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THE BACKGROUND TO AIR FRANCE'S RECOVERY

by

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Overview

At the start of the 1990s, an economic crisis put the European air transport sector into difficulty. In 1993, Air France went into the red. Christian Blanc was called to the rescue. He put in place a number of strategies : he attempted to boost staff morale, he implemented a powerful strategy to help Air France's commercial development by deciding to build a hub at Roissy-Charles de Gaulle (CDG) airport, he merged Air France with Air Inter, and he took great care to establish good relations with the employees. He successfully managed to guide the company out of the crisis. In 1997, his successor, Jean-Cyril Spinetta, ensured the development of the group by signing three-yearly agreements with the pilots and other professionals, optimising salary management, and reducing operating costs. The alliance with Delta Airlines, completed in 1999, opened up the American market to Air France, and its merger with KLM in 2004 made Air France the number one European passenger airline. In 2006, Air France-KLM became the world leader in air transport in terms of turnover.

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TALK : Pierre-Henri GOURGEON

Having experienced a serious economic crisis in 1993, Air France gradually recovered. In 1996, Air France accounted for 13.2 % of the airline activity of all European carriers, whereas Lufthansa accounted for 14.6 % and British Airways, 23 %. There was no wish to do better than British Airways because the European Commission, in exchange for an agreement whereby the State gave Air France 3 billion Euros in financial aid (20 billion Francs), forced the company to limit its production for the following three years. This period came to an end in September 1997 : this was a very important date for the recovery of Air France because additional aeroplanes were then brought into service very quickly. It was also at this time that Jean-Cyril Spinetta succeeded Christian Blanc.

After 1996, the British Airways' European market share started dropping steadily and had fallen to 16.6 % in 2002 when the three airlines were close to parity. KLM, which had a market share of 11.3 % in 1996, but which had dropped to 9.6 % between 2003 and 2004, began to take British Airways' and Lufthansa's share of the market once the merger of Air France with KLM took place. Between 2005 and 2006, Air France's market share was 17 %, Lufthansa's 16.2 %, British Airways' 16.1 %, and KLM's 9.9 %. Air France therefore had become the leader in a market which itself had grown by 50 % in the space of ten years.

In 2006, Air France-KLM dominated the European market with a market share of 27 %, and the group became the global leader in air transport in terms of turnover.

In my talk, I will make many references to Air France-KLM, British Airways and Lufthansa since these are the three principal companies in terms of international air traffic. Leaving domestic travel to one side, Air France-KLM is far and away the leader in international transport, followed by British Airways and then Lufthansa. Japan Air Lines is in fourth place, and the highest placed American airline occupies fifth place. This is quite simply because in the United States, airline companies devote themselves principally to domestic activity.

The keys to success

Air France's recovery did not take place solely due to new management methods, such as the title to my talk might suggest. Ordinary everyday techniques were used, such as those which promoted social management and reducing costs, while at the same time relying on certain strengths, sometimes largely unknown, which I will highlight during my talk.

Social management

We are constantly ensuring that the system is stable with regard to employee relations. Global transport companies are particularly susceptible to social upheavals. In other countries, the right to strike exists, but, in order to avoid deadlock, it has to be carried out in a controlled and reasonable way. In France, going on strike is a primary constitutional right and occupies an important place. As a result, all forms of transport activity are exceptionally difficult to manage with respect to employees. This factor is therefore a priority for us in terms of management.

Cost reduction

The air transport sector is constantly evolving and therefore one has to innovate all the time. However, at the same time one has to simplify one's activities in order to reduce costs, otherwise one will be overtaken by others. Consequently, we are constantly putting ourselves under pressure, but everyone in the company understands the reasons and accepts them.

Strengths of the company

Our three fundamental assets to which I will refer, are the balance we achieve in our network, our use of alliances, and our hub activity. All of these factors work towards our main aim which is to satisfy the business traveller.

The story since 1990

In 1990, an economic downturn took place in the United States and started to reach Europe. With the exception of British Airways, which was privatised in 1987, and which was economically buoyant between 1991 and 1992, all the airlines experienced economic difficulties.

The crisis at Air France

In 1993, other airline companies started making money but Air France went further into the red. This period marked the dawn of liberalisation. In France, liberalisation took various forms. Widespread discussions were held debating the pros and cons of these changes. Trade barriers were opened, competitors were able to contest traffic rights, and people were forced to adapt. A change in the political party governing the country added a bit of spice. In short, at the end of 1993, Air France was in turmoil and the Interior minister told the Prime Minister to do something quickly 'otherwise the riot squad won't even be enough'. Christian Blanc stepped in and calmed everyone down by brushing aside any fears of job redundancies and obtaining a huge sum of state aid. This prompted a desire to move forward : the staff were motivated by this development and the Air France employees understood that from that moment, the State would no longer help them out, and that they would have to fend for themselves.

A new organisation

Between 1994 and 1995, the management team, keen on reorganisation, envisaged creating five companies within Air France, each one dealing with a geographical area (America, Africa, Asia, Europe, and France). Each would have its own fleet, pilots, air hostesses, commercial operations, and so on. At almost the same time, Christian Blanc sought advice from Steve Wolf, the former chairman of United Airlines, who in an attempt to save his company, had implemented a 'Shares-for-Salary' scheme giving (more or less) power to pilots. Wolf was subsequently forced to step down from the company. He quickly pointed out to Christian Blanc that breaking up the company would make the whole system fall apart, because an airline company is a network whose base must be strong and whose parts must be able to inter-communicate. At the same time, he recommended speeding up the construction of a hub at the Roissy-Charles de Gaulle (CDG) airport.

The establishment of a hub

In the United States at the end of the 1960s, Frederick W. Smith, who was a student at Yale, had the idea that the only way of optimising the handling of letters and parcels in the postal system, regardless of their origin and destination, was to make them transit through a single point (a 'hub') and then to send them to their respective destinations. In this way, it would be possible to fill aeroplanes with an adequate amount of mail. Frederick W. Smith created FedEx, the international express transport company, of which he is the current president. Applying this concept to passengers is a little complex but it has been working in the United States since the 1980s. The first airline to bring this method to Europe was KLM, who built its hub in Amsterdam : as a result, it managed to come just behind Air France in 1994 in terms of turnover. Following this, Lufthansa and British Airways also built hubs, but during this time at Air France, questions continued to be asked about the logic of such an idea until the day that the decision was taken. Raquesh Gangwal, a former colleague of Steve Wolf's at United, was in charge of establishing the hub and surveyed relevant people to decide if this would meet their needs rather than look for reasons not to create it.

The Roissy-Charles de Gaulle hub project started in 1996. Let us consider a flight from Turin to Paris. This flight would not be justified by only the local passengers flying between Turin and Paris. But half of the people on this flight will be flying onwards from Paris to other parts of the world. We know that one in 2 passengers travels to New York, one in 2 to Rio, one in 2 to London, one in 3 to Tokyo, and so on. Thus, although the Turin to Paris flight is not justified because of the small local market, it is justified by the onward movements of the passengers. This is how we can do our job : connecting Europe with the rest of the world.

The Air France-Air Inter merger

In 1996, it did not seem possible that Air Inter could remain independent from Air France. Air Inter had nothing to gain because giving its transit passengers to Air France was not lucrative. Air France was not interested in the domestic flights operated by Air Inter because they did not generate any money apart from the connecting flights. A merger of the two companies was the only solution to resolve this conflict of interests. In March 1997, the Air France group merged officially to become the Air France company. Now the strong domestic network is totally consistent with the international network.

A very exciting period

In 1998, the three-yearly cost reduction plans initiated by the management strategy began. This year also saw the implementation of the Shares-for-Salary scheme following a strike by pilots. Other important events included the SkyTeam alliance in 2000, the creation of Air France-KLM in 2004, and the privatisation of Air France in 2005.

Profitable growth

Growth on its own is not enough without profit. From 1997 to 2003/2004, even though profits remained poor, we were never in the red. Since 2004, with an improved financial situation thanks mainly to the Air France-KLM alliance, we are in the process of economic recovery with profitability rates which are not very high but acceptable (936 million Euros for the year 2005/06 for a turnover of approximately 21 billion Euros).

The pilots

Between 1994 and 1997, the Air France accounts were negative, especially in 1995. Management compared their figures with other companies and concluded that special financial measures had to be taken in the case of the pilots. At the end of 1996, it was announced that the aim was to reduce the pilot costs by 15 %. It did not take long for difficulties to arise : the very powerful alliance which had been established two years earlier between the pilots and Christian Blanc became a battleground, resulting in strikes. Management defused the crisis by agreeing with the new leader of the pilots to find a solution within the year. During this truce, which should have ended on June 1st 1998, discussions were stormy. The pilots refused the management's plan to reduce the new pilots' salaries by creating a double salary scale. Discussion became heated and at this point, the management changed : Jean-Cyril Spinetta arrived at the end of 1997 and inherited this prickly subject. I took up my post on April 1st 1998 and we worked very closely to find a solution, but by May 31st we still had a stalemate. We had suggested a Shares-for-Salary scheme at the beginning of May. We realised that it would not be accepted if we made it compulsory, so we suggested it be approved on a voluntary basis. It was clear that the trade unions wanted a confrontation : if they stopped French air transport ten days before the football World Cup, the government would have to give in, and instruct the Air France management to accept the union demands. By accepting the truce, the trade union officials had, in fact, simply chosen the best moment to strike.

And the strike took place. We spent ten days negotiating, both day and night. We ended up with an 'all win' agreement in which the company maintained its 15 % reduction in costs and the pilots got what they wanted because they finally accepted the Shares-for-Salary scheme on a voluntary basis. The result was a sort of three-card trick : the State gave free shares to the pilots ;

in return the pilots accepted a reduction in their salaries ; and this in itself created a reduction in costs thereby improving profits and the value of the company. Finally, the State actually became richer because the remaining shares which it possessed, should have increased in value from their initial cost. Additionally, at this time giving shares was not accounted for in the company's books, which meant that on the one hand, salaries were lowered and on the other, the accounts were healthier. As for the pilots, they neither paid taxes nor social security contributions on that part of their salary which was converted into shares. Generally speaking, the system works : 78 % of pilots chose to take this Shares-for-Salary scheme which lowers their annual salary, while the salaries of the remaining pilots are frozen but maintained.

Contractualisation

Under the leadership of Jean-Cyril Spinetta, we are constantly trying to manage employee relations by negotiating contracts with various professional categories, a process which we refer to as 'contractualisation'. We started with the civil aviation air-traffic controllers in 1988. We negotiate an agreement with the pilots every three years. Clearly, this is not the best solution and at the end of three years, the discussions are sometimes contentious and there may be strikes, but at least we put things into perspective and in principle, there are no strikes during the period of the contract. This is progress for the passengers. Contractualisation calms things down. We have an agreement with the stewards and stewardesses and soon we will draw up a contract with the ground staff. The professional organisations of Air France are now, for the most part, in favour of contractualisation. Two months ago, we negotiated a new agreement with the pilots for the next three years : no-one objected.

A balanced network

All continents and all destinations are served more or less equally in our network. This is an advantage by comparison with British Airways is concentrated more on North America and Asia, and Lufthansa which serves the same areas as British Airways but also includes Northern Europe. We have developed more routes to South America, we dominate the African market and we are also present in North America and Asia, not to mention the Caribbean and the Indian Ocean which, due to their close links with France, represent an important long-distance activity for us. When an air traffic crisis began in North America after the terrorist attacks of September 11th 2001, because of our presence in so many areas, we were able to divert our activity to Africa and the French overseas territories and *départements*. When SARS (Severe Acute Respiratory Syndrome) broke out in Asia, our network in Africa and South America allowed us to minimise the impact of this event on our revenues. In a business which is naturally very sensitive to geopolitical events, our flight network balance allows us to withstand potential difficulties better.

The Delta alliance

In 1999, air traffic within Europe, within the United States, and between Europe and the United States, represented 50 % of all world air traffic. United Airlines had formed an alliance with Lufthansa, British Airways with American Airlines, and Delta, the third American carrier was looking for a partner. So were we. Having hesitated between Continental Airlines and Delta, in the end we chose Delta. At Air France, people were worried that because of Delta's profits of a billion dollars, they would swallow us up. In spite of such fears, we have learned to live together and we enjoy a very good relationship. In an alliance, generally speaking, it is the smaller of the two who benefits more than the larger, and we at the time were the smaller one...

An asset for Europe

The leaders of these alliances are the three European companies – Air France, British Airways and Lufthansa. Because of its geographical location, its history and therefore the anteriority of its economic wealth between America and Asia, Europe has the means for global air travel, and therefore for global business, at its disposal, since it is a economic centre. For Europe, this is an exceptional asset and is a great strength vis-à-vis global rivals. Companies that want to have

worldwide influence continue to locate in Europe. We try to explain this to European managers, for example at the European Commission in Brussels, or to our friends at the French civil aviation authority when they are told not to hand out traffic rights at random and rashly, especially to companies from the Gulf emirates. These companies invest billions of dollars to try to seize as large a part of world air transport between Asia, the United States and Europe as possible in order to create wealth which will enhance sales of services, tourism and other sorts of activities in oil-rich deserts.

An access to the world market

One should also be aware that the liberalisation of air transport, which is often taken for granted, is not yet finished.

Air France may only serve non-European countries from a French departure point : for example, we do not have the right to fly between Berlin and New York. The American airlines can, because they have bilateral agreements with all the countries. So what can we do to get around this difficulty ? Thanks to our Roissy-CDG hub, we can encourage people from other countries to travel via Paris. Once they are in France, we have the right to transport them to the rest of the world.

Air France also does not have the right to operate domestic flights in the United States : we can fly from Paris to New York or Paris to Chicago, but not from New York to Chicago. Similarly, the Americans do not have the right to fly from Paris to Marseilles. However, since our alliance with Delta gives us access to the American market, we are now able to pick up business travellers wherever they are.

It is easy to see that we complement each other in our alliance and this is possible without one taking control of the other. In any case, this would be impossible because Congress continues to oppose the control of an American airline by a non-American company, and vice versa.

Top of the computer list

There is another advantage to this alliance. If one wants to book a Paris-San Diego flight using a travel agent, the travel agent will say that there is no direct flight and that one has to change aeroplanes. How are connecting flights shown on the travel agent's computer screen ? At the time that the rules were drawn up to show flight offers, the American authorities thought it was easier for a passenger to take several flights using the same airline. In this way, the passenger would not have to change terminals and would be less likely to lose his baggage. This is why flights with connections are shown on the screens of travel agents starting with the shortest flights and those which are operated by the same company, in other words where the flight number begins with the same company code (AF for Air France, DL for Delta, BA for British Airways, and so on.). The Delta alliance was crucial for us from this point of view because it allowed us to put our AF code on all the domestic Delta flights which originated from the Delta hubs in Atlanta and Cincinnati. Conversely, it allowed Delta to put its DL code on our flights. As a result, our connecting flights appear among the first flights to be displayed in the list on travel agents' computer screens using the GDS (global distribution system), on any one of the four major GDS software systems (Amadeus, Sabre, Galileo or WorldSpan). Prior to this, one had to scroll down to the fourth page of the displayed list or even further in order to realise that there was a possible connection between a Delta and an Air France flight. To make it easier, flights are also listed in order of the length of the flight. All these factors are very important to us as we were told that 80 % of flights sold appear on the first page displayed on the screen, and that the first line alone accounts for 50 % of sales ! It is obvious that the larger our network is and the greater the number of connections we have, the better we will be able to meet clients' needs and therefore the more likely that our flights will be listed higher up in the system.

Aeroplane-sharing

The same flight can be referenced in two different ways. For example, a flight from CDG to Cincinnati has the initial code DL 043 and then a second code AF 8700 : the origin, destination, time of departure and length of flight are identical. In one case, it is sold as a Delta flight and in the other as an Air France flight, but this flight is operated by a single aeroplane and both companies sell the seats on the aircraft. Of course, there are certain passengers who are displeased when they discover that they are in a Delta aircraft whereas they thought that they bought an Air France ticket, or vice versa, but people get used to it and this aeroplane-sharing enables us to be much more efficient.

Capturing the business client

Business passengers are everywhere in the world and their number is increasing due to globalisation. Even SMEs (small and medium-sized enterprises) are using air travel more and more to meet future business partners.

If we are able to poach passengers from Lufthansa in Frankfurt or from British Airways in London, it is because these passengers have not been able to get a seat on their usual flights, and this also works in reverse. The real competition comes into play when the business travellers are forced to take connecting flights. They prefer flights which are less time-consuming, allowing them to keep to their business schedule. Therefore, we have to offer the greatest number of connecting flights possible.

As far as connections between medium-haul and long-haul flights (ie. between Europe and the rest of the world), with a wait-time of less than two hours is concerned, we have 21,000 possible connecting flight options per week, whereas Lufthansa has 13,000 and British Airways 7,000.

Thus, statistically speaking, we are much more often at the top of the travel agents' computer screen and this enables us to win new clients and to keep them. In 2006, the SkyTeam alliance which consists of Air France-KLM, Alitalia, Delta Air Lines, Continental Airlines and Northwest Airlines was the number one across the North Atlantic representing 35 % of the flights available and the world number two in terms of market share. Eleven million passengers have joined the Air France-KLM frequent flyer programme (Flying Blue) and this consolidates our market share and assures us of ticket sales.

Managing revenues

The heart of the business, especially in relation to connecting flights, is revenue management.

Making decisions in real-time

Let us take the following scenario : in Madrid, two clients arrive at the same time at the Air France ticket counter. The first passenger wants a Madrid-Paris return ticket in business class which costs 1,280 Euros which has an excellent profit ratio per kilometre for us. The second client wants to go to Bangkok : this ticket costs 2,550 Euros and the profit ratio is much lower. We have a Paris-Bangkok flight which is proving difficult to fill and there is only one seat left on the Madrid-Paris flight. We have to make a choice. If we want to optimise our global network, we should sell the Madrid-Bangkok flight via Paris, knowing that the seat occupied from Madrid to Paris will be registered in the accounts of this Madrid-Paris route at less than 200 Euros. If, in Madrid, our ticket staff objectives are based purely on profitability on the Madrid- Paris flight, the ticket clerk will clearly choose the first client.

This is one example of what may take place at any moment because requests from all over the world from tens of thousands of travel agents' computer screens (not to mention direct requests from passengers using the Internet) come in all the time. In practice, every second, several hundred decisions like this are made by expert computer systems which we programme to obtain

the best possible overall result. If one makes a mistake, and mistakes do happen, we immediately lose money.

Last minute ticket sales

Everyone thinks that low-cost seats on aeroplanes can be bought at the last minute. This cannot be done by companies which work on the basis of refunding tickets. It would be too easy for the passenger to be refunded the cost of a ticket bought at the normal price, once and then to buy a ticket at a reduced price as this would ruin the system. This system does not exist in major airline companies.

However, we do sell low-price tickets, but we reduce the prices in advance. There are special agents who operate this system. Their aim is not only to fill up the aircraft but also to optimise revenues. For a long-haul flight, their first concern is to sell the economy seats three months in advance because if the aeroplane is only 65 % full on the departure date, their supplier (the airline) will want to know why. To reduce the gamble and take the necessary steps, they refer to previous records which display the uptake of different classes of reservations which were sold, and which are therefore essential to airlines.

Rising prices

Filling up aeroplanes by increasing ticket prices is an essential mechanism which is well known ; even low-cost budget airlines do this. Low-cost airlines only have one class but every day the prices increase : EasyJet may even be more expensive than Air France for a domestic flight one week in advance. One should also appreciate that for domestic flights, Air Inter got us into the habit of cutting costs and operating our flights on time because of the high speed TGV train – real value for money – which is one of our major competitors.

Different classes of tickets

In order to fill our aeroplanes, we use different classes of tickets. In a 747, there are fifteen classes ; one first class, four business class, and about ten economy. Depending on the class, the ticket is either 100 % refundable, refundable under certain conditions, or unrefundable. There are also classes of tickets which are reserved for elderly people, or which are for travel which includes a week-end, and so on. Essentially we try to give the passenger the choice of ticket that best suits him and in such a way that he will not cancel his ticket and we cover our costs as closely as possible. Having said this, we have to make sure that we do not sell too many cut-price tickets in advance, because if we open up too many reduced price seats, we will undoubtedly fill the aeroplane more easily, but we will not make an optimal profit. This is why I asked the teams to make smaller price differentials between the classes. Consequently, it is more difficult to find low priced seats. One month prior to the departure date our flights are not as full as last year but are just as full or even slightly fuller on the day of departure. Revenues are up at least 10 %.

Offering a choice

As a result of the liberalisation of air fares, we created a price jungle such that a passenger might buy an expensive ticket which he could have bought more cheaply. On the Internet screen, we now highlight where the lower cost flights exist over a certain time period. This allows the passenger to change his departure date according to the different prices available. This can only work if the price variation really reflects the demand. In this case, it is a 'win-win' situation : the passenger can change his flight and buy a cheaper ticket and we are able to fill an aeroplane which we had difficulty filling (which is why the ticket was cheap). As a result, the passenger frees up a seat on a more expensive flight and we may avoid us losing a potential passenger to another airline.

Adapting the organisation

In airports, we are installing self-service electronic terminals. If you have a Flying Blue frequent flyer card, these terminals issue your electronic ticket or your boarding card. This then allows you to go directly to a special baggage counter for frequent flyers. The e-check-in, which can be printed out on one's own printer, allows you to go directly to the security check. Everything is designed to avoid queueing.

Clearly, these innovations have a great impact on the people who work at the airport. This is why we are reorganising and redefining tasks and why we stopped three years ago recruiting additional staff for the following six years. This enabled us to achieve 30 % growth during this period because the productivity coefficients are very strong. When electronic ticketing appeared, we closed our travel agencies and transferred the employees to telephone call centres to cope with the increase in the numbers of bookings by telephone. It is now the Internet which is replacing the telephone and our call centres are losing staff. We have negotiated contracts with our staff in order to manage these changing situations better. These contracts include clauses regarding job stability, professional mobility, training and constant changes in the profession.

Air France-KLM

Despite warnings from all quarters about our alliance with KLM, it has been an excellent move as we have transformed a rival into a partner who is now helping us to deal with our competitors.

No new reorganisation

In order to use all the potential strengths of our new alliance for the benefit of the customer and to our commercial advantage, we asked managers of both companies not to make any reorganisation plans for at least the next three years. This is the opposite of what usually happens when mergers take place. Then, before putting our strategy into action, we asked them to assess the potential points in common at managerial level as a result of our alliance. Of course, they allowed themselves a safety margin in their estimates so that when we asked them and their opposite numbers to put these synergies into place, the results were much better than expected. Two years after the merger, people know each other and get on well because they have worked together for some time.

The SMC

There is a managing body called the Strategic Management Committee (SMC) which links the two companies. It is made up of eight people ; four directors from Air France and four from KLM. Its president, Jean-Cyril Spinetta, has the casting vote. Everything is structured so that the decisions of the SMC are reached by common consensus and that the KLM management is not destabilised at any time. Of course, it is Air France that bought KLM, but we have retained their managers because they presented the merger positively to their staff and it is clear that they made the right decision as this merger is proving to be a success. We have therefore presented the working methods and decision-making processes of KLM positively, while having a close working relationship. The SMC meets for one day every two weeks, alternating between Paris and Amsterdam, to hear from managers about their common ground. As a result, Dutch management has got to know and appreciate French managers better, and vice versa. However, we still do not allow the hierarchies to draw up a new common organisation chart and this is why the situation is working well. One must not forget that in this alliance there are two cultures : we do not speak the same language, our social organisation is different, and each company is a sort of standard-bearer for his country. Integration can only go so far.

In the future, the SMC will undoubtedly be replaced by an executive committee made up of about twelve members, one per sector. These members will be those who are working in one group or the other. They will meet up periodically to decide future projects and the way the group moves forward, but our relationship will only be functional.

Our network is very powerful. Our group accounts for 75 % of the forty-seven routes which the main companies serve between Europe and the rest of the world. In comparison, British Airways accounts for 55 %, and Lufthansa and its partner Swissair, less than 50 %. Statistically, our business passenger finds the best flight times with us and his purchasing manager, the best price. Because we are capable of satisfying 75 % of his needs, he has signed a contract with us - as have five thousand other companies - giving him the best discount.

Our financial results demonstrate our success. In the period 2005/2006, Air France increased its number of passengers by 11 % by comparison with 2004/2005 ; for KLM, this increase was 10.7 %. Revenues have increased respectively by 14.2 % and 11.4 %, and in these revenues, growth, as a result of connecting flights, is 16.8 % for Air France and 10.9 % for KLM. These figures show that the reason for our growth is the efficiency of our system of connecting flights as part of our service to business passengers.

DISCUSSION

Question : *For a Paris-New York flight, for example, the time spent before and after the flight (ie. getting to and from the airport,) and in the airport itself (check-in, baggage reclaim etc) together account for one-third of the entire travelling time. Have you discussed this with the airports ?*

Pierre-Henri Gourgeon : We are dependent on the ADP (*Aéroports de Paris* : the body which manages the Parisian airports). The S3 terminal will not be available to us until 2007 although it had been intended for use in 2003. Currently, our hub lacks access doors with walkways. For 50 % of our flights, passengers have to be transported to their departing flights by bus.

Everywhere else in the world, airports are served by numerous train networks. This is not the case in France. There is of course a TGV station in the Roissy-CDG airport, but it is a rail/airport terminal connection, (and not on a mainline network), and none of the TGV lines using the rail/air connection go through the centre of Paris. Since there are not enough passengers arriving at the airport by TGV, there are only a limited number of TGVs which serve the airport. This is why we have been campaigning for a long time to have an express train link between Paris and CDG, but the RATP (*Paris public transport system*) and the SNCF (*French National railway company*) do not consider this a priority.

Contractualisation

Q. : *Is Air France the only airline company to contractualise ? Does this change management on a daily basis ?*

P.-H. G. : In the United States, pilots cannot strike unless George W. Bush says they can. However, he would only allow it if all other attempts to resolve the crisis failed. Anglo-Saxons prefer rules. From the 19th century onwards, federal laws stated that when an economic sector, which affects other sectors, goes on strike, this has consequences which go beyond its own sphere of activity. This was recognised by maintaining the right to strike. In keeping with this system, in 1998 the French Prime Minister told the pilots' trade union 'you do not have the right to strike at this time ; you can only go on strike after new negotiations'.

The process of contractualisation makes us act like KLM, Lufthansa, and the American airlines. It is clearly a huge change for management : it is no longer a question of holding back the means to end a strike but constantly to ensure negotiations can take place in order to deal with potential disputes. Everyone has to understand that one always gets more if one does not strike than if one does strike, and every effort should be made to ensure that there are no exceptions to this rule. The most difficult part is not conveying this message to the professional organisations, but to the management.

Non-business travellers

Q. : *Are non-business travellers an interesting market for you ?*

P.-H. G. : Of course we have passengers who are tourists, as well as passengers who travel privately. We also have special offers. Our price is often higher than the lowest price offered by other companies. But for our price, we offer a different service. The passengers may be in Economy class, but they are treated better than they would be elsewhere, and are safe in the knowledge that we are a big company which will not let them fend for themselves on the other side of the world if there is a technical problem. In general, this is not the case with budget airlines. We refuse to allow ourselves to be drawn into the trap of bringing our prices into line with other airlines. What we want to sell is our brand.

Hubs

Q. : *There are conflicting opinions concerning the end of hubs. What is the current thinking ?*

P.-H. G. : Originally, in the United States, the hubs were designed for medium-haul connecting flights between different states. Today, however, medium-haul Airbus and Boeing aircraft are able to fly for seven hours with many passengers on board and therefore are able to provide a direct service. Budget airlines, whose low prices attract a large number of passengers, can therefore now offer both a lower price and a direct flight. This has effectively put an end to the hubs which were artificially maintained by companies which operated connecting flights when they could have operated direct flights. Our strategy is to create direct routes whenever possible, in order to ensure that rival companies do not get the business first. However, in most cases, our connecting flights are those linking a medium-haul to a long-haul flight and we are far from able to offer a non-stop direct service in every case. What is true for the United States is not true for us.

Q. : *A hub was created in Dubai. It is essentially for connecting long-haul flights, for example between Australia and the United States. Why does Air France not build a hub in Dubai ?*

P.-H. G. : To do something like that, you need to have a shareholder who has a pot of gold ! But there are other reasons for not doing it : the local market, which ultimately is essential to ensure the success of a hub, does not exist in Dubai. Australia, which has only 18 million inhabitants, is the only continent where we do not fly because there is not enough volume of traffic. In fact, no one has ever built a hub in a place where there already is a hub, since the existing hub is a real deterrent. Chicago, which is the only city with two hubs, is no exception because the two hubs were built at the same time and not one after the other.

Budget airlines

Q. : *How is it possible to resist the onslaught of budget airlines ?*

P.-H. G. : We do better on the 'good' routes. On the Geneva-Paris route three years ago, Swissair offered six daily flights, Air France ten, and EasyJet four. Today, Swissair no longer operates this route, EasyJet only has three daily flights and Air France has eleven. Why ? EasyJet passengers and Swissair passengers (whose hub is Zurich) do not take a long-haul flight connection to Paris, whereas 60 % of our passengers do, and this covers the cost of half the aeroplane. For example, a person living in Geneva who wants to save money by buying an EasyJet flight to Paris (because it is the cheapest fare at 50 Euros) in order to catch an Air France flight to San Francisco (at a cost of 1,500 Euros), would therefore pay a total of 1,550 Euros. However, an Air France Geneva-CDG-San Francisco flight will only cost him 1,200 Euros. This is how we do business. Because, with us, the connection is free, the passenger cannot be ensnared by the budget airline.

However, budget airlines are formidable on short-haul flights : EasyJet managed to oust Swissair from the Paris-Geneva route. However, they will not be able to win every time. For example, on the Paris-Marseille flight, we saw off EasyJet which pulled out because the TGV

train fare is less expensive than their fare, especially if bought a few days prior to the departure date. Our 25 flights have such a positive effect that we managed to get all the business class clientele. EasyJet, with its four daily flights, was a non-starter.

Q. : *What will be your long-term strategy if the railways become privatised ?*

P.-H. G. : Our activity at Orly is in direct competition with the TGV. However, we benefit from a large market which allows us to stand up to the competition. Any large French company needs to travel both within France and internationally. The volume of travel may be such that we agree to reduce our fares substantially. If the company does not think that the reduction we propose is sufficient, there is no contract. The only option left to such a company is to negotiate with other airlines for its international flights, but the company will not then benefit from our reduced domestic fares. This is the reason that we now see airlines rethinking their strategy. Our presence in the domestic network weighs in our favour with passengers by these companies or private individuals who have chosen the Flying Blue frequent flyer programme. For this reason, we have a very precious share in the French market. If the TGV keeps growing and if the routes become open to competition, why not consider buying it ? This is a very long-term idea which may become a reality. When Jean-Cyril Spinetta said that one day we might have TGVs with the Air France flag painted on them, this made the headlines in all the newspapers.

Why such success ?

Q. : *I am confused, having heard you speak, because I was looking for a specific explanation for Air France's success, whereas what I have heard is the common sense explanation which applies to other companies. I get the feeling that there was a major turning point when Christian Blanc arrived at Air France. But was his arrival its cause or its consequence ? With what should we credit Jean-Cyril Spinetta ? Is he himself a cause or a consequence ? One wonders how long this happy situation will last.*

P.-H. G. : Broadly speaking, the facts were as follows : Air France was going through a crisis. Christian Blanc was called to the rescue. He understood how to get out of the crisis, avoided a catastrophe, and outlined his conditions, which included a refusal to lay off employees, to the government. He asked for financial aid worth 20 billion Francs (roughly 3 billion Euros) and a third runway at Roissy. At Air France, the morale of the employees was low. He turned this around and gave top priority to discussion. Christian Blanc managed to get us out of the crisis. Jean-Cyril Spinetta then managed our development. Today, Air France employees are clearly much more motivated than those of other airlines because they understand Air France's strategy and have confidence in Air France's capacity to purchase more aeroplanes and therefore to buy the future. Our system of delegation gives them a sense of responsibility. Passengers notice their motivation and interpret it as a sign of the company's good health.

The threats

Q. : *How do you manage to deal robustly with external factors such as the increase in the price of oil, the threat to include transport in carbon dioxide quotas, and the reactions of local residents who have to suffer the problems associated with air traffic ?*

P.-H. G. : When oil prices increase, budget airlines are most affected because the increase reduces the percentage of their price differential. Because Air France-KLM is already capable of withstanding oil price increases, it would be a great deal easier if this percentage was reduced. With regard to oil reserves, not only would the airlines be the last ones to need oil, but the pessimistic forecasts concerning the depletion of resources in the medium term is not borne out, if only because the increase in the price of oil pays for the increase due to the exploitation costs of resources.

Aircraft manufacturers are now producing aeroplanes which use less petrol and emit less carbon dioxide. As a result, Air France, which can renew its stock of new aeroplanes, is already going in the right direction with regard to these reductions.

Hubs allow the use of large aeroplanes rather than many smaller ones. It is best to solve the problems of the environment as best one can using an existing hub which may expand, rather than reproduce these problems elsewhere with new airports. The hub is not only profitable, but it is also globally efficient.

Q. : *What, then, are the problems which are likely to worry you ?*

P.-H. G. : Internal problems such as the malfunctioning of the infrastructure, (but we are heading in the right direction), disputes arising between Air France and KLM, (but we are constantly vigilant), or the problems of competition such as the development of very low cost Chinese or Indian airlines, although we could become partners or even owners of one of these airlines. A real problem – but a long-term one – would be if Europe were to lose its leadership in the international air transport sector to the Gulf countries.

Presentation of the speaker :

Pierre-Henri Gourgeon : From 1990 to 1993, he was the managing director of French civil aviation (*Direction Générale de l'Aviation Civile*). In 1993, he began his career at Air France and was chairman and managing director of Servair (catering and airport management) until 1996. From 1996 to 1997, he was chairman and managing director of Esterel (electronics distribution). He became president of Amadeus France in 1997 and president of the board of directors of Amadeus International in September 1997. He was appointed assistant general manager in charge of development and international affairs from 1997 to 1998. He has been executive managing director of Air France since 1998.

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