>
<td>75.8%</td>
<td>13%</td>
</tr>
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</table>

#### Mishandled Baggage Reports per 1,000 Passenger

<table>
<thead>
<tr>
<th>Carrier</th>
<th>2004</th>
<th>2005</th>
<th>2006</th>
<th>2007</th>
<th>2008</th>
<th>2009</th>
<th>AVG</th>
<th>CAGR</th>
</tr>
</thead>
<tbody>
<tr>
<td>American Eagle</td>
<td>8.38</td>
<td>7.89</td>
<td>12.51</td>
<td>11.6</td>
<td>9.06</td>
<td>7.44</td>
<td>9.48</td>
<td>-1.96%</td>
</tr>
<tr>
<td>Atlantic Southwest</td>
<td>10.94</td>
<td>14.5</td>
<td>11.33</td>
<td>7.74</td>
<td>5.81</td>
<td>6.24</td>
<td>9.43</td>
<td>-8.93%</td>
</tr>
<tr>
<td>Comair</td>
<td>8.89</td>
<td>8.37</td>
<td>7.73</td>
<td>8.84</td>
<td>5.86</td>
<td>4.63</td>
<td>7.39</td>
<td>-10.30%</td>
</tr>
<tr>
<td>Express Jet</td>
<td>5.45</td>
<td>5.1</td>
<td>7.15</td>
<td>7.46</td>
<td>5.52</td>
<td>2.86</td>
<td>5.59</td>
<td>-10.19%</td>
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<tr>
<td>Mesa</td>
<td>n/a</td>
<td>n/a</td>
<td>7.92</td>
<td>9.95</td>
<td>7.61</td>
<td>4.32</td>
<td>7.45</td>
<td>-14.06%</td>
</tr>
<tr>
<td>Pinnacle</td>
<td>n/a</td>
<td>n/a</td>
<td>n/a</td>
<td>6.3</td>
<td>4.87</td>
<td>4.53</td>
<td>5.23</td>
<td>-10.41%</td>
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<tr>
<td>SkyWest</td>
<td>7.94</td>
<td>8.11</td>
<td>6.85</td>
<td>9.21</td>
<td>5.76</td>
<td>4.92</td>
<td>7.13</td>
<td>-7.67%</td>
</tr>
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#### Involuntary Denied Boardings per 100,000 Passengers due to Oversold Flights

<table>
<thead>
<tr>
<th>Carrier</th>
<th>2004</th>
<th>2005</th>
<th>2006</th>
<th>2007</th>
<th>2008</th>
<th>2009</th>
<th>AVG</th>
<th>CAGR</th>
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<tbody>
<tr>
<td>American Eagle</td>
<td>0.38</td>
<td>0.79</td>
<td>2.15</td>
<td>1.19</td>
<td>2.79</td>
<td>3.14</td>
<td>1.74</td>
<td>42.2%</td>
</tr>
<tr>
<td>Atlantic Southwest</td>
<td>3.2</td>
<td>2.68</td>
<td>6.89</td>
<td>5.43</td>
<td>5.22</td>
<td>3.94</td>
<td>4.56</td>
<td>3.5%</td>
</tr>
<tr>
<td>Comair</td>
<td>4.58</td>
<td>1.08</td>
<td>2.97</td>
<td>3.32</td>
<td>4.48</td>
<td>3.17</td>
<td>3.27</td>
<td>-5.9%</td>
</tr>
<tr>
<td>Express Jet</td>
<td>n/a</td>
<td>n/a</td>
<td>n/a</td>
<td>n/a</td>
<td>n/a</td>
<td>2.39</td>
<td>2.39</td>
<td>0.0%</td>
</tr>
<tr>
<td>Mesa</td>
<td>n/a</td>
<td>n/a</td>
<td>1.7</td>
<td>1.94</td>
<td>1.19</td>
<td>1.21</td>
<td>1.51</td>
<td>-8.1%</td>
</tr>
<tr>
<td>Pinnacle</td>
<td>n/a</td>
<td>n/a</td>
<td>n/a</td>
<td>n/a</td>
<td>4.71</td>
<td>1.6</td>
<td>3.16</td>
<td>-41.7%</td>
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<tr>
<td>SkyWest</td>
<td>0</td>
<td>0.7</td>
<td>1.26</td>
<td>2.73</td>
<td>2.02</td>
<td>1.57</td>
<td>1.38</td>
<td>17.5%</td>
</tr>
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</table>

#### Complaints per 100,000 Passengers Boarded (In May of Each Year)

<table>
<thead>
<tr>
<th>Carrier</th>
<th>2004</th>
<th>2005</th>
<th>2006</th>
<th>2007</th>
<th>2008</th>
<th>2009</th>
<th>AVG</th>
<th>CAGR</th>
</tr>
</thead>
<tbody>
<tr>
<td>American Eagle</td>
<td>0.48</td>
<td>0.32</td>
<td>0.88</td>
<td>1.26</td>
<td>0.39</td>
<td>0.71</td>
<td>0.67</td>
<td>6.74%</td>
</tr>
<tr>
<td>Atlantic Southwest</td>
<td>0.23</td>
<td>0.28</td>
<td>0.95</td>
<td>0.57</td>
<td>0.27</td>
<td>0.52</td>
<td>0.47</td>
<td>14.56%</td>
</tr>
<tr>
<td>Comair</td>
<td>0.36</td>
<td>0.26</td>
<td>0</td>
<td>1.22</td>
<td>0.56</td>
<td>0.96</td>
<td>0.56</td>
<td>17.76%</td>
</tr>
<tr>
<td>Express Jet</td>
<td>0</td>
<td>0.3</td>
<td>0.31</td>
<td>1.22</td>
<td>0.56</td>
<td>0.96</td>
<td>0.56</td>
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</tr>
<tr>
<td>Mesa</td>
<td>n/a</td>
<td>n/a</td>
<td>0.69</td>
<td>0.58</td>
<td>0.6</td>
<td>0.63</td>
<td>0.63</td>
<td>-2.25%</td>
</tr>
<tr>
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<td>n/a</td>
<td>n/a</td>
<td>0.91</td>
<td>0.97</td>
<td>0.33</td>
<td>0.74</td>
<td>-28.69%</td>
</tr>
<tr>
<td>SkyWest</td>
<td>0.39</td>
<td>0.36</td>
<td>0.36</td>
<td>0.63</td>
<td>0.28</td>
<td>0.57</td>
<td>0.43</td>
<td>6.53%</td>
</tr>
</tbody>
</table>
1) Financial Analysis

- Revenues grew at CAGR 25% from 2004-08, due to the acquisition of ASA; Growth rate between 2007-08 is 3.49%; Revenue per seat mile increased 8.2% between 2007-08
- Cost per seat mile increased 10.9% between 2007-08, attributed to rising fuel costs and possibly contract dispute with Delta
- Fuel cost per seat mile at all time high of 7.1 cents (2008), Fuel costs, which is over a third of SkyWest’s costs, increased 19.6% between 2007-08
- Net income retracted by -29.06% between 2007-08 -- net income was reset back to years before ASA acquisition (please confirm)
- Operating profit margin dropped every year; biggest drop occurred between 2007-08 from 10.21% to 7.3%
- Gross profit margins growth started to slow down in 2007 and decreased by 35% in 2008 after increases of 34% and 25% in 2005 and 2006, respectively
- Average passenger load factor from 2004-08 is 76.48%; breakeven load factor has been increasing at 2.58% every year - 74.4% in 2008, resulting in a 3.23% net margin
- The number of passengers riding independent regional airlines has increased steadily from 2008-2004, with a CAGR of 15.43%
- The acquisition of ASA in 2005 increased SkyWest market share due to the expansion of operations of (how much in terms of passengers and flights)
- Accumulated depreciation and amortization is $824M in 2008, indicating that planes are getting older and some may need to be replaced
- All debt ratios have improved between 2007-08
- 2004-09: On time arrivals of 81.2% is higher than industry average of 75.8%; Mishandled baggage reports is 7.13 per 1,000 passengers, lower than industry average of 7.39; Denied boarding due to oversold flights is 1.38 per 10,000 passengers, lower than industry average of 2.57; Complaints is 0.43 per 100,000 passengers, compared to industry average of 0.58 (business/function-customer service)

Conclusion

Overall, SkyWest’s financials are pretty strong. The regional airline industry is growing at a rapid rate, which has resulted in constant growth over the past 4 years. The acquisition of ASA resulted in a major revenue increase in 2005. SkyWest’s ability to successfully manage regional airline metrics such as on-time arrivals, mishandled baggage, customer complaints and denied access by overbooking has been an important factor to their success. There are concerns over SkyWest’s 2008 financial reports as the operating margin dropped by roughly 3%. This can be attributed to the increase of expenses, most notably fuel costs. Having said that, SkyWest is in a leading role in the regional airline industry.
2) SkyWest Inc.’s Strategy

a. Vision
- To give consumers access to the connection to flights of major partners in a reliable, efficient manner

b. Mission
- To provide quality and timely customer service and maintain a reputation as the #1 Regional Airline in the industry
- To provide clients, employees with a safe flying experience by implementing training programs (Aviation Safety Action), technologies (Stetston Quality Suite) that would mitigate potential safety hazards

c. Business/Functional Strategy

Customer service
- High level of customer service is SkyWest’s differentiation strategy
- SkyWest Inc. beat American Eagle (subsidiary of AA) as #1 Regional Airline (2006)
- SkyWest: number one on-time Airline by DOT; 2nd fewest involuntary denied boarding; 4th regional airlines; complaints per 100,000 passengers
- SkyWest was able to turnaround ASA’s standing on the Transportation Department’s performance list from 20th to 10th place, within two years of acquisition from Delta
- SkyWest enjoyed respectable profits even when other competitors produced flat earnings or lost money due to its reputation of being well run

Partnership alliances with major carriers
- Delta Connection contracts represent approximately 59.9% of SkyWest’s capacity, while 40.1% of capacity dedicated to United Express contracts
- SkyWest diversified risk by partnering with Midwest Airlines in 2006, relationship ended in 2009 after Midwest acquired by competitor - Republic Airways Holdings
- SkyWest positioned to compete for more code-share contracts; Western Airlines purchased by Delta Airlines

Human resources
- Non-union workforce provided greater flexibility in comparison to competitors
- SkyWest Airlines non-unionized while ASA is unionized by ALPA
- SkyWest never experienced work stoppage due to strong employee satisfaction
- Offer competitive salaries, bonuses, rapid pilot promotions, retirement plans, employees stock purchase plan – discouraged unionization

Safety and Maintenance
- Participated in a voluntary reporting program (Aviation Safety Action), 6-week training program that helps pilots identify potential safety hazards
- Implements Stetson Quality Suite, mobile data collection and reporting software used to ensure companies meet/exceed safety and quality standards
- 2:1 maintenance time to flight time ratio; line service inspection every fifth day
- Proactive safety maintenance policies that immediately carries out directive from manufacturer if a part is unsafe, as opposed to waiting for FAA’s directions

Fleet of Airplanes
- SkyWest’s fleet consists of: 442 aircraft, 374 Bombardier Regional Jets (10 more acquired in 2009), 12 ATR 72 twin-turboprop aircraft (2009)
- SkyWest/ASA combined firm orders to acquire new regional aircrafts; cost-efficiency to operate, manage aircraft operation costs
• Bombardier Regional, quietest commercial jets, offer amenities such as; flight attendant service, stand-up cabin, overhead/under-seat storage, lavatories, etc.
• Speed of Bombardier Regional Jets was comparable to larger aircrafts operated by the major airlines and had a range of approximately 1,600 miles
• Bombardier Regional Jet operating cost lower than a 12-seat or a larger jet aircraft
• Embraer, ATR Turboprops cost efficient for short-haul routes vs. larger jet aircrafts

Cost differentiation
• SkyWest offers differentiated products; Embraer, ATR Turboprops expected to operate in high frequency service, low volumes passenger traffic, comfort features, made operations Bombardier Regional jet impractical

d. Strategic Objectives
• Expand contractual relationships, attract permanent business from low-cost carriers including: US Airways, Southwest, and JetBlue
• Expand operations internationally, particularly in China, Brazil and Mexico who are all in high growth, emerging regional aviation markets
• Expand contracts and diversify operations to reduce dependence on Delta and United
• Fight for the removal of “scope clause” restrictions to increase number of routes

e. Financial Objectives
• Continued growth/increased revenue; only 3.49% between 2007-08 compared to CAGR 25% in previous 5yrs
• Reduce operational costs; acquisition of ASA from Delta Airlines
• Continue to find cost-effective ways to run operations to offset additional costs associated with rising fuel cost and mandatory legislations
• Expand acquisitions to increase operational revenue; access to the East Coast markets/national coverage, expanded scope of operations; regional jets to their fleet, $1 billion in operations
• Hedge $25 million outstanding debt from Delta, and the additional $5 million incurred from legal negotiations

Summary: SkyWest Inc. is able to survive within a highly competitive industry due to its business strategy commitment to quality customer service, employee satisfaction and proactive safety management. The drive to provide quality service ensures SkyWest’s position in securing strategic partnerships with major carriers and customers. Proactive safety management helps SkyWest build a strong brand image that to diffuse fears associated with flying. Lastly, employee satisfaction is crucial for SkyWest’s strategy because it deters unionization from happening so that they can continue to enjoy the flexibility in making important business decisions.

3) SWOT Analysis
a. Resource Strengths

Tangible
• Technology systems: Stetson Quality Suite – for safety and quality standards
• ASA acquisition yield to an annual growth rate of 29.6%
• Combined revenue passenger miles increased 4.9%(2009), load factor improved 80.0% to 82.3%(2009); 2nd quarter improved revenue profits JetBlue/US Airways/Alaska Air Group; turnaround conditions; JetBlue June bookings picked up
• Large geographical base; SkyWest operations served 158 cities in 42 states; hubs, maintenance based in international locations, Regional carriers in Europe, Latin America, China,

**Intangible**

• DOT recognized SkyWest as the number one on-time Airline, 2nd fewest involuntary denied boarding, 4th regional airlines, and complaints per 100,000 passengers
• Reputation for being well-run – ability to improve service ASA operations form 20th to 10th places; named as Regional Airline Company in 2002
• Strategic alliances – Delta Connection, United Express, Midwest Connect
• SkyWest Airlines – non union – flexibility in making decisions
• Company’s proactive safety and maintenance policy
• Well-respected training program that attracts tuition paying FAA personnel
• Compensation package and strong employee satisfaction discouraged unionization

**b. Weaknesses**

• Liquidity threats - $25M outstanding debt form Delta
• Revenues and customers highly dependent on partnerships with majors
• Limited partnership with Delta and United makes SkyWest susceptible to risks and limits opportunities for growth in revenue and customers
• Delta controls all passengers, cargo, and other revenues associated with each flight,
• SkyWest paid a fixed dollar amount per completed flight block hour and reimbursed all direct costs (ie. fuel, ground handling, and aircraft maintenance and ownership)
• Major partners, United (2006) and Delta (2007) in bankruptcy protections
• 59.9% combined Delta Connections, 40.1% United Express
• SkyWest/ASA partnership is complex – fixed fees, incentives, provisions, etc.
• Scope clauses limits the size of aircraft to be flow – restrict business opportunities
• Planes capped at 76-seats, average passenger load factor at 76.48% (2004-2008)
• Limited domestic opportunities – Republic Airways acquired Midwest and Frontier Airlines, unsuccessful acquisition ExpressJet (2008), stronger competitor,

**c. Opportunities**

• Establish partnership with for other network and low-cost to diversify operations
• Expanded contractual relationships; operated few routes for Continental, overtures into established partnerships with low-cost carriers (US Airways, Southwest, JetBlue)
• China, Brazil and Mexico are all high growth, emerging aviation markets
• Opportunities to help build airline in Brazil or China; trained employees, purchasing power helped buy at lower rates, organize 10- to 20-aircraft operations needed major regional carrier in countries
• Removal of “scope clause” may result in increased routes, capacity and business

**d. Threats**

• Risks associated with having only two major partnerships – Delta and United
• Slow-down in long term growth in industry; business customers decreased by 60% and market not expected to revert back to pre-recession numbers until 2011
• Terrorist attacks, rising fuel costs, focused media attention on safety
• Consolidations of major carriers due to the unsustainable condition of the industry; potential mergers will limit partnership and growth opportunities for SkyWest
• Threat of strike and unionization of employees

**Summary:** The core competencies that stand out in the SWOT analysis are operations management, human resource management, safety, and customer service. Major carriers
have upper hand in controlling SkyWest’s supply of passengers, flight routes and fleet size. Limited partnership with Delta and United makes them the sole supplier for customers, thereby decreasing SkyWest’s bargaining power.

4) SkyWest’s Value Chain System

a. Primary Activities & Costs:
   i. Strategic partnerships/Alliances
      • Regional airlines derive most, if not all, of their revenues from contracts with majors
      • 95% of regional airlines revenues from contracted fees per departure with majors
      • Regional airlines subject to a number of operating constraints, ranked poorly by Airline Quality Report for problems caused by major carriers
      • SkyWest Inc.’s alliances – Delta 59.9% and United Express 40.1%
      • Pressure for major airlines to cut cost forced regional airlines to accept lower fees
      • SkyWest’s revenue decline by $18.3M from reductions in flight schedules by majors

   ii. Logistics
      • Regional airlines provide service from small cities to support network carriers’ hub-and-spoke system – short-haul flights that services small communities
      • To ensure passengers continued flying with regionals, airline was required to deliver passengers to their destination on time so that they don’t miss their connecting flight
      • DOT recognized SkyWest as number one on-time Airline, average mishandled baggage, 2nd fewest involuntary denied boarding, 4th regional airlines; complaints per 100,000 passengers

   iii. Customer Service
      • Majors’ condition for partnership with regional carriers: Regional airlines must maintain high levels of customer service, develop a strong safety image, maximize on time arrivals and acquire new aircraft
      • SkyWest awarded as #1 Regional airline in the industry by two magazines
      • Reputation for being well-run – ability to improve service ASA operations form 20th to 10th places; named as Regional Airline Company in 2002

   iv. Financial / Cost Management
      • Increasing jet fuel price will cost airlines 35-50% of overall operating costs
      • Increased merger activities lead to higher debt load and could destabilize the industry
      • Limited partnership with United and Delta for customer and revenues - both carriers had been in bankruptcy protection in 2006 and 2007, respectively
      • SkyWest Inc. operated its subsidiaries separately, but combined functions in finance, treasury, IT and admin to realize economies

b. Supporting Activities & Costs:
   i. Human Resources
      • 40% of airline expenses comprised pay for airline professionals
      • Most airline employees are represented by one of many labour unions – union have the ability to stop work through strikes, results in financial loss for airline companies
      • ASA unionized while SkyWest Airlines is non-union
      • Handsome, competitive total compensation package; offered level of employee satisfaction, result discouraged unionization

   ii. Marketing
      • Passengers would not fly with airlines that had an unsafe image
      • Paranoia associated with flying due to recent Sept 11 terrorist attacks
Summary: The airline industry’s primary activities include strategic partnership with major airlines, logistics, customer service and financial management. SkyWest is faring very well in most factors with the exception of their strategic partnerships. Partnership alliances with network carriers play a pivotal role in getting customers for regional airlines. Since SkyWest only has two key partners (Delta and United), they are unable to further capitalize on market shares. Despite this limitation, SkyWest is excelling in other value chain activities such as customer service and cost management to maintain a healthy financial condition and remain competitive in the industry.

5) Representative Weighted Competitive Strength Assessment
(Chart: Refer to External Assessment)

Summary: The best performing company within the regional airline industry was SkyWest Inc. SkyWest has a strong customer service, good reputation for safety and harmonious relationships with employees. Pinnacle Airlines Corp. had the lowest score due to their unsafe practices that killed 49 people in 2009. Republic Airway Holdings followed SkyWest with an overall score consisted of an average score for their strength ratings. Lastly, ExpressJet and Mesa Air Groups scored lower as they both had bad financial management scores.

6) Main Strategic issue:
Business platform lacks diversify due to limitations with having only two partnerships
How can SkyWest Inc. develop and expand strategic relationship with other carriers in the industry to realize higher financial returns and better control over their operational activities?

a. Supporting Facts:
• Delta Connection contracts 59.9% and 40.1% from United Express
• As of 2008, SkyWest operating approximately 430 Delta Connection flights per day
• Delta was entitled to passenger cargo and other revenues associated with each flight
• SkyWest’s unfavourable relationship with Delta Airlines due to a legal dispute over Delta’s refusal to pay $25M payment owed to them
• Ongoing negotiations regarding compensation of expense with partner Delta Airlines – company suffered a $5million reduction in revenues
• Wind-down of SkyWest partnership with Midwest Airlines. Midwest’s subsequent bankruptcy and purchase by a main competitor Republic Airways Holdings
• $18.3M decline in SkyWest’s revenue was due to reduction in flight schedules made by the company’s major partners
• Business travelers are flying low-cost, resulting in a decrease of 60% business market share for major carriers and 20% increase for low-cost airlines
• Regional airlines subject to a number of operating constraints and are fared poorly in Airline Quality Report for problems caused by major carriers
• Passengers are of the major carriers’ and the identity of regional airlines was not normally the concern or interest of the passenger
• ASA came in worst for bumping passengers due to overselling seats even though it was Delta Airlines that was responsible for overselling them
• Regional issues are controlled by the major partners; partners controlled the regionals’ scheduling not allowing enough time to load and unload passengers luggage
• Increased pressure for major carriers to cut costs forces regionals to also cut costs
SkyWest’s position in the market reveals the need to address the main problem with its business strategy as it restricts long-term growth for the company to sustain itself and survive as a company. Dependence on profit growth and differentiation strategy has not provided enough revenue to stay ahead of major carriers plus low-carrier strains. On this note, it is apparent that there is a critical need to re-evaluate internal position of operations while building strategic measures to reduce expenses and increase revenues. The following paragraphs address these points while revealing three concerns of limited partnerships, high fuel costs, and restrictions with unions in terms of scope clause. Thus, pointing out the dynamics to lost growth.

**Analysis**

Currently, SkyWest’s partnerships are limited to two major carriers (Delta Airlines and United Airlines). Major carriers have the upper hand when discussing contracts with regional airlines because they are much larger in scale and dominate supply of flight routes. They are also subjected to restrictions regarding fleet size and geographic coverage due to scope clauses between both carriers and their unionized employees (Internal, 3b). These limitations influence the ability to fly longer routes at higher capacity and benefit from economies of scale. Planes are capped at 76-seats, average passenger load factor at 76.48% (2004-2008) (Internal, 3b). The breakeven load factor has been increasing at a rate of 2.58% every year (Internal, 1). Moreover, United and Delta had both just emerged from bankruptcy protection in 2006 and 2007, respectively, and both operate using similar business models. Both are exposed to same types of economic and environmental risks (External, 1b, 1e). These risks fell onto SkyWest and worsened by 2007-08 recession. It’s 2008 net margin of 3.23% are the lowest in the last five years; rising fuel costs and reduction of flight schedules has attributed to a $165.3 million drop in revenues in the mere first quarter of 2009 (Internal, 1).

SkyWest had originally partnered successfully with the major carrier Midwest Airlines prior to being acquired by Republic Airways Holdings. Republic is a regional carrier and direct competitor of SkyWest. They took ownership of Midwest and Frontier Airlines (External, 2b, 2i). Republic’s move not only made itself a bigger competitor, in terms of size, its acquisitions of Midwest and Frontier brought the company a supply of flight routes, which reduced the number of major flight routes being offered to the rest of the regional airline market. This event left SkyWest reliant on remaining partnership contracts with Delta and United, which represents 59.9% and 40.1% of SkyWest’s operating capacity, respectively (Internal, 2c, 4a). Consequently, Delta controls all passengers, cargo, and other revenues associated with each flight, and SkyWest is paid a fixed dollar amount per completed flight block hour and is reimbursed all direct costs including fuel, ground handling, and aircraft maintenance and ownership (Internal, 3b). Delta’s contract with ASA is similar, except ASA is reimbursed a percentage of cost only after completing a minimum number of flights rather than a fixed rate. Moreover, Delta has the option, not SkyWest, to extend or terminate the ASA Delta Connection Agreement in 2020 (Internal, 3b). This agreement is critical to SkyWest because it represents over a third of SkyWest’s total daily flights (775 out of a total 2105) and is broader in geographical reach (Internal, 1). Delta’s refusal to pay expenses gives them greater bargaining power and has already cost SkyWest $5 million during negotiations but
SkyWest is wary of damaging the partnership going forward and risking nearly 60% of its revenue source (Internal, 3d). SkyWest’s contracts with United are similar, except that they are expiring even sooner in 2011, 2013, and 2015.

SkyWest’s dependency on major carriers risks poor performance level and damaged reputation in terms of customer service, mishandling baggage and cancelling flights. The numerous reports on regional airlines’ baggage problems, are often due to poor scheduling decisions made by partners, limiting time between flights and regional’s transfer luggage. In order to not fall into this perceived negative image of airlines, SkyWest must find a method to manage these risks and maintain a high level of service (Internal, 4aiii). As mentioned above, scope clauses restrict SkyWest’s ability to purchase larger aircrafts with more than 76-seats. This restriction diminishes conveniences for SkyWest customers, since smaller planes limit SkyWest’s area of service. This puts SkyWest at risk, as there is a possibility that customers will look elsewhere for an airline that covers a larger geographic scope. In addition, the scope clause takes the opportunity away from SkyWest to expand their network outside of major airlines. If the scope clause was not placed on SkyWest, there would have been a greater opportunity for the company to create more business from its partners. SkyWest is limited in their networking abilities with other airlines that could potentially lead to higher operating revenues.

Next, SkyWest faces a risk of ASA labour union seeking a “single carrier determination” from National Mediation Board in an attempt to unionize SkyWest Airlines employees, which increases the possibility of conflicts against the employers of SkyWest, including strikes. As SkyWest acquired and as the parent company of ASA, they must take on all of the relations with their employees, including union employees. However, SkyWest Airlines’ employees are not unionized, thus creating a conflict of interest between SkyWest Airlines and ASA employees. ASA union has created serious concern from ASA employees, as the concept of consistency is not administered from the parent company. Therefore, SkyWest must come up with plausible solutions to avoid a strike, which can severely damage performance levels and ability to acquire new contracts.

Despite previous unsuccessful attempts to acquiring partnerships with major and low-cost carriers such as Continental and US Airways, SkyWest will need to continue to maintain its high levels of customer service and safety image, maximize on-time arrivals and obtain financing for new aircraft, in order to attract new contracts and diversify business risks (Internal, 2d). Depreciation and amortization is $824M as of 2008, indicating that planes are getting older and some may need to be replaced (Internal, 1). Despite economic downturn, SkyWest has been able to improve all debt ratios between 2007-08, representing a possibility to obtain more credit (Internal, 1). Horizontal integration is also an option for SkyWest to guarantee access to flight routes, as long as the company can remain solvent through the process.

Finally, rising fuel costs are heightening the pressure that SkyWest is already experiencing with partners and ALPA’s simple carrier determination as attempts to unionization. In the realm of these concerns is an opportunity to build revenues which can be possible through acquiring new flight services, negotiate fair deals to distribute control over flight routes, and increase availability of resources, to help in compensating for fuel consumption, reducing costs associated to fuel. Primarily, fuel consumption has been caused by limited partnership in that Delta had refused to pay $25million in maintenance of fuelling aircrafts within their contracts (Internal, 3b). This added by recession and lack of available alternatives to manage the added debt accumulated. Another important factor
to help address increases in fuel costs would be to improve weather systems software in reducing cancellations. The accompaniment of establishing systems that can forecast economic conditions to prevent profit loss provides manageable alternatives to prevent financial loss from accidents related to no fault of their own. All of these measures help address the availability of compensation to manage and stabilize fuel costs that are increasingly hindering business quality and image of service that SkyWest attempts to maintain. Thus, this is a valuable opportunity to focus attention on allocating funds to better use. Consequently, streamlining resources and management of fuel costs that are currently at 35-50% of total operating expenses illustrate the need to rearrange revenues (External, 1b, 3d). This approach is highly critical in being able to build and expand business in acquiring new planes and transforming business into new markets such as low-cost carriers, purchase agreements, fuel hedging to tackle fuel price hedging operational expenses at hubs and maintenance locations. Vertical integration is the key to a unique strategy in taking the next leap in reducing fuel consumptions to be managed proactively vs. reactively.

Recommendation
Based on the above points, SkyWest need to diversify its portfolio and expand into new markets, demographically as well as globally in order to survive and remain competitive in the airline industry. Particularly since recently acquiring contracts has been a serious concern as seen with Midwest lost to Republic Holdings, a major rival. In addition, bankruptcies and takeovers establish additional constraints on SkyWest to build and attract partnership relationships. This is further influenced by high fuel costs and additional regulatory restrictions from “scope clause”. It is also evident with ALPA tried to use “single carrier determination” as an attempt to campaign in building a union at SkyWest. This is one key point visible within business/functional strategic analysis that drives factors in revealing SkyWest concerns that are depleting its ability to build revenue growth in the U.S. Airline industry. Additional illustrations are in the collective agreement as it is preventing expansion opportunities with passenger seat size of purchasing new aircrafts. Irony of this situation is that SkyWest pilots were open and “took on flights that were 70-90 seats at same rate as 50-seat aircrafts”. This reveals good relationships that the company has built with their workforce however the restrictions aren’t helping strategic initiatives within partnerships.

Consequently, internal and external analysis reveals the need to diversify business risk by acquiring new contracts through partnerships, and if credit allows, mergers and acquisitions as well as overseas ventures. It is important to develop ventures, acquisitions with major carriers, which currently SkyWest is missing out on. Thus, providing valuable framework within business functional operations to build a structure that is proactively managing problems that have incurred as a result of no fault of their own. Establishing fair business practices in the process while cost effective management procedures to sustain stable expenses like fuel cost and scope clause that hinder expansion and profit growth as internal, external and financial analysis revealed. In a nutshell differentiation into new markets as source of diversification in all aspects of operations are leveraged opportunities if taken, could provide the needed positional competitive edge, to bring SkyWest to a heightened platform of success.