

Alitalia's network benefits from Etihad partnership. Time now to shed the dependency culture

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29-Apr-2016



Since Etihad's Dec-2014 investment in a 49% stake in Alitalia the Italian airline has enjoyed much positive change. It has worked to move its brand and product more upmarket to differentiate itself from fierce LCC competition in Italy, where Ryanair is the biggest airline by seats.

Alitalia's long haul offering has benefited from its partnership with Etihad. This has mainly been due to codeshare access to a much wider range of destinations in the Middle East and Asia Pacific. However, this summer's launch of a Rome-Beijing service indicates growing self-confidence too. Alitalia has also shown renewed confidence by growing its small niche to Latin America, the main region where it takes the lead over Etihad. On short/medium haul the LCCs still provide a strong challenge, although Alitalia's European offering has been fortified by closer commercial ties with other Etihad investments (in particular airberlin).

However, Alitalia continues to be loss-making (to the tune of EUR199 million in 2015). This is a hard continuing habit to kick, even if the airline still insists that it will break the habit in 2017. The rest of the industry is collectively experiencing record profitability in 2016; an airline that cannot be profitable in such conditions still has much work to do.

Rome is Alitalia's main hub

Since the investment by Etihad in Dec-2014, and Alitalia's relaunch under a new strategy at the start of 2015, the Italian airline's network has been built on three hubs: Rome Fiumicino, Milan Linate and Milan Malpensa.

By far the biggest of these is Rome Fiumicino, where Alitalia has approximately three times the weekly seat capacity that it has at Milan Linate. Rome is not only the base for many of Alitalia's largest domestic routes, but also the hub for most of its largest international and intercontinental routes.

Fiumicino has been the main focus for Alitalia's new long haul routes since the Etihad investment. It is also a highly competitive battleground for many of Europe's leading LCCs.

See related report: Rome Fiumicino Airport: Vueling, Ryanair, easyJet and Alitalia are locked in mortal combat

Linate is a foothold in the business-focused Milan market; Malpensa is a niche long haul base

Milan Linate is an important foothold for Alitalia in the more business-focused Milan market. Its focus here is European destinations, in particular connecting with the hubs of partner airlines. However, it also serves a number of seasonal leisure destinations from Linate.

At its third hub, Milan Malpensa, Alitalia has less capacity than at the other two. Malpensa, where easyJet is the leading airline by seats, acts as Alitalia's base in Northern Italy for some important long haul routes that are also served from Rome. These are Abu Dhabi (launched after the Etihad investment), Tokyo and New York.

In terms of seat capacity, Malpensa ranks as Alitalia's sixth largest base behind its two large hubs and the island-based cities of Catania, Palermo and Cagliari.

Alitalia has had a new CEO since 7-Mar-2016

The management of Alitalia at the very highest level has undergone two changes since Jan-2015. The previous CEO, Silvano Cassano, stepped down in Sep-2015 after only a year in the job, and the post was temporarily filled by the chairman, Luca di Montezemolo, until a permanent successor was found.

In Dec-2015 Alitalia announced that its new CEO would be Cramer Ball, although his appointment only took effect on 7-Mar-2016. He has experience of leading loss-making airlines in which Etihad owns an equity stake, having previously served as CEO of Jet Airways (24% owned by Etihad) and Air Seychelles (40% owned by Etihad).

During Mr Ball's tenure at Jet, which he joined in Sep-2014, there was a narrowing of losses in FY2015 (year to March) and the airline is expected to report a return to profit in FY2016, although he left just before the end of the financial year. At Air Seychelles, Mr Ball oversaw a return to profit in 2012 and 2013.

Mr Ball is an Australian national; his early career included spells at both Ansett and Qantas before he took up a number of roles for Etihad in Australia, New Zealand and Thailand.

Losses continue; profit target for 2017

According to CAPA research, Alitalia has not reported a profit this century

Alitalia has undergone a number of reorganisations and changes of holding structure over the years, but none of its incarnations has been profitable for many years. According to CAPA research, Alitalia has not reported a profit this century.

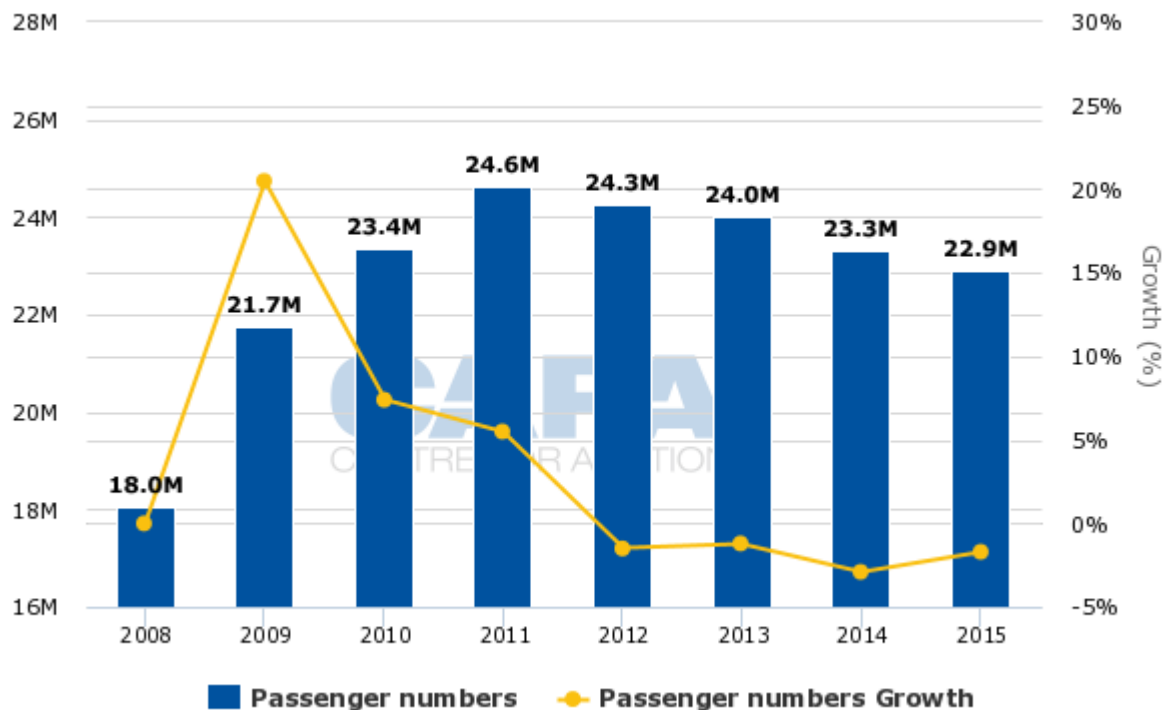
On 1-Jan-2015, the business was transferred into a new company, Alitalia - Società Aerea Italiana S.p.A. (Alitalia SAI), with a plan to record a profit in 2017. It is in this new entity that Etihad took a 49% stake for EUR387.5 million.

On 29-Apr-2016, Alitalia SAI reported a EUR199 million net loss for 2015, narrower than the consolidated net loss of EUR578 million reported by the previous entity Alitalia - Compagnia Aerea Italiana S.p.A. for the year 2014. Alitalia also reiterated that it remained on schedule to become profitable by 2017 under its three year plan.

Annual passenger numbers have fallen every year since 2011

According to Alitalia's corporate website it carried 22.9 million passengers in 2015, a reduction of 1.7% from 2014. Passenger numbers have fallen modestly every year since a peak of 24.6 million in 2011. In the three years prior to that (from 2008 to 2011) passenger numbers had experienced strong growth of 37%.

Alitalia passenger numbers and annual change in passenger numbers 2008 to 2015



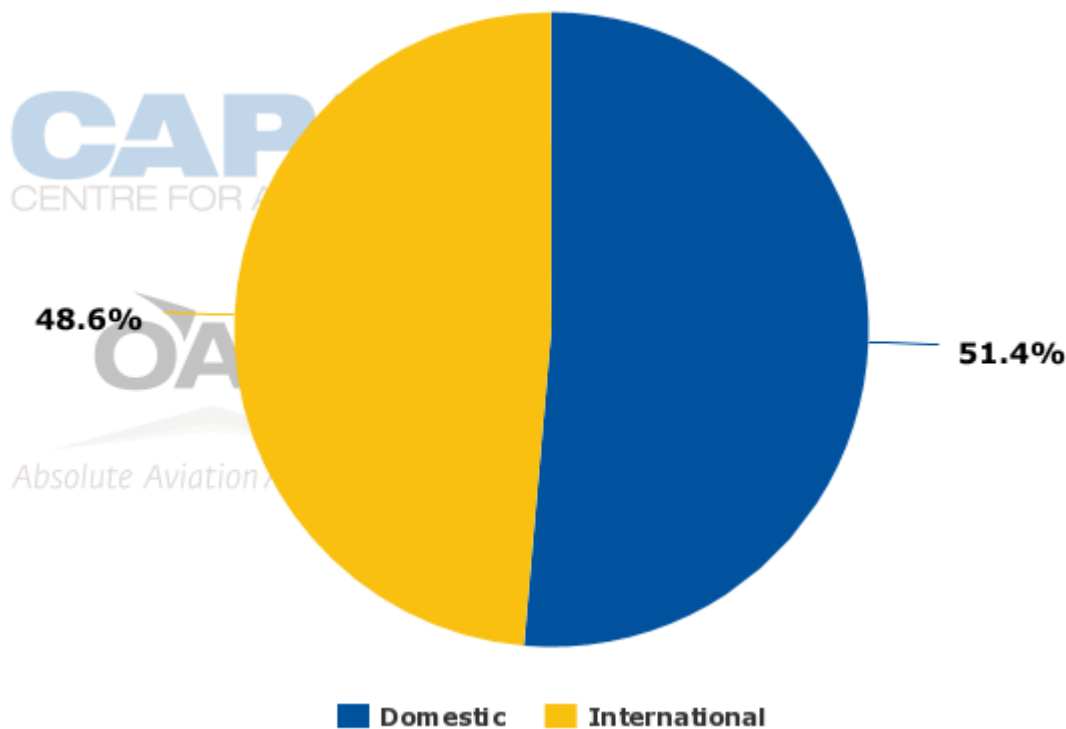
Source: CAPA - Centre for Aviation, AEA and airline reports

Alitalia's network strongly biased towards domestic routes

Alitalia's network has a strong domestic bias, with 51% of seats for the week of 25-Apr-2016 operated on routes within Italy. It has 41 domestic routes out of a total of 122 on its network.

As the summer season ramps up towards its peak, the proportion of domestic seats will increase to 54% of Alitalia's total in the week of 11-Jul-2016, when 47 out of its 135 routes will be domestic (data source: OAG).

Alitalia international vs domestic seat capacity 25-Apr-2016 to 1-May-2016



Source: CAPA - Centre for Aviation and OAG

International seat capacity dominated by Europe

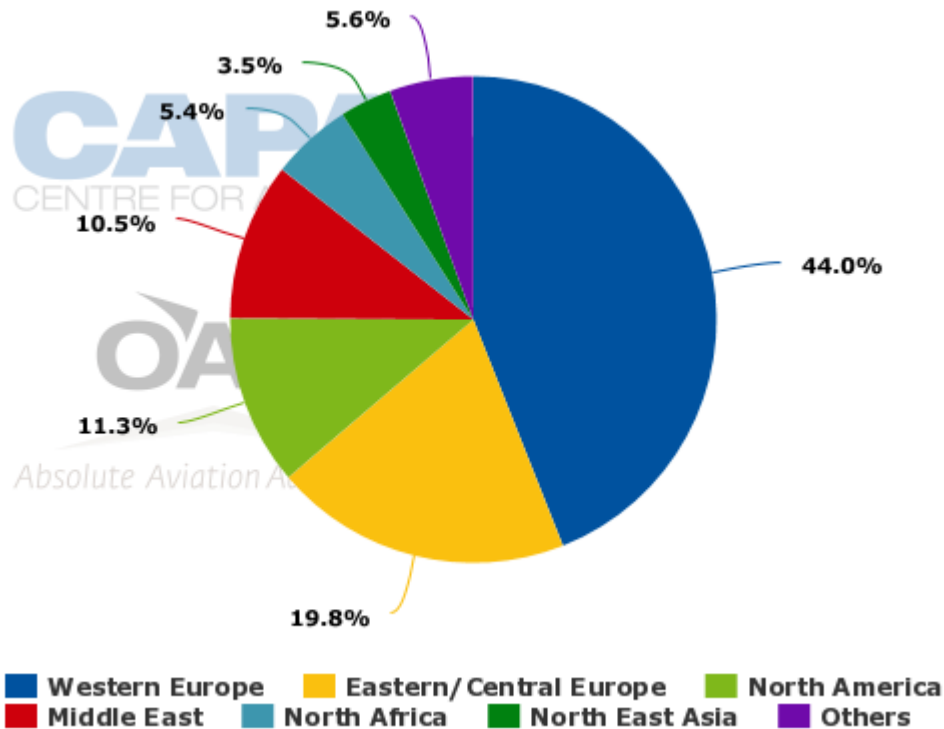
Alitalia's international seat capacity is dominated by routes to Europe, which account for 64% of its international seats this summer (44% to Western Europe and 20% to Eastern/Central Europe based on the week of 11-Jul-2016, according to OAG schedules data).

North American routes account for 11% of international seats

North American routes account for 11% of international seats, just ahead of the Middle East with a similar share. North African routes take up 5% and North East Asia just under 4% of Alitalia's international seats.

The remaining international seats are to Latin America, where Upper South America accounts for 3% and Lower South America 2% (week of 11-Jul-2016, source: OAG).

Alitalia international seats by region 11-Jul-2016 to 17-Jul-2016



Source: CAPA - Centre for Aviation and OAG

Alitalia's proportion of long haul seats has grown, but it remains underweight against its major European competitors

Alitalia's network has a much higher proportion of seats in its domestic market

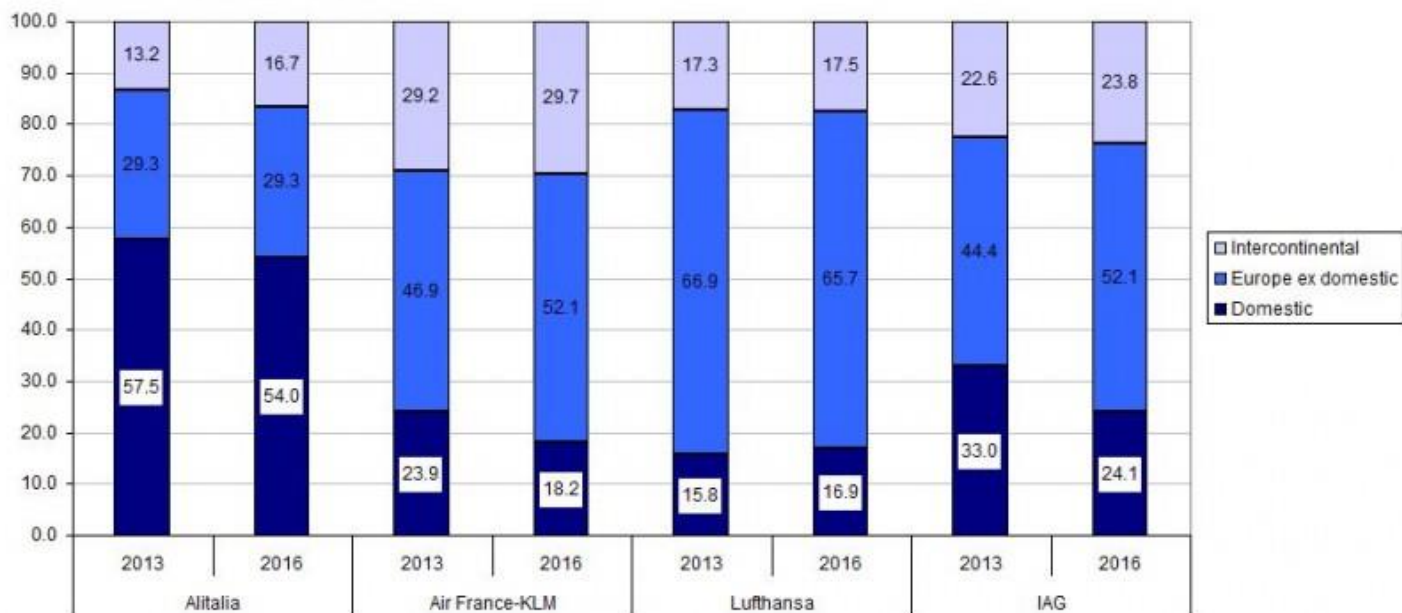
By comparison with the networks of Europe's big three legacy airline groups - Lufthansa, IAG And Air France-KLM - Alitalia's network has a much higher proportion of seats in its domestic market. Alitalia's 54% compares with 24% for IAG, 18% for Air France-KLM and 17% for the Lufthansa Group in domestic markets (week of 11-Jul-2016, data source: OAG).

The share of Alitalia's total seat numbers dedicated to its domestic network has fallen a little from 58% three years ago, while its intercontinental network has increased its share from 13% to 17% of the total. IAG and Air France-KLM both have a much higher proportion of total seats on intercontinental routes (see chart below).

Lufthansa Group's share of its seats on long haul routes is similar to Alitalia's, although, in absolute terms, the Lufthansa Group has five times as many. Air France-KLM has six times as many and IAG seven times as many intercontinental seats as Alitalia markets (week of 11-Jul-2016, data source: OAG).

Italy is one of Western Europe's five large markets, a nation similar in population to France and the UK, and larger than Spain (but smaller than Germany). This under-representation on long haul routes means that Alitalia has always had to rely on partners in order to give its customers access to much of the world beyond Europe.

Alitalia and Europe's "Big Three" seat capacity by region Jul-2013 and Jul-2016 (% of total seats)



Data based on 8-Jul-2013 to 14-Jul-2013, and 11-Jul-2016 to 17-Jul-2016

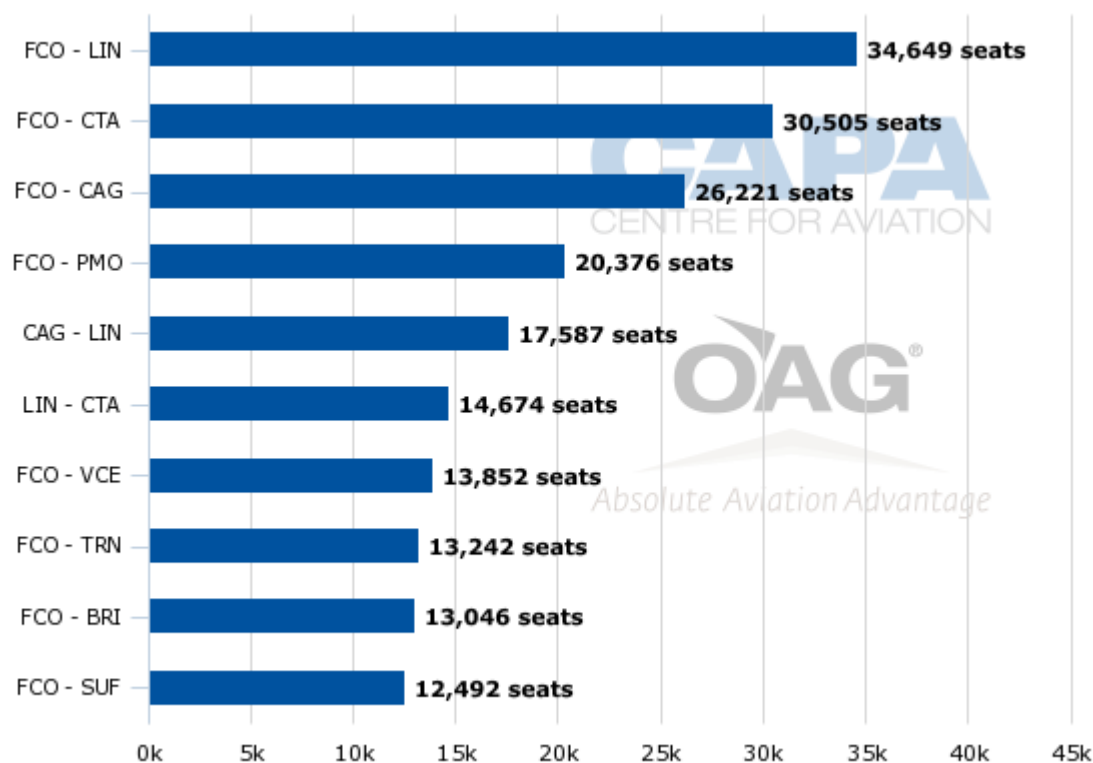
Source: CAPA - Centre for Aviation and OAG

Fiumicino-Linate is Alitalia's biggest route

Rome Fiumicino, Alitalia's main hub, features in eight of its top 10 domestic routes by seats this summer (week of 11-Jul-2016, data source: OAG). The biggest route by seats, both domestically and across the network, is between Fiumicino and Alitalia's number two base, Milan Linate.

Much of the rest of the list is leisure-oriented, including routes from Rome to Catania, Cagliari, Palermo, Brindisi and Lamezia Terme, and from Linate to Cagliari and Catania.

Alitalia top 10 domestic routes by seats 25-Apr-2016 to 1-May-2016



Source: CAPA - Centre for Aviation and OAG

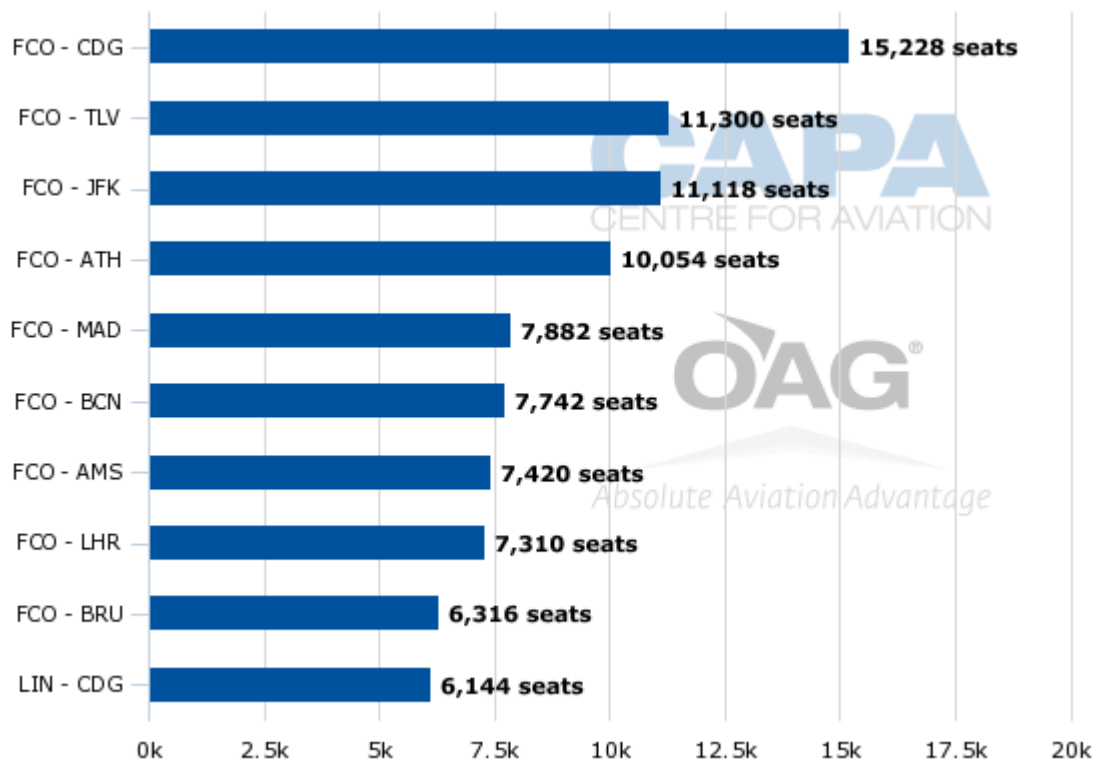
Major European hubs dominate top 10 international routes, led by Rome-[Paris CDG](#)

Rome Fiumicino also features in nine of Alitalia's top 10 international routes by seats. This list includes major European hubs served from Rome, including Paris CDG, Amsterdam, Madrid and London Heathrow.

Again, this reflects the need to connect with long haul destinations through other airlines. Rome-CDG is Alitalia's biggest international route by seats, while Milan Linate-CDG is the only one in the top 10 not to feature Fiumicino.

Alitalia remains in the SkyTeam immunised North Atlantic JV with Air France-KLM and Delta. Its biggest North Atlantic route is Rome-New York JFK, the only long haul route in its top 10 international routes.

Alitalia top 10 international routes by seats 25-Apr-2016 to 1-May-2016



Source: CAPA - Centre for Aviation and OAG

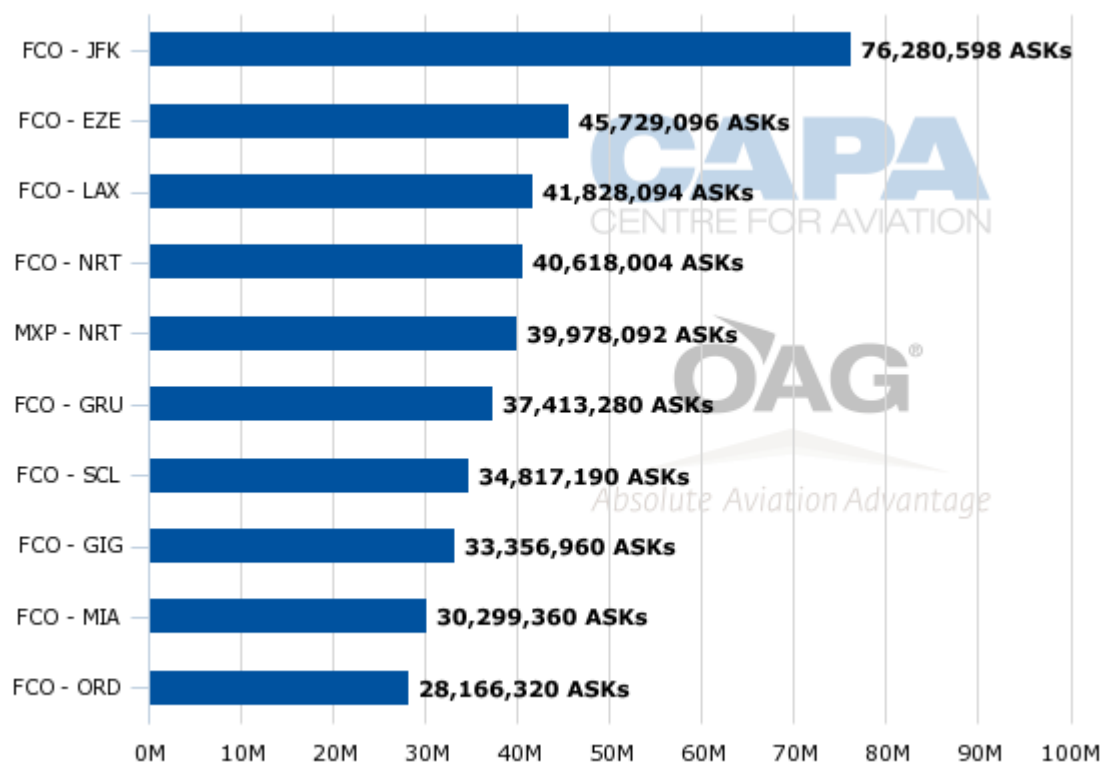
Paris CDG is the main hub of Alitalia's SkyTeam partner Air France, which also used to be a 25% shareholder in Alitalia. Air France-KLM and Alitalia have a joint venture agreement on routes between Italy and France and the Netherlands, but this will not be renewed when it expires in 2017 (a decision taken at the time of the Etihad investment in Alitalia).

US and LatAm destinations each take up four of the top 10 long haul routes

A look at Alitalia's top 10 international routes by ASKs (rather than by seats) reveals its biggest long haul routes. Nine of these are from Rome, while one is from Milan Malpensa (to Tokyo Narita).

Four of the long haul top 10, including the biggest (Rome-New York), are US routes – Rome to Los Angeles, Miami and Chicago being the other three. There are four Latin American destinations in the list (Buenos Aires, Sao Paulo, Santiago and Rio de Janeiro) and two Asian routes (both are two Tokyo, from each of Rome and Milan).

Alitalia top 10 international routes by ASKs 25-Apr-2016 to 1-May-2016



Source: CAPA - Centre for Aviation and OAG

Abu Dhabi routes are also important to long haul network

Although Alitalia's connections with Etihad's Abu Dhabi hub are not in its top 10 routes either by seats or ASKs, they are an important part of the network. Alitalia serves Abu Dhabi from Rome Fiumicino, Milan Malpensa and Venice Marco Polo.

Etihad also operates on the Rome and Milan routes (week of 11-Jul-2016). These services feed into Etihad's network, providing Italian passengers with access to its Middle East and Asia Pacific destinations. At the time of Alitalia's Jan-2015 relaunch, services to Abu Dhabi from Bologna and Catania were also planned, but they have not materialised.

See related report: Alitalia's "new" strategy realigns it to feed Etihad, but needs to change loss-making mindset

Capacity growth will be 3% this summer, led by LatAm and new Beijing service

According to OAG data Alitalia will increase its total seat capacity by approximately 3% this summer, with the strongest growth being to Latin America. It has three new long haul routes this summer: one to Asia and two to Latin America.

It plans to start a four times weekly Rome Fiumicino-Beijing service on 18-Jul-2016, operating with 250-seat, three-class A330 aircraft. The relaunch of this route, which Alitalia last operated in Mar-2013, will follow the start of new services to Santiago (Chile) on 1-May-2016, and Mexico City on 16-Jun-2016.

The new route to Beijing represents a crucial investment for Alitalia

Beijing will be its third destination in the Far East, in addition to Tokyo and Seoul. According to Mr Ball, Alitalia is “committed to strengthen our presence in the Far East. The new route to Beijing represents a crucial investment for Alitalia as we continue to expand our network through increased long-haul flying to strategic markets”.

Air China is the only airline currently flying direct between Beijing and Rome. Alitalia also serves China as part of its codeshare agreement with Etihad Airways, offering service to Beijing, Shanghai and Chengdu via Abu Dhabi. Alitalia will be the sole operator on Rome-Santiago and Rome-Mexico City.

Codeshare developments with Etihad partners – airberlin, Virgin Australia and Air Serbia

In Apr-2016 Alitalia and its fellow Etihad equity partner airberlin announced plans to strengthen their commercial relationship, building a so-called a new ‘air-bridge’ between Italy and Germany. This will involve a combined weekly frequency increase of up to 25% on direct services from Italy. Airberlin will also add capacity from Florence and Venice to Duesseldorf, increasing its current daily operation from both Italian cities to three times daily.

Under the new commercial agreement the two airlines will codeshare on more than 1,400 weekly services on 91 different routes, including 56 direct services and 750 weekly flights between Italy, Germany, Austria and Switzerland. This builds on the codeshare agreement first established between the two Etihad investments in 2014 and extended in Oct-2015.

See related report: Airberlin's new codeshare with Alitalia is no substitute for the loss of Etihad codeshare routes

In a further sign of Etihad's guiding hand, in Apr-2016 Alitalia also commenced a new (third country) codeshare with Virgin Australia (in which the Abu Dhabi airline has a 25% stake). The codeshare will cover Alitalia's Abu Dhabi-Rome and Abu Dhabi-Milan Malpensa services.

In addition, Alitalia has reportedly expanded its codeshare with Air Serbia, with Air Serbia placing its code on Alitalia's Rome-Amman service (*Airline Route*, 25-Apr-2016). Alitalia plans to place its code on Air Serbia's Belgrade services to Ohrid, Pula and Varna, effective mid-Jun-2016.

Fleet synergies with Etihad partners identified

Fleet is another area in which Etihad has identified the potential for cooperation among its equity partners, including Alitalia. For example, airberlin agreed to take 14 A320s ordered for Alitalia. In addition, Alitalia has said it was considering cooperative options with Etihad for adding aircraft to its long haul fleet. Alitalia may also receive aircraft currently on order for Etihad.

According to the CAPA Fleet Database, Alitalia's fleet comprises 102 aircraft at 29-Apr-2016, consisting of 11 Boeing 777-200ER and 91 Airbus aircraft. The Airbus equipment comprises 13 A330-200s and 78 A320 family aircraft. The average fleet age is 10.4 years.

Alitalia must develop a profit culture

Alitalia certainly seems to be in a better place than where it was before Etihad invested, but the real sign of success will be if and when it can generate sustainable profitability. Its target to make a profit in 2017 was set at the outset of the Etihad era and it says that it remains on course to achieve this.

Elsewhere much of the rest of the global airline industry is characterised by record high margins

Nevertheless, each year of loss that passes subliminally reconfirms the acceptability of loss-making in Alitalia's collective psyche. Elsewhere much of the rest of the global airline industry is characterised by record high margins, with low oil prices flattering the results of most participants.


The following observation, made by CAPA in a Jan-2015 assessment of Alitalia, still applies (see related report: Alitalia's "new" strategy realigns it to feed Etihad, but needs to change loss-making mindset):

The most important change needed will be to shed Alitalia's deep-rooted dependency culture, bred by years of coming back from the dead.

Alitalia needs to show that it can develop and embed a profit culture.

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-  airberlin SWOT: even Etihad's millions can't help it to profit in year of peak airline sector margin

10-Dec-2015

James Hogan, the CEO of Etihad Airways, which owns a 29% stake in airberlin in addition to minority stakes in other European airlines, was recently reported saying that Etihad would not increase these holdings, even if the EU were to change foreign ownership limits. Etihad has already provided more than EUR800 million in various forms to airberlin since 2012. The German airline now needs time to implement its fourth restructuring plan since 2011.

After several years of losses, airberlin's results for 9M2015 – another operating loss that only narrowed slightly due to asset disposals – suggest that it will not fulfil its Mar-2015 promise of "significantly improved results" in 2015. Another big loss looks likely, in a year when the global airline industry is set to record margins consistent with historic cyclical peaks and fuel prices are lower than they have been since airberlin last made an annual operating profit.

In this report, we assess airberlin's strengths, weaknesses, opportunities and threats. It seems that Etihad is right not to throw more good money after bad.



- Gulf airlines in London Heathrow: slot purchases expand capacity further, improving connectivity

23-Feb-2016

In the world's most premium air market, London Heathrow, Gulf airlines are increasing their presence. Emirates has obtained a sixth daily slot, the first time in a decade that it will grow above five daily flights at Heathrow (it has meanwhile been growing at Gatwick). Qatar Airways has offered six flights since May-2014 but on smaller aircraft, while Turkish Airlines will have six daily flights on three days a week from Mar-2016. Etihad has not grown slots since last decade but has increased capacity by deploying A380s. Emirates will have an all-A380 operation at Heathrow in Jun-2016.

Oman Air bills itself as a boutique airline focused on Oman, but with a high share of connecting traffic and ambitious growth plans, Oman Air is becoming a Gulf network airline. It paid USD75 million – reportedly a record – for a morning slot at Heathrow in order to have twice daily service. Beside the growth, the Big 3 Gulf airlines hold 2% of international Heathrow slots but account for 5% of seat capacity (more than local airline Virgin Atlantic). Including Oman Air and Turkish they hold 3.5% of slots. London Heathrow is a premium focus of attention but Gulf airlines are growing faster elsewhere in Europe as they diversify their networks away from London and the UK. In 2006, one in two of Emirates' Western European seats went to the UK, but in 2016 only 30% will.