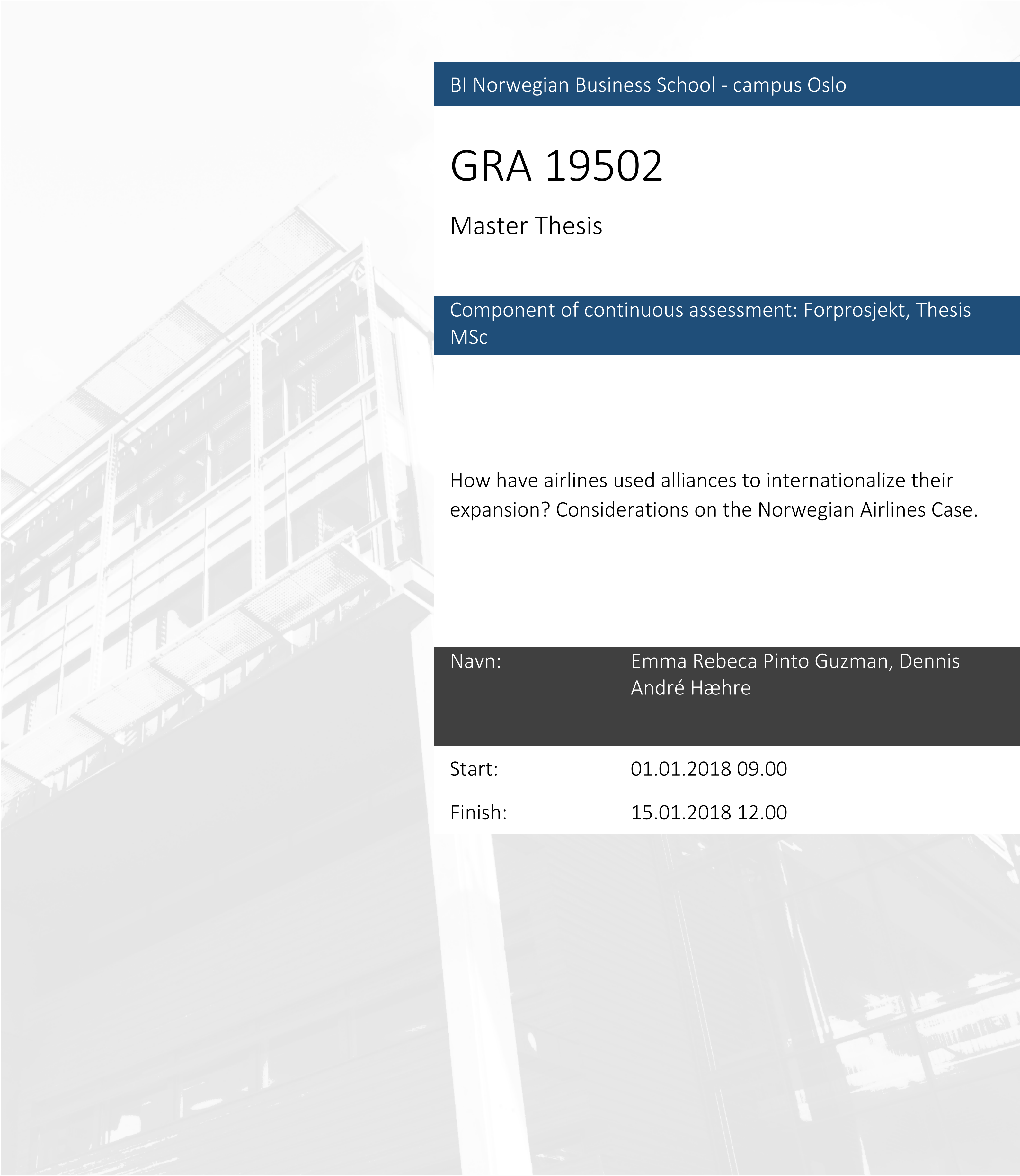

BI Norwegian Business School - campus Oslo

GRA 19502

Master Thesis

Component of continuous assessment: Forprosjekt, Thesis MSc

How have airlines used alliances to internationalize their expansion? Considerations on the Norwegian Airlines Case.

Navn: Emma Rebeca Pinto Guzman, Dennis André Hæhre

Start: 01.01.2018 09.00

Finish: 15.01.2018 12.00

Preliminary Master Thesis Report:

How have airlines used alliances to internationalize their expansion? Considerations on the Norwegian Airlines Case.

Advisor: Debbie Harrison.

Written by: Dennis Hæhre and Emma Rebeca Pinto Guzman.

Study Programme: Master of Science in Business – Strategy Major

Executive Summary

One of the most important trends in industrial organization of the past quarter century has been the growth of collaboration between independent companies. Firms have progressively liaised with other firms in order to participate in activities and gain resources outside of their limits.

In this Preliminary Master Thesis Report we aim to show the actor the path we will follow in order to success answering the question "How have airlines used alliances to internationalize their expansion? Considerations on the Norwegian Airlines Case."

First an overview on Strategic Alliances is done to put the reader in context, followed by a preliminary literature review on Airline Alliances. Then the area of study and the research question, design and method are presented. Finally, we designed a brief implementation plan to help us as a guide for our research.

Contents

Introduction:

According to the Merriam Webster dictionary an alliance is a bond or connection between families, states, parties, or individuals, an association to further the common interests of the members; and finally a union by relationship in qualities. The Cambridge dictionary also defines alliances as a group of countries, political parties, or people who have agreed to work together because of shared interests or aims and as an agreement to work with someone else to try to achieve the same thing.

Strategic alliances are today an effective vehicle for cross organizational learning and resource and knowledge sharing among partners (Kale et al., 2000; Li et al., 2010).

Das and Teng (2000) proposed that the first reason for firms to sign up for an alliance is to obtain valuable resources. For the matter of this paper, the importance of succesful alliances is not only to obtain valuable resources but to reinforce and strengthen a valuable position in the international and globalized market of the airlines industry.

Few inventions have changed how people live and experience the world as much as the invention of the airplane. Due to this relevant position in human history, the airline industry has definitely progressed. Business, migration, connectivity and related matters have been touched by these advances. Even the concept of distance has been reconfigured.

This said, it is natural to understand that the airline industry develops itself in a highly competitive market. These last years it has been shaken by industry wide trends regarding domestic and international expansion.

An Overview on Strategic Alliances

Strategic alliances can be defined as" purposive strategic relationships between independent firms that share compatible goals, strive for mutual benefits, and acknowledge a high level of mutual dependence" (Mohr and Spekman, 1994). Gulati (1995) stated that an alliance is "any independently initiated interfirm link that involves exchange, sharing, or co-development". Strategic alliances are voluntary cooperative inter-firm agreements aimed at achieving competitive advantage for the partners (Das & Teng, 2000).

Interfirm alliances comprise cooperative relationships that are not completely defined either by formal agreements or by tenure. Henceforth, regarding the theory of economic organization, they are considered to be between the extreme structures: markets and hierarchies. Therefore, cooperative relationships between firms have been viewed as "intermediate" or "hybrid" organizational forms (Grant & Baden-Fuller, 2004).

The term "strategic alliance" has been used to refer to "agreements characterized by the commitment of two or more firms to reach a common goal entailing the pooling of their resources and activities" (Teece, 1992).

For a given factor (product or service), a firm may choose to: (1) produce it on its own; (2) purchase it from the spot markets; or (3) make it jointly with partner firms. (Das & Teng, 2000).

Strategic alliances bring together otherwise independent and sometimes competing firms to share resources in different stages of their value chain. Making an alliance allows a firm to focus their own resources on its main activities, core skills and competencies while acquiring other components or capabilities it lacks (Chan et al., 1997).

Alliances can take many forms, ranging from simple contracts with no equity ties, partnerships, to more formal agreements involving equity rights and shared managerial control over collective activities. These alliances and the network organizations they forge are becoming increasingly crucial as harder competitive conditions require firms to adopt flexible and more focused organizational structures (Chan et al., 1997). Strategic considerations involve using alliances to enhance a firm's competitive position through market power or efficiency (Kogut, 1988).

Global alliances allow companies to enhance their own international competitiveness through the use of their partner resources as well. In other words they can be used as a means to accelerate the international expansion of a firm. (Garcia-Canal, 2002) Global competition highlights asymmetries in the skill endowments of firms. Collaboration may provide an opportunity for one partner to internalize the skills of the other, and thus improve its position both within and without the alliance (Hamel, 1991).

The steps made in order to enter an alliance are, according to Gulati (1998) the decision to enter an alliance, the choice of an appropriate partner, the choice of structure for the alliance, and the dynamic evolution of the alliance as the relationship develops over time.

Alliances are unpredictable crucial factors of many corporations' competitive strategies. Among their blessings, they quickly open up doors to new markets, light up the way to competence development and provide a possibility to achieve scale economies. However, like every strategic decision, alliances can perform poorly and lead to dissatisfaction and disappointments. These successes or difficulties, according to (Larsson et all, 1998) could be triggered by collective learning processes.

Firstly, an important factor for determining interorganizational learning happens to be how one of the organizations could be an asset, a good partner or a competitor in the "race to learn" for the rest of the allies.

The authors proposed that an interorganizational dilemma is faced when (1) being a good partner provokes exploitation by partners trying to extract the most profit attempting appropriation of the joint learning, and (2) such opportunistic behavior would in turn weaken the collective knowledge creation and development in the strategic alliance.

There are many trade-offs between how joint learning is developed in alliances and how the outcomes of this learning are spread among the participants. Larsson et al

(1998) have identified five approaches to collective learning regarding their receptive capacity and transparency among the partners. The strategies include collaboration (highly receptive and highly transparent); competition (highly receptive and nontransparent); compromise (moderately receptive and transparent); accommodation (nonreceptive and highly transparent); and avoidance (neither receptive nor transparent).

Strategic alliances are shaped by several factors that allow for understanding the variation in alliance development, endurance and behavior. Obstacles for a common interorganizational learning could be the little motivation or absorptive capacity and communication between the organizations. Power imbalances, opportunism, information asymmetry, agent/principal conflicts and opposite learning strategies can also be named in the list of obstacles to a successful alliance. On the other hand, a healthy interaction, trust, long lasting relationships and mutual understanding of each other makes an alliance likely to be profitable and create valuable knowledge for all the parties.

Literature review on Airline Alliances

In the airline industry, strategic alliances are characterized by joint, dedicated marketing entities for network-wide cooperation (Fan et al. 2001). Recognition for mutual flyer program, shared lounges, extensive code-sharing, coordinated schedule and fare planning are features of strategic airline alliances with a goal of delivering a seamless travel experience across the entire alliance network. For instance, all members of the Star Alliance know one another's frequent flyer programs, and many of them cooperate through code-sharing.

However, any one of these characteristics alone is not sufficient to elevate the level of cooperation to a strategic one. Fan et al. (2001) distinguish between two different characteristics of strategic alliances. Those are exclusive memberships and a joint marketing entity. In other words, a member of one strategic alliance cannot simultaneously be a member of another strategic alliance. Still, all carriers can at any time engage in a tactical cooperative agreement with multiple airlines in the same or different alliance.

During the 1980’s the U.S. airline industry was deregulated, and the European airline industry was liberalized (Hokey M., Seong-Jong J.). This gave carriers greater freedom when it comes to operating routes and fares, and a dramatic restructuring of the global airlines industry occurred. Which paved the way for new strategic possibilities, which led to the emergence of strategic alliances in the 1990’s (Hokey, Soeng).

The significance of unrealized network and other scale economies in the airline industry was not understood at the time airlines were deregulated. The industry appeared to lack economies of scale (Bailey and Liu 1995). Since then, strategic alliances have become increasingly important elements in a firm’s portfolio of strategies and are viewed as a source of competitive advantage in the airline industry (Suen, 2002).

Agusdinata and Klein (2002) argued that the formation of strategic alliances is one of the most meaningful developments in the industry which, beyond the coordination of schedules and fares, aim at cost reductions through the possibility of joint procurement opportunities in a strategic network approach. Further Wagner et al. (2005) found that airlines involved in alliances showed higher joint procurement activities than airlines that were not involved in strategic alliances in his research.

There is a stream of research that addresses airline productivity issues (Schefczyk, 1993; Park, 1997). This stream of research includes studies measuring the extent of benefits of airline alliances and then assessing their impact on airline productivity, market shares, firm value creation, and competitiveness. Since strategic alliance has emerged as a popular business strategy for many airlines, some articles have identified the potential benefits of forming strategic alliances. Wan et al. (2009) identified the following five potential benefits of airline alliances. First, alliances allow airlines to expand their market bases internationally, while circumventing regulatory and legal barriers (Oum et al., 1996; Park, 1997). For instance, airline alliances often include code sharing agreements that allow one alliance member to sell tickets to destinations served by other alliance carriers.

Second, joining an alliance can provide cooperation benefits. An alliance can provide cost saving potentials resulting from sharing facilities, maintenance costs, sharing frequent flier plans, and joint marketing (Iatrou and Alamdari, 2005). Third, alliances may lead to traffic increases for partner airlines. Alliances can facilitate both linking cities within an international network and streamlining transfers between carriers. Consequently, load factors may increase, or the alliance members may be able to use larger aircraft with reduced per-seat flight costs on international routes (Harris, 1977, Wright et al., 2010). This is the one of the main reasons airlines in an alliance can gain competitive advantages over a non-aligned airline, according to Park (1997).

Fourth, passengers may benefit from more flexible schedules, shorter travel times, improved luggage handling, and shared frequent flyer programs (Dennis, 2000). These benefits can help build passenger loyalty for alliance carriers and, in turn, increase the effectiveness of loyalty programs.

Fifth, alliances may create more effective cooperation, which can lead to the elimination of competition on parallel, hub-to-hub routes if carriers cooperate, rather than compete, on price (Huston and Butler, 1988). Additionally, effective cooperation can lead to an improvement of firm value (Wassmer and Meschi, 2011).

There have been a number of empirical studies on alliances' impacts on performance, including Park and Cho (1997) and Oum et al.'s (2000), which show that alliances improve a carrier's performance on a number of economic measures, including productivity, pricing, profitability, and share price.

Some studies have focused on and measured the impact of airline alliances on airfares. These studies have come to different conclusions. For instance, Brueckner and Whalen (2000) found that airline alliances resulted in airfare reduction through joint pricing. Later, Wan et al. (2009) argued that it was not as simple as that, and found that the extent of impact an alliance has on airfares depended on the ability to coordinate fares. Zou et al (2011) analyzed if cooperation led to higher fares though lower operating costs. While their results were mixed and not conclusive, they did find that two of the major airline alliances, Skyteam and Star Alliance, appeared to charge significantly higher fares for through-tickets(?) than the sum of segment tickets purchased separately. However, other studies such as Gayle (2008) have conducted a similar analysis and found no evidence that such cooperation or collusive behavior among airline alliance were present.

Berry's early study (1990) incorporated passenger preferences in a product differentiation model of airlines. He/She found that passengers are willing to pay a premium for services that relate to airlines' network coverage. In his subsequent paper, Berry (1992) estimated the effects of airlines' network coverage on airline city-pair profitability. However, the welfare implications are left open

Setting aside prices, Bailey and Liu (1995) argued for the importance of network effects in the airline industry, highlighting that alliances can provide consumers with convenient, on-line connection opportunities. The authors further found that the transition to a smaller number of firms has been welfare-improving. In other words, consumers are willing to pay more to have fewer firms in order to enjoy certain welfare-enhancing service improvements (Bailey and Liu, 1995)

Context / The Area of Study

We would like to write our master thesis focusing on the airlines industry. We will analyze airlines based in Norway, and how they have used their alliances in order to expand internationally. We have chosen the airlines industry because we feel this industry suits our research proposal, being that alliances are fairly common in the airline industry. Additionally, we have seen an increased focus on internationalization in the last years in this industry, and the importance of serving an international market has become critical for the success for airlines. In our study, we would like to analyze how the firms expand, and whether an alliance makes this process more successful. Further, we want to analyze how these firms makes use of their alliance during this process, and how to best make use of their alliance.

The Research Question:

How have airlines used alliances to internationalize their expansion? Considerations on the Norwegian Airlines Case.

We have decided to do a qualitative methods study, therefore we pose a Research Question that will be answered with qualitative investigation. It is composed by two parts that include the topic of Strategic Alliances in an international context and then we narrow the exploration into a particular case: Norwegian Airlines.

Research Design

We have chosen to follow a qualitative approach. The detailed design of our thesis is not yet set in stone, as we feel it will depend on our data gathering and interview possibilities, we have advanced in the request for Norwegian Airlines and Scandinavian Airlines to concede us an interview. A comparative analysis is highly likely, as our main plan is to interview two airline companies with a different strategy regarding alliances, and therefore it would be effective to compare these two firms in strategy and actions to analyze how being in an alliance impact how the firm expands internationally. This is depends on the data we are able to gather from these firms. If this is not possible, we might work towards a case study, with a single airline company. Then, analyzing that firm and how being in an alliance changes their approach to an international expansion.

Research Method

Data Collection

The core tool of our thesis will be interviews, and we hope to gather most of our data interviewing people from Norwegian airlines, or international airlines if necessary. As of now, we have approached both Norwegian Air Shuttle and Scandinavian Airlines System (SAS) and asked for the possibility for an interview in the coming months.

While neither of these airlines were able to confirm an interview for the coming month, neither of them declined our request. We did receive contact information from both firms for people we can approach when we have time and preparations in order, and hopefully these will be able to assist us. However, the representative from Norwegian did say that as of now, they are somewhat tired of being interviewed for research project, so a face to face interview were unlikely.

The reason that we have chosen to focus on these two airlines primarily is because their location and market share internationally. Both are global airline companies who have had to expand their operation on several occasions, and this is one of the things we are interested in. SAS is a member of Star Alliance, so we are curious to find out how being in an alliance have impacted how they have expanded internationally. Whether or not precautions were made in regards to the other members of the alliance when expanding, or if there are some benefits to being in an alliance when the company expanded into different regions.

When it comes to Norwegian Air Shuttle, they are not in an alliance as of right now in the same way that SAS is a part of Star Alliance. They have different networks and companies they are partner with, but not in the same formal way as a traditional airline alliance. We are curious as to why that is, and whether they believe that they have benefitted from not being in an alliance, or if they see some points of their operations and expansions being made easier if they had been in an alliance.

Our plan for the interviews is to conduct semi structured interviews. The structure and construction of the interviews will follow Bryman and Bell (2015) framework and we intend to include questions that give us a broader perspective of the firm, in addition to direct, follow-up and probing questions

The reason for not performing a survey is that surveys are limited to the questions formulated in advance. We believe interviews will help us get a better understanding of the strategy and actions the firms have taken.

Data analysis

Transcribing and analyzing the interviews will be a large part of the thesis work. The thesis will be analyzed through content analysis, using an inductive analytical approach. In this part, coding is a crucial segment in the process of doing content analysis (Bryman and Bell 2015, 299). We hope to find some data that can help us answer or at least provide some information regarding our research question.

Research Design Criteria

It will be important to evaluate possible validity issues regarding our method. From Bryman and Bell (2015), validity can be described as "the integrity of the conclusions that are generated from a piece of research".

This is separated into two parts, internal and external validity. Internal validity is concerned with the issue of causality and the importance to gain credibility. External validity is mainly concerned with the issue of transferability, whether the research is applicable to other contexts and situations. We want to keep this in mind during our thesis, and try to make sure our research fits into these criterias.

Implementation Plan

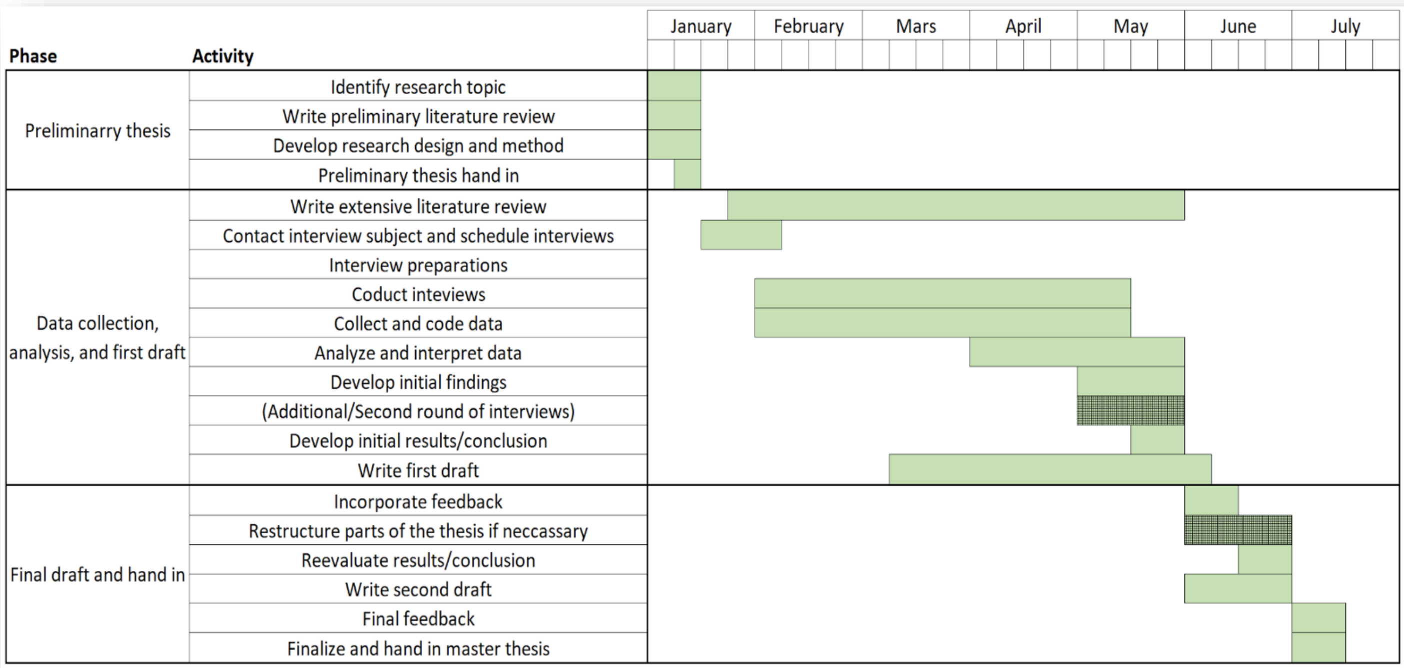

Figure 1 Implementation Plan

References

Agusdinata, B., de Klein, W. (2002). The dynamics of airline alliances. Journal of Air Transport Management, 8, 4, 201-211.

Bailey, E., Liu, D., (1995). Airline consolidation and consumer welfare. Eastern Economic Journal, 21 (4), 463–476

Berry, S. (1990). Airport presence as product differentiation. American Economic Review, 394-399

Berry, S. (1992). Estimation of a model entry in the airline industry. Econometrica, 889-917.

Brueckner, J.K., Whalen, W.T. (2000). The price effects of international airline alliances. Journal of Law and Economics, 43 (2), 503-546.

Bryman, Alan, and Emma Bell. 2015. Business research methods: Oxford university press. Fourth Edition

Chan, S. H., Kensinger, J. W., Keown, A. J., & Martin, J. D. (1997). Do strategic alliances create value?. Journal of financial economics, 46(2), 199-221.

Das, T. K., & Teng, B. S. (2000). A resource-based theory of strategic alliances. Journal of management, 26(1), 31-61.

Dennis, N. (2000). Scheduling issues and network strategies for international airline alliances. Journal of Air Transport Management. 6 (2), 75-85

Fan, T., Vigeant-Langlois, L., Geissler, C., Bosler, B., & Wilmking, J. (2001). Evolution of global airline strategic alliance and consolidation in the twenty-first century. Journal of Air Transport Management, 7(6), 349-360.

Garcia-Canal, E., Duarte, C. L., Criado, J. R., & Llaneza, A. V. (2002).

Accelerating international expansion through global alliances: a typology of cooperative strategies. Journal of World Business, 37(2), 91-107.

Gayle, P.G. (2008). An empirical analysis of the competitive effects of the Delta/ Continental/Northwest code-share alliance. Journal of Law Economics, 51 (4), 743-766.

Grant, R. M., & Baden-Fuller, C. (2004). A knowledge accessing theory of strategic alliances. Journal of management studies, 41(1), 61-84.

Gulati, R. (1995). Social structure and alliance formation patterns: A longitudinal analysis. Administrative science quarterly, 619-652.

ISO 690

Gulati, R. (1998). Alliances and networks. Strategic management journal, 19(4), 293-317.

Hamel, G. (1991). Competition for competence and interpartner learning within international strategic alliances. Strategic management journal, 12(S1), 83-103.

Harris, R.G. (1977). Economies of traffic density in the rail freight industry. The Bell Journal of Economics 8 (2), 556-564.

Hokey, M., Seong-Jong, J. (2016). A comparative performance analysis of airline strategic alliances using data envelopment analysis. Journal of Air Transport Management, 52, 99-110

Huston, J.H., Butler, R.V. (1988). The effects of fortress hubs on airline fares and service. The early returns. Logistics and Transportation Review, 24 (3), 203-215.

Iatrou, K., Alamdari, F. (2005). The empirical analysis of the impact of alliances on airline operations. Journal of Air Transport Management, 11 (3), 127-134

Kale, P., Singh, H., & Perlmutter, H. (2000). Learning and protection of proprietary assets in strategic alliances: Building relational capital. Strategic management journal, 217-237.

Kleymann, B., & Seristö, H. (2017). Managing strategic airline alliances. Routledge.

Kogut, B. (1988). A study of the life cycle of joint ventures. Management International Review, 28(4), 39-52.

Larsson, R., Bengtsson, L., Henriksson, K., & Sparks, J. (1998). The interorganizational learning dilemma: Collective knowledge development in strategic alliances. Organization science, 9(3), 285-305.

Li, N., Boulding, W., & Staelin, R. (2010). General alliance experience, uncertainty, and marketing alliance governance mode choice. Journal of the Academy of Marketing Science, 38(2), 141-158.

Mohr, J., & Spekman, R. (1994). Characteristics of partnership success: partnership attributes, communication behavior, and conflict resolution techniques. Strategic management journal, 15(2), 135-152.

Oum, T. H., Park, J. H., & Zhang, A. (2000). Globalization and strategic alliances: the case of the airline industry.

Oum, T.H., Park, J.H., Kim, K., Yu, C. (2004). The effect of horizontal alliances on firm productivity and profitability: evidence from the global airline industry. Journal of Business Research, 57, 844–853.

Oum, T.H., Park, J.H., Zhang, A., 1996. The effects of airline code sharing agreements on firm conduct and international air fares. Journal of Transport Economics and Policy, 30 (2), 187-202

Park, J.H. (1997). The effects of airline alliances on markets and economic welfare. Transportation Research Part E, 33 (3), 181-195

Park, J.H., Cho, D.S. (1997). The effect of strategic alliance on performance. A study of the international airline industry. Journal Air Transport Management, 3 (3), 155–164

Schefczyk, M. (1993). Operational performance of airlines: an extension of traditional measurement paradigms. Strategic Management Journal 14 (4), 301-317.

Suen, W. (2002). Alliance strategy and the fall of Swissair. Journal of Air Transport Management, 8, 355-363

Teece, D. J. (1992). Competition, cooperation, and innovation: Organizational arrangements for regimes of rapid technological progress. Journal of economic behavior & organization, 18(1), 1-25.

Wagner, C.M., Huber, B., Sweeney, E., Smyth, A. (2005). B2B e-marketplaces in the airline industry: process drivers and performance indicators. Int. J. Logist. Res. Appl. 8 (4), 283-297. (National Institute for Transport and Logistics)

Wan, X., Zou, L., Dresner, M. (2009). Assessing the price effects of airline alliances on parallel routes. Transportation Research Part E, 45, 627-641

Wassmer, U., Meschi, P.X. (2011). The effect of code-sharing alliance formations and terminations on firm value: the role of co-specialization and scope extension. Journal Air Transport Management. 17 (5), 305-308

Wright, C.P., Groenevelt, H., Shumsky, R.A. (2010). Dynamic revenue management in airline alliances. Transportation Science, 44 (1), 15-37.

Yoshino, M. Y., & Rangan, S. (1995). Strategic alliances: An entrepreneurial approach to globalization.

Youssef, W., & Hansen, M. (1994). Consequences of strategic alliances between international airlines: the case of Swissair and SAS. Transportation Research Part A: Policy and Practice, 28(5), 415-431.

Zou, L., Oum, T.H., Yu, C. (2011). Assessing the price effects of airline alliances on complementary routes. Transportation Research Part E, 47, 315-332.