



**TRAFIKFLYGHÖGSKOLAN**  
Lunds universitet

## **Too many ducks in one pond**

**– a study of the Swedish domestic airline industry and its prospects –**

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## Summary

This report is intended to outline the domestic airline industry in terms of capacity and forecasts, and to analyse the financial condition and prospects of its operators. The outcome of the study has been severely impaired by the insufficiency of information supplied by airlines, which has rendered the report more indicative than was initially my intention.

The domestic airline industry, after suffering from post 9/11 turmoil, has recuperated well and generated a 3.4% annual growth during the first 8 months of this year. Considering economic growth forecasts as well as estimations made by LFV, the domestic air travel market is expected to grow at around 3% in the short term. This growth will however be far from sufficient to bridge the vast gap between industry capacity and utilisation. With an average industry cabin factor of roughly 60% during the first 6 months of this year, an approximate two million seats were unoccupied during the period. It is clear that this overcapacity must be corrected, and while doing so most airlines are suffering.

SAS, benefiting from the advantage of being the Swedish Goliath, is expected to turn its recurring negative result around as its restructuring is coming into effect. In the meantime SAS is able to endure the turbulence with its comparatively solid funds.

Malmö Aviation is the only airline that has published a first half (2005) close to break-even result. Fleet reductions as well as renegotiated salaries in combination with financial streamlining have enabled, on a relative base, an impressive six-month period. Taking this positive performance in combination with an adequate wallet, Malmö Aviation appears to be at least a short to medium term survivor.

Skyways future appears somewhat clouded as no traffic information or other statistical data is obtainable, and what has been happening during the first part of 2005 is unknown to the public. In 2004 however, the airline reported a significant loss compared to an industry rare profit in 2003. By the end of 2004 Skyways available funds did not look impressive, and unless the bad performance has been turned around, the company could be heading for potential troubles eventually leading to a call for a cash infusion.

Skyways is the only one of the five major airlines not to fly on the more important domestic routes. This could possibly pose a threat if other airlines experiencing grander economies of scale decided to enter into Skyways' turf.

Due to lack of financial data, not much can be noted about flynordic, apart from the occasional cries of delight in the media by the CEO. According to the company, flynordic is the fastest growing Swedish operator and generated a 73% cabin factor during the first half of 2005. flynordic has also got a steady cash book to lean upon in the owner Finnair, which purchased the company in 2003.

FlyMe looks to be in a very vulnerable position. With a cash burn rate of around SEK10mn a month during the first six months of the year, and with only SEK44mn of funds left at the end of June, its survival is seemingly hanging onto a loose thread. The airline has already raised new funds twice during 2004, but has since commencing its operation never managed to report a profit. Since FlyMe is running out of money fast and most probably not able to raise new funds, it is heading for bankruptcy. It is likely that this takes place before the end of this year.

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## **1. Introduction**

Following the introduction of the “no-frills” airlines, a number of new competitors have been established in the Swedish market over the past few years. Today, around 15 airlines fly domestic passengers with an abundance of capacity, rendering the market a seemingly much too congested place.

Despite signs of health, such as this year’s so far 3.5% growth in domestic travel<sup>1</sup>, the industry has not entirely recuperated from its latest crash post 9/11. In addition, margins are shrinking and the need to boost the cabin factor is becoming more important than ever before.

The likelihood of fewer airlines servicing the well-trafficked routes grows as competition becomes fiercer. The majority of the major Swedish carriers<sup>2</sup> reported officially or informally a net loss in the first half of 2005 (flynnordic’s results are not broken out of Finnair’s consolidated results and Skyways only report on an annual basis, which render this statement inapplicable to these airlines). Although these companies claim they are about to turn red numbers into black, margins seems unlikely to widen and it remains to see if costs can really be reduced to desirable levels. In any event, as costs are being cut, strong competition nurtures price war which in its extension may serve to keep new entrants out of the market place. Threat of new entrants has been suggested to for example take the shape of Ryan Air. The question is, given overcapacity and price wars, which ducks are the most likely survivors as the water level in the Swedish air industry pond has sunk into mud.

## **2. Purpose**

As suggested in the introduction section, the purpose of this report is to chart the domestic airlines’ playing ground in terms of industry capacity and forecasts, and the financial condition and prospects of operators. Although the intention is not to firmly determine each airline’s fate or doom, this is an attempt to come to a reasonable conclusion as to which operators are more and which are less likely to survive the toughening competition in the market.

## **3. Limitations**

The major limitation to this study is the shortage of company specific information. flynnordic does not disclose any financial statements as these are consolidated into Finnair’s. Skyways results can be found on an annual basis but give no information or even indication of traffic statistics. Thus to make forecasts of these two companies cannot be made to any degree of accuracy. I have however discussed also these companies to the extent I have found feasible. Another vital limitation when trying to examine the domestic market is the mixture of domestic and international operations in published information.

## **4. Methodology**

Despite the impediments presented by above mentioned limitations, I believe that I have still managed to create a fairly good overview of the industry and its dynamics, and of the companies operating therein. The first step was to plough through what financial information

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<sup>1</sup> Luftfartsverket. “Utförligare flygplatsstatistik”. 1997-2005

<sup>2</sup> This report examines issues of competition concerning the largest airlines trafficking the busiest routes: SAS, Malmö Aviation, flynnordic, Skyways and FlyMe

that was available in terms of annual and interim reports. I scanned the net for fact sites and articles on each of the airlines. Finally I contacted each of the airlines to see what further information they were willing to omit. A lot of the statistical information presented in graphs has also been altered, but is based on the sources specified.

#### **4.1. Limiting the study**

I have opted to examine only five carriers in the study. I have excluded smaller airlines, such as for example Direktflyg, and Swedline, due to few passengers transported and/ or because these companies do not traffic the more important routes. Others, such as Gotlandsflyg (and Kullaflyg) operate routes which experience a considerable degree of competition. Although these companies have contributed greatly to domestic competition and ticket price reductions, they operate too few routes and will for that reason not be included in the study.

In addition, the smaller airlines do not generally disclose any financial information which makes them more difficult to examine. In my opinion however, to exclude these companies does not impact significantly on the outcome of this study considering the vast market share of the largest five airlines.

### **5. Results**

In this section, the majority of my findings are presented. I have chosen to look at only the short term findings of the industry and companies I have selected due to the very dynamic nature of the environment in which they operate.

#### **5.1. General outline of the domestic airline industry**

Findings regarding industry trends have been obtained mainly from LFV statistics but restructured to fit this study. In general it shows the significance of the major airports and point to an overall positive growth trend in the Swedish market.

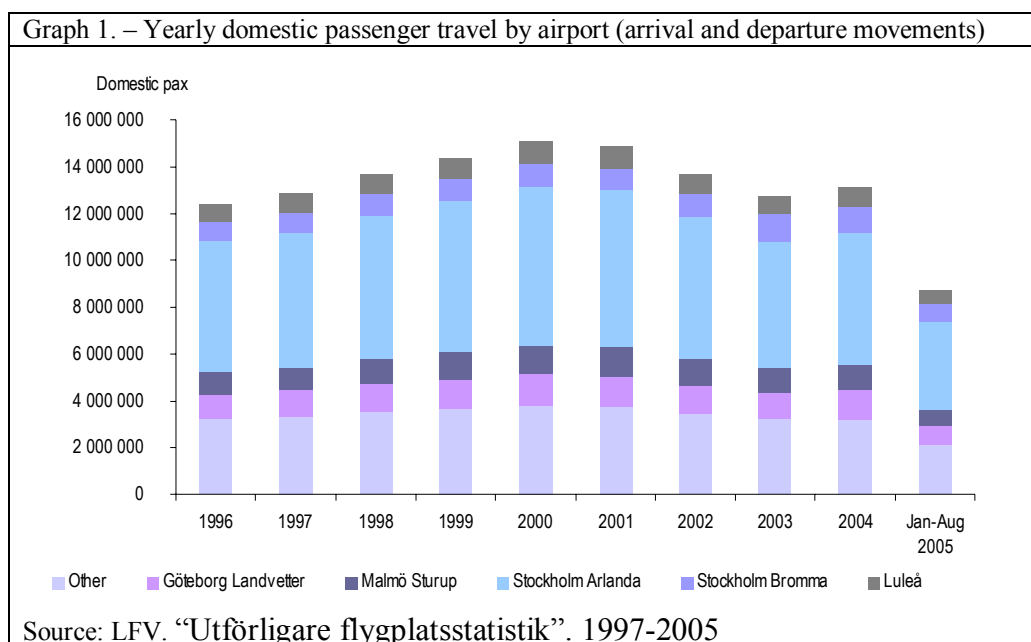
##### **5.1.1. Swedish domestic air passenger movement**

As has been previously mentioned, there are around 15 airlines of various sizes operating the Swedish domestic air passenger market. The five largest operators together cover around 30 destinations, leaving less than 10 smaller airports (trafficked by the smaller companies) unattended<sup>3</sup>.

The 5 heaviest trafficked airports; Arlanda, Bromma, Landvetter, Sturup and Luleå, facilitate approximately 75% of all domestic air travel. When adding Sundsvall/ Härnösand and Umeå to the “big five”, roughly 85% of intra-Swedish air transport is accounted for. Arlanda is not surprisingly the dominant airport, and account for about 45% of total domestic passenger travel. (Luftfartsverket. “Utförligare flygplatsstatistik”. 1997-2005)

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<sup>3</sup> According to information on a number of airlines’ webpages

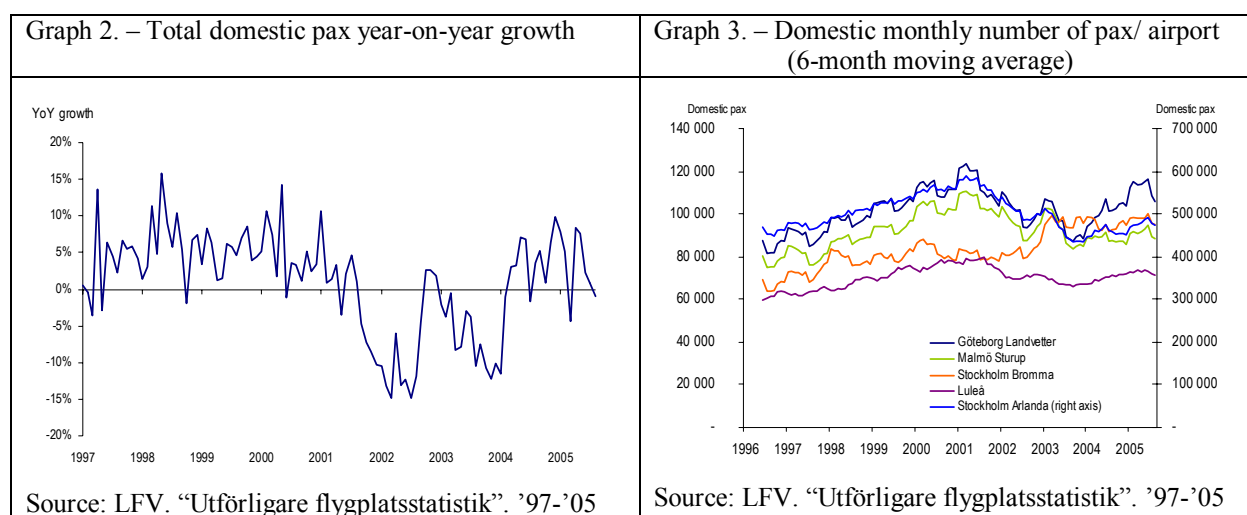


Considering the volumes running through the largest 5-7 airports, it may be argued that in order to generate economies of scale (on a relative basis), the domestic airline need to be present at and operate routes between at least a few of these airports. If this assumption holds true, it also validates the selection of airlines made as the most appropriate for this study.

### 5.1.2. Domestic travel trends

The trend in graph 2 below shows growth in domestic travel on a yearly basis. It is well known that the industry fell into negative growth post 9/11, but perhaps the fact that full growth recuperation was not ascertained until 2004 may not be widely recognised. Although this year has shown an overall positive growth trend, domestic travel is still not at levels experienced during late 90's and early 00's.

Graph 3 shows yearly growth per month and airport on a 6-monthly moving average (in an attempt to eliminate the strong seasonal effects of passenger travel). The “Big 5” demonstrate trends similar to each other, with the exception of Bromma which show a significant upswing during 2002. The overall domestic market grew at a 3.4% rate up until August 2005. (Luftfartsverket. “Utförligare flygplatsstatistik”. 1997-2005)

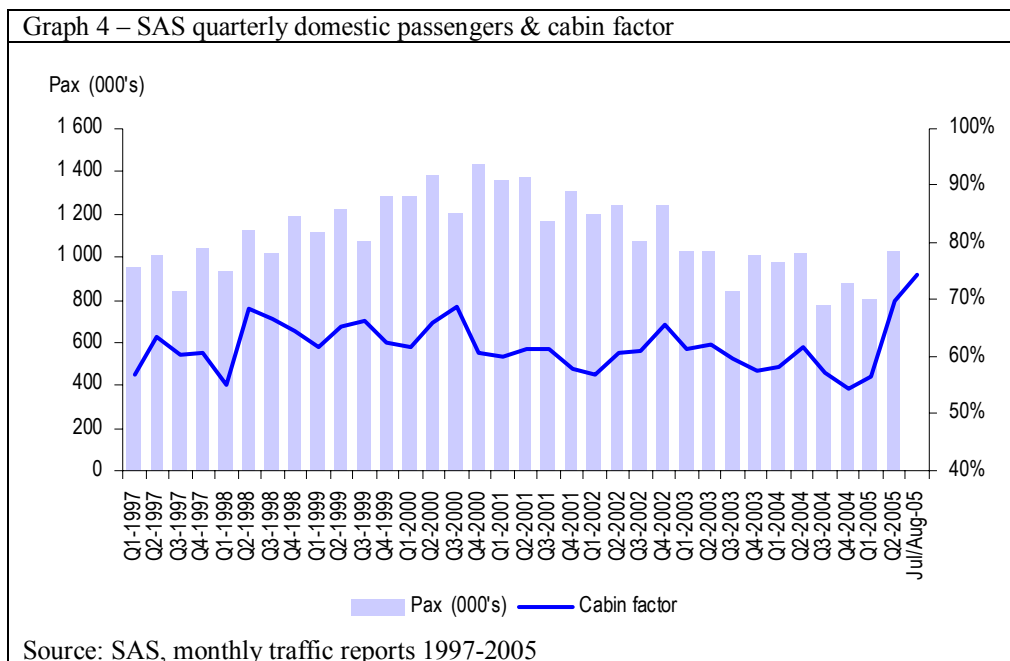


## 5.2. The airlines and their performance

It should be noted that in regards to examining the domestic passenger travel, some level of inconsistency is an unfortunate feature of this analysis. Statistics of international flights (i.e. domestic-to-international destination routes) is sometimes treated as domestic travel data.

### 5.2.1. Scandinavian Airlines – focus on boosting cabin factor

With its close to 65-70% market share (April to July 2005)<sup>4</sup> in domestic air travel, SAS continues to dominate the Swedish market. Following recent years' toughening competition and market overcapacity, SAS has reduced its ASK (available seat kilometre) in order to improve its overall cabin factor<sup>5</sup>. SAS cut its domestic capacity (ASK) back in 1H-05 (1<sup>st</sup> half 2005) by 29% compared to 1H-02. For the months July/ August this year the cabin factor rose to an average 74% from 60% in the same period the previous year, solely as an effect of a 20% reduction in capacity.



In addition to reducing capacity on Swedish domestic routes, SAS has introduced “one-way pricing” and argues that this is the foremost reason behind the increase in cabin factor since April this year. It is however worth mentioning that the volume of passengers increased by less than one percent compared to April-August the previous year.

On a grander scale, SAS continues its restructuring program, “Turnaround 2005”, throughout this year, and management expects the initiative will generate further savings through improved productivity and cost efficiency. Operating costs related to domestic air travel are as a result also expected to come down, allowing for improvements in its so far negative result. (SAS Annual report. 2004 and 2005). So far this year SAS reported losses both in the first and second quarter of SEK61mn and SEK219mn respectively.<sup>6</sup>

<sup>4</sup> SAS Analyst material Q2-05

<sup>5</sup> Cabin factor or load factor = RPK/ ASK

<sup>6</sup> SAS Quarterly report. Q2-05

### 5.2.2. Malmö Aviation – best in class?

After a shaky mid 90's, the Braathens family bought Malmö Aviation (MA) for 1 Swedish Krona in 1998<sup>7</sup>. The company has since consolidated its position in the domestic market as one of the most prominent airlines.

Following half a decade of consistent losses, MA this June announced a loss of only SEK4mn during the first half of the year compared to a SEK34mn loss for the same period last year.<sup>8</sup>

The close to break-even result was generated in spite of income falling by SEK50mn year-on-year in 1H-05, as a consequence of shrinking the fleet from 11 to 9 aircrafts.<sup>9</sup>

This above class average result was generated despite a cabin factor of 57% which was only 4%-points above that of previous year's factor.<sup>4</sup> What appears to be the main reason behind MA's turnaround is that cost savings are taking effect. The company negotiated at the end of last-, beginning of this year a 30% reduction in leasing costs for its nine Avro RJ 100. In March 2005, MA announced a savings package designed to lower costs by approximately SEK70mn, corresponding to more than 10% of total income.<sup>10</sup> The main reductions were made through cutting back wages, which allowed for instant effects. In June the next package reducing costs by SEK40mn was presented, which is expected to take full effect in 2006.<sup>8</sup>

### 5.2.3. Skyways – focus on low traffic destinations

Skyways flies on 16 domestic and 5 international routes.<sup>11</sup> The airline has focused primarily on less heavily trafficked routes as it is partly owned by and in partnership with SAS. Despite both companies being present in the Swedish domestic market, this March was the first time the two airlines openly began competing on the same route: Arlanda-Skellefteå. In 2004, the airline transported a total of 1.2mn passengers, which qualified Skyways as the second largest Swedish airline in terms of carry.<sup>10</sup>

Skyways is also an unlisted company and publish close to nothing in terms of statistics and frequently recurring financial information. The company is hence in a similar fashion to flynnordic difficult to analyse.

Skyways' financial performance plummeted during 2004 to a SEK65mn loss. This compares to an operating profit of SEK32mn in the previous year. Skyways is obviously experiencing the same turmoil as other airlines operating the Swedish market, but it may be worth mentioning that the number of passengers carried also fell 11% between 2003 and 2004. There is no further financial information for 2005 available.<sup>12</sup>

As a result of the poor performance in 2004, Skyways decided to reduce the number of employees by 40% (~300 employees) and to degrade roughly 20 captains to co-pilots. In addition, the company has been discharging half its fleet (implying all aircraft of type Saab-340 and Embraer-145) to retain only 17 Fokker-50s.<sup>11</sup>

### 5.2.4. flynnordic – fastest grower

It is virtually impossible to make predictions regarding the future of flynnordic considering the diminutive level of information published by the owner Finnair. Given flynnordic's significance as an important part of Swedish domestic air travel industry, it is however

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<sup>7</sup> <http://www.malmoaviation.se>

<sup>8</sup> Dagens Industri, Hedensjö, Björn, “Kapade kostnader rätt väg för Malmö Aviation”. 2005-08-31

<sup>9</sup> Malmö Aviation webpage. Press release. 2005-08-31

<sup>10</sup> Dagens Industri, Gianuzzi, Mikael, “Braathen-arvtagaren: Jag skulle aldrig köpa aktier i ett flygbolag”. 2005-07-19

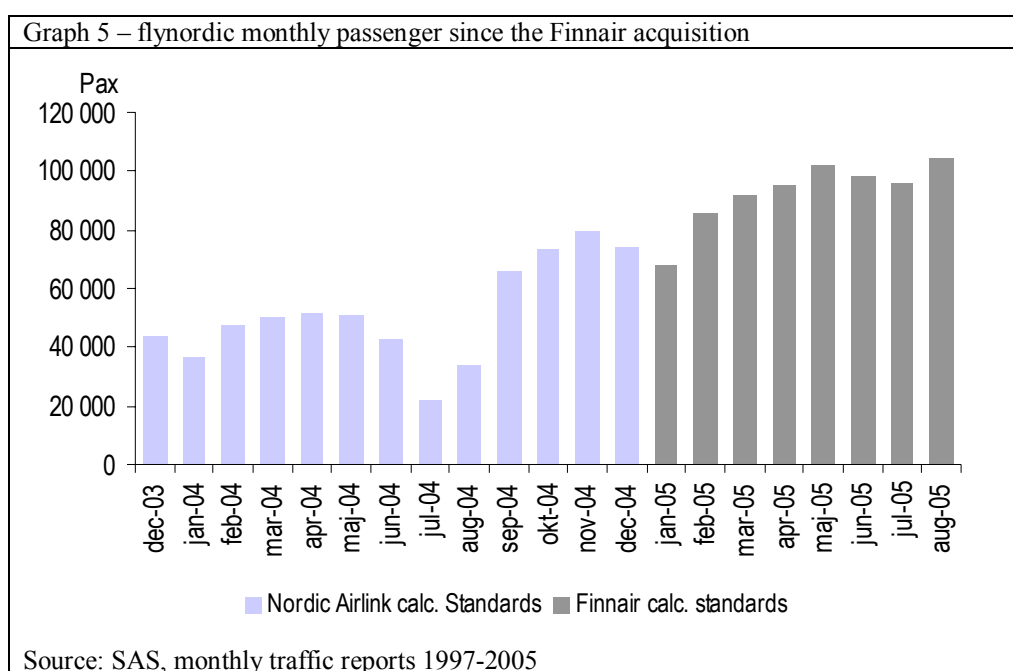
<sup>11</sup> <http://www.skyways.se/>

<sup>12</sup> Dagens Industri, “Brakförlust för Skyways”. 2005-08-05



necessary to comment on its establishment and later in this study try to come to some suggestive conclusions.

flynordic was bought in 2003 by Finnair who wanted to establish themselves in the Swedish and Nordic no-frills airline industry.<sup>13</sup> Prior to Finnair’s involvement, flynordic had been flying under the name Nordic Airlink between Arlanda and Luleå. The company currently operates seven MD-80s with which it this year has managed to generate a ~73% cabin factor.<sup>14</sup> Following the acquisition, the company expanded to include routes to Gothenburg, Umeå, Oslo and Copenhagen. When comparing the first 8 months of 2005 to the same period in 2004, the company shows a growth rate of more than 100%<sup>15</sup>. flynordic claim to be the fastest growing company with around 100,000 passengers in around 200 departures per month. The company has a strong international engagement, and co-fly to several destinations with Sterling.<sup>12</sup>



#### 5.2.5. FlyMe – Below minima?

As FlyMe entered the market in March 2004, it chose to compete as a low-cost carrier on the most challenging routes. FlyMe initiated the routes from Arlanda to Gothenburg, Malmö and Helsingfors, and has added Östersund to its list of destinations. On the routes Gothenburg-Arlanda and Arlanda-Malmö, FlyMe attained a 23% and 34% market share in the second quarter this year.<sup>16</sup> The planned opening of a route to London earlier in 2005 year has been postponed.

Since commencing operation, FlyMe has not yet reported a single quarter in black numbers. The average quarterly loss for the six full quarters in service has been roughly SEK30mn.<sup>17</sup> While operating the busiest routes and offering the lowest priced tickets (note that average

<sup>13</sup> <http://www.flynordic.com/showMainContent.do?pageName=about>

<sup>14</sup> Flynordic webpage. Press release. 2005-08-11

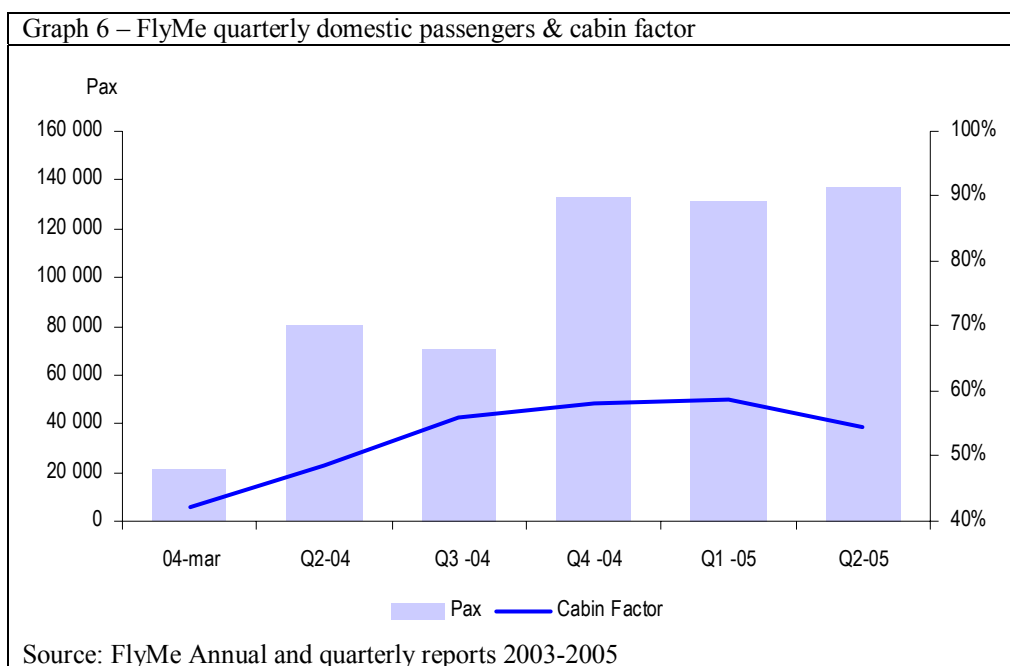
<sup>15</sup> Finnair monthly traffic report. Note that the comparing periods use different calculation standards, but in exact comparison, the growth between two periods is 121% and >100% is thus an equitable statement.

<sup>16</sup> FlyMe Quarterly report. Q2-05

<sup>17</sup> FlyMe Annual report 2004 and Quarterly report Q2-05

ticket prices are unknown, but according to LFV, FlyMe tender the lowest rates)<sup>18</sup>, FlyMe lost on average SEK220 per ticket during the first half of 2005.

The company anticipated a 2005 full-year SEK56mn loss, but reported a SEK59.3mn negative result already by the end of June.<sup>19</sup> Although the acting CEO has stated that the second half of this year will be significantly better than the first, and that he expects that FlyMe will be reporting a profit already in Q1-06<sup>20</sup> (1<sup>st</sup> quarter 2006), it may be suspected that there are insufficient funds available to keep FlyMe’s fleet of four 737-300s in the air for that long.



## 6. Discussion

This section is concerned with my own conclusions and opinions. Conclusions are drawn on *available* information, and given the general scarcity of statistics and financial data, not necessarily on the *best* information.

### 6.1. Operating the Big 5 key to scale

Given the volume of passengers passing through the largest five airports, operating routes between these quite obviously give rise to improved economies of scale. Hence, in order to remain competitive in the longer term the domestic airline should arguably be present on at least a few of these. In the short term however, it appears feasible to be operating routes with lower levels of passengers, but only for as long as these are left unattended by companies experiencing greater economies of scale. Certainly, if the difference between the largest airports and the tier below were not so significant the argument would fail, but in Sweden that is not the case. Out of the airlines examined in this study, Skyways is the only carrier not to operate any of the more significant routes.

<sup>18</sup> Ahlgren, Mats. Luftfartsverket. Telephone interview 2005-08-30

<sup>19</sup> FlyMe Quarterly report. Q2-05

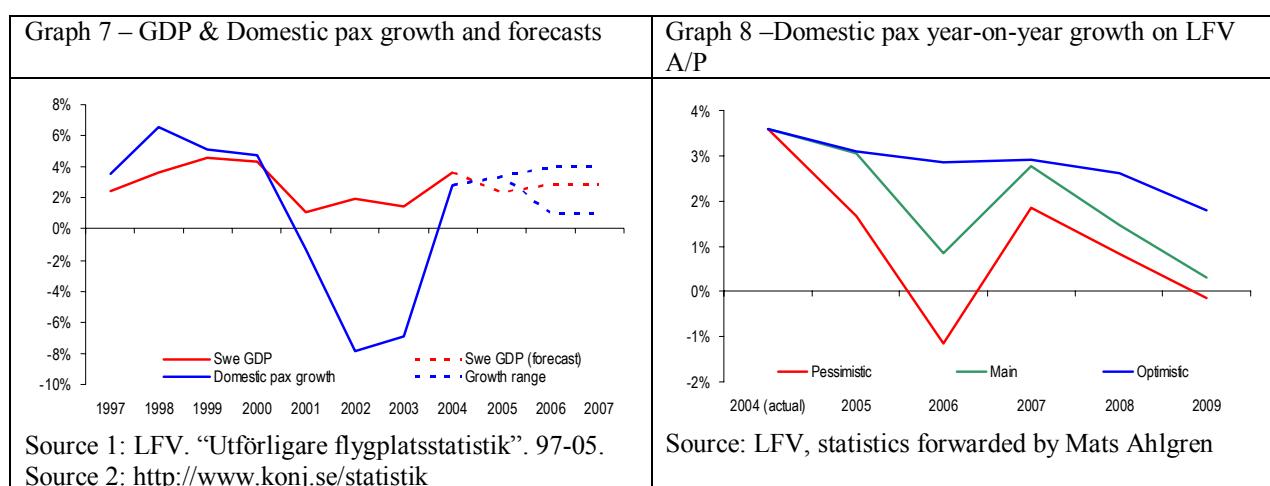
<sup>20</sup> Dagens Industri, "FlyMe Hoppas på vinst nästa år", 2005-08-12

## 6.2. Industry forecasts

There has been quite strong correlation between economic growth and growth in domestic passenger travel during the past decade. The correlation factor since 1997 is 0.75, which provide a reasonable foundation on which to base forecasts. Given the projected 2.9% GDP growth in 2006 and 2007<sup>21</sup>, to be compared with 2.4% (full year estimate) for 2005, it seems reasonable, given the fact that the immediate effects of recovery after 2001 is diminishing, to expect a domestic passenger growth of around 3% in 2006 and 2007.

It is unclear how the new environmental tax on tickets of approximately SEK70 per passenger and leg flown will impact the volume of travelling. For the cheaper tickets this will raise prices by around 20-40%. It is however unlikely that the new tax by itself will have a massive impact on travelling, given that in percentage terms for the vast majority of tickets the rise is not that significant.

A realistic range of growth, which takes the GDP growth correlation into account, would seem to be embraced within an optimistic upper limit of 4% and lower limit of 1%. The latter 1% make room for the possibility of slower economic growth and conceivably further rise in oil prices. The “positive” upper 4% border would bring domestic travel up to levels similar to the late 90’s, but still below 2000 and first half of 2001. In any event, whether in reality growth ends up at 1% or 4% will have fairly limited impact on the market given the acute level of overcapacity that the industry is experiencing, as discussed in the following section.



According to LFV’s projections, the passenger growth is likely to dip in 2006 followed by a stronger 2007.<sup>22</sup> The forecasts are however due to be amended following the new tax which was approved in the government’s last budget. LFV’s current forecasts are more or less in line with the GDP related outlook.

### 6.2.1. Over-capacity

The overcapacity in domestic air travel is evident in the low industry average cabin factor of somewhere just above 60%. This unutilised capacity left more than 2 million seats empty in the first six months of 2005 alone. Although, full capacity utilisation is unrealistic, it is clear that the industry is not behaving efficiently. And although growth is back on track, it would take 10 years at a 4% annual growth rate to get close to full capacity employment. Assuming

<sup>21</sup> <http://www.konj.se/statistik.4.302e67fd1ec1776c7fff1583.html>

<sup>22</sup> LFV, statistics forwarded by Mats Ahlgren

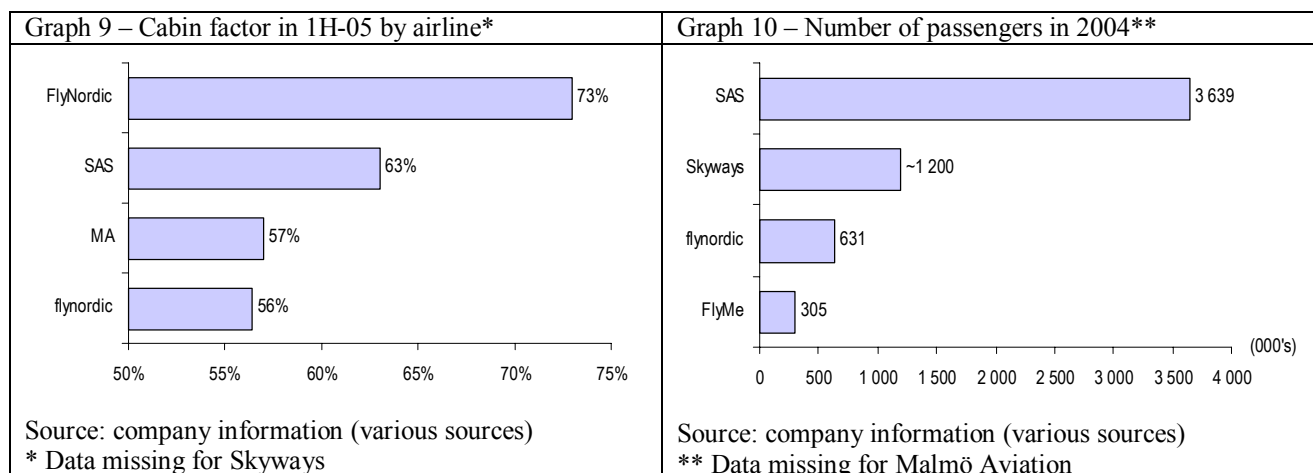
a 2% annual passenger growth, which seems more realistic longer term, it would take the market more than 20 years to close the gap between capacity and domestic travel demand. All of the domestic players, bar flynordic, have reduced their capacity during the last six months, but given the 75 000 empty seats per week during 2005 it does not seem likely that the market has yet approached an adequate level of efficiency.

The obvious reason is that no airline is willing to axe its own supply in favour of the whole market. Airlines contribute to meeting the existing total demand simply because they are forced to. This is never as apparent as when a highly competitive market also becomes a market in recession as has been the case subsequent to 9/11.

The conclusion, in any event, to be drawn is that the market growth will not to any greater extent bridge the discrepancy between capacity and demand. The gap as it is viewed by each individual airline, including SAS, is to either gain market share or retain existing passengers in combination with slashing capacity.

### 6.3. The airlines and market evolution

It is difficult to make any accurate comparisons of the domestic airlines, mainly due to the insufficiency of information, but also because most of them are going through streamlining which are problematical to evaluate. However, as was stated early, this study is only intended to give an overview of the industry and an indication of status and likely development of its members.



#### 6.3.1. Economies of scale benefactor, SAS, is the oldtimer here to stay

SAS, being the dominant domestic airline, is undergoing considerable restructuring in an effort to move more in line with low-cost carriers. The streamlining will continue at least throughout this year with effects and costs of redundancies being felt beyond the next. In spite of a cost base with legacies from a traditional airline, SAS no doubt is the greatest benefactor from economies of scale in the Swedish market. In addition, the company currently generates healthier levels of cabin factor, bar flynordic, than the rest of the market. This summer proved particularly good in this sense for SAS.

The toughening competition will probably in retrospect have been a very healthy influence on the Swedish Goliath, and which has awakened the company from its former monopolistic behaviour. The Nordic region and Sweden in particular remains key for SAS, and strategically it is unthinkable that the company would surrender these markets.

In terms of survival, the SAS group saw its unrestricted equity fall from SEK5.4bn to SEK4.4bn during the first six months of 2005.<sup>23</sup> The burn rate in terms of negative net income was SEK469mn for the whole group, and the Swedish contribution was a pre-tax loss of SEK280mn in 1H-05. In spite of the cash burn, the group's funds offer SAS a fair deal of leeway in terms retaining domestic requirements if need be.<sup>21</sup> Without extending the analysis beyond these considerations, SAS has comparatively deep pockets and will be able to endure more years of stiff competition and turmoil. Unless the company is being sold to another, and in such case probably foreign, airline, I firmly believe SAS will remain a survivor within the Swedish domestic airline industry.

### 6.3.2. Malmö Aviation is on the right track

Malmö Aviation's hammering on costs has paid off. As mentioned, already the first six months of this year almost generated break-even. With the possible exception of flynordic, MA certainly has proven to be best in class, and has to be deemed a very likely profit producer for the full year 2005.

The latest cost cutting measure, presented in June, will certainly render MA one of the most efficient domestic operators in terms of cost structure as judged from their 1H-05 result. MA is however lagging in terms of capacity utilisation, improving which would possibly guide the company into being the foremost Swedish carrier at any rate in the short term.

In terms of capital, MA also seems at least for the moment to be out of harm's way considering its unrestricted equity of more than SEK100mn<sup>24</sup>. The only possible question mark could be the Braathen family's suggested reluctance to make further investments, should MA due to continued market turmoil and/ or inability to match cost to income become short of funds.

In my opinion, MA has a comparatively stable foundation on which to continue its recent best in class improvement, and hence I deem the company as a very likely short to medium term survivor.

### 6.3.3. Uncertain for the niche operator Skyways

The secretive operation of Skyways leaves a lot to assumptions and imagination. What is clear however is that last year must be noted as a serious setback. After withstanding the turbulence that followed 9/11 relatively well and producing a profit in 2003, Skyways did suffer the unpredictable nature of the market in 2004.

Substantial cost cut backs and reducing the fleet to one type only will certainly put Skyways in a more competitive condition, but an important advantage currently enjoyed are the routes which Skyways operate. On the majority of these routes the level of competition is still lower and the company is more able to control prices. In spite of what has previously been discussed in terms of operating routes between larger airports, as long as Skyways in conjunction with a few other smaller airlines are permitted to fly undisturbed on such low passenger routes, it seems to make good business sense.

SAS has recently opted to start competing with its partner on one important route, and it is more than plausible that other domestic and perhaps also foreign airlines will commence flying on Skyways' so far unattended routes. In such case, Skyways will most probably suffer from not being present on the more important airways and face problems matching its cost base with the rest of the industry.

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<sup>23</sup> SAS Quarterly report. Q2-05

<sup>24</sup> Malmö Aviation Annual report. 2004

In addition to this scenario, which would imply an undeniable degree of uncertainty, Skyways low equity capital stock of SEK~29mn could fairly easy deplete. To what extent the company can boost its funds in a situation where it would be needed, is unknown. Consequently, for these reasons in my opinion, a shadow of uncertainty is cast on Skyways both in the short and medium term.

#### 6.3.4. Something must be done right in flynordic...

At least if you trust the sporadic media comments by the CEO, Maunu von Lüders, and the monthly cabin factor figures presented by Finnair. It is based on the limited information supplied by the company not possible to make any reasonable analysis regarding flynordic's current and future existence. However, if Finnair believe it makes strategic sense to keep a Nordic low-cost carrier and flynordic is indeed operating at a positive (or soon to be positive) result, there is no reason to believe that flynordic would be forced out any time soon. My “guess” is that flynordic in combination with the expansion of international routes also has arrived to stay.

#### 6.3.5. FlyMe is facing near-term dark skies

FlyMe appear to be on the brink of non-existence. With a burn rate of approximately SEK10mn per month during the first six months of this year and remaining equitable funds of only just north of SEK44mn<sup>25</sup>, doom seems near. Should FlyMe prove unable to change the trend, the company will run out of money around November-time.

It is plausible that one out of four possible outcomes will become reality already this year. The first possible scenario would be to reach break-even before running out of funds. Management stated in the Q2 report that the second half of this year will be significantly better than the first half, and that a profit will be generated sometime during the first quarter 2006. One should not disregard the fact, however, that the best quarter ever was Q1 this year during which almost SEK24mn was lost.<sup>26</sup> The inverted cost to income relationship has been present for as long as FlyMe has been in operation, and it does sound a little too optimistic to think that the new CEO can perform a smaller miracle and turn everything around at this very point in time. In my opinion, it does seem likely that the wallet will be emptied once more.

The second possible outcome is that FlyMe will be sold at or near scrap value. If there are any potential buyers around is an open question, but for a company which has never generated profits, desirable assets would most probably be of the intangible art. To the extent that FlyMe is a brand of value will not be addressed here.

The third thinkable scenario is another round of financial restructuring, implying new capital to be emitted. Since the initial instalment in which SEK60mn was contributed to create FlyMe in 2003, there have been two additional new share offerings of in total SEK183mn.<sup>27</sup> The first were made in June last year and the second in December. Considering that FlyMe in spite of additional capital has not been able to turn the company around, it does not bode well for yet another offering. In my opinion, since investors must have lost confidence in FlyMe, a new attempt to raise capital will probably fail.

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<sup>25</sup> FlyMe Quarterly report. Q2-05

<sup>26</sup> FlyMe Quarterly reports. Q4-03 to Q2-05

<sup>27</sup> <http://www.flyme.se/sv/omflyme>

This leads to the fourth and final possible outcome, which in my opinion is the most credible one, namely bankruptcy.

#### **6.4. Conclusion**

As a concluding summary can be said that the domestic air transport market is likely to grow at an above economy expansion. The domestic market is characterised by overcapacity to which the majority of airlines are adjusting.

flynordic aside, Malmö Aviation seem to be on the right track with effects of recent restructuring already visible. SAS is trying to retain its dominant position while streamlining its organisation. The continued existence of Skyways is arguably somewhat less certain than its competitors, and FlyMe seems to be heading for a near term ill-fated ending.

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