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AVIATION

Cathay finally realises benefits of budget airlines with deal

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It took the city's biggest airline 16 years to arrive at the conclusion that it needed a low-cost unit. Now, instead of starting from scratch, Cathay Pacific Airways has bought five-year old HK Express to keep pace with rivals in the budget sector.

Cathay joins a long list of established Asian airlines to bolt on a budget firm, following in the footsteps of Singapore Airlines, which set up Tigerair and Scoot, and Qantas with its Jetstar brand, as well as Japan's All Nippon Airways, which created low-fare units Vanilla Air and Peach.

But aviation analysts hold mixed views on whether the city's flagship airline will benefit significantly from the acquisition deal announced yesterday.

CAPA Centre for Aviation chief analyst Brendan Sobie said Cathay would be able to take the fight to its regional competitors but gaining control of a rival airline was only one part of the solution.

"Purchasing an LCC [low-cost carrier] will not be a solution for a lot of the issues Cathay faces, and these will still need to be resolved as part of a new wider strategy that is emerging," he said. "However, taking on HK Express strategically is the right move and should improve its long-term position in an extremely competitive and challenging market."

But Kelvin Lau, head of auto, transportation and industrial research at Daiwa Capital Markets, doubted the no-frills model would work in an increasingly expensive and substantial airport such as Hong Kong's.

"I think they do have many expertise in the aviation industry but whether Hong Kong is a place to run [a budget carrier] is not one they can control, because it is a high-cost place for an airline to start up," Lau said.

Cathay would need to tinker with the business model to enable it to turn a profit, he added.

Successive Cathay executives previously repeatedly mulled, studied but ultimately failed to see the merits of launching a home-grown no-frills airline.

In the earliest conclusions made by the airline in 2003 – at the time arch-rival Singapore Airlines founded Tigerair – a review showed it feared a customer backlash and was keen to protect the brand's premium image.

These views hardened over time as Cathay believed it could compete with budget carriers using larger aircraft while packing twice as many passengers in.

Chairman John Slosar told university students in a speech last year that the debate boiled down to costs. "Flying a big wide-body aeroplane with lots of passengers on it rather than a single-aisle plane, I would definitely have lower costs than any low-cost airline for sure," Slosar said.

People involved in the company's numerous reviews of low-cost carriers said no action had been taken because it did not believe there was a dedicated market for a no-frills firm. Cathay instead believed some customers wanted cheap fares and would be willing to forgo things such as luggage allowances and free seat selections, according to sources who were not authorised to be named.

16

Number of years since Cathay Pacific concluded in 2003 that it feared a customer backlash and was keen to protect its premium image

The threat posed by low-cost airlines by the time HK Express became the city's first budget carrier in 2013 thrust Cathay into the spotlight. It vigorously opposed the creation of Jetstar Hong Kong, which regulators in 2015 refused permission to fly.

Dr Law Cheung-kwok, aviation policy chief at Chinese University, said the government had "good intentions" to establish more local airlines, but had failed. Dragonair was taken over by Cathay in 2006 and became Cathay Dragon, while Oasis Hong Kong collapsed in 2008.

Hong Kong Airlines currently faces an uncertain future as it attempts to restructure to stave off financial difficulties.

Cathay CEO Rupert Hogg last summer underscored the company's softening stance, saying the airline would only launch a budget carrier "if and when" it felt cheaper travel could turn a profit.

The financial distress of HNA Group – parent of HK Airlines – has now presented Cathay with an irresistible opportunity to mould an established budget airline without the years of spending and growing one from scratch.

Yet Cathay had signalled it would wait until 2024 for such a move, when a third runway would mean a boom in opportunities in the sector. As competition swelled on multiple fronts, Cathay had to further cut its fares to maintain market share.

Achim Czerny, an associate professor in aviation management at Polytechnic University, said the deal was the right thing for the airline as it could not wait for the extra runway. He predicted more budget airlines would have arrived in the city by then.

"Entering the budget airline space will help Cathay Pacific maintain a strong market position," the scholar said.