

SKYJET

Cost Reduction Strategy Airlines

Medium-Hard difficulty
Interviewer-led case

This case discusses a cost reduction strategy for an Airline company.

The case is intended to cover all aspects of the case scorecard, to provide the interviewee with a tool-kit for approaching cost reduction cases or questions in the future.

Problem definition

Your client today is SkyJet, a top 10 regional airline in the US who has been steadily growing over the last 30 years. SkyJet operates a fleet of 150 aircrafts, primarily using regional jets, and services over 20 destinations within the US. They have continually evolved their unique “best-in-class customer experience” model to maintain a market leading load factor.

Recently, SkyJet has faced pressures from their board to improve their bottom line, and the board is focused on cost savings as the lever to do so. Given this, you have been tasked with coming up with a comprehensive cost reduction strategy for the Chief Strategy Officer to support SkyJet in their next phase as a company.

How would you approach developing a cost reduction strategy?

Additional information

If asked, please share that:

- The board is hoping to find ~\$40M in annual cost savings in the next 5 years, while minimizing impact to their brand and revenue
- Load factor definition: Load Factor is a key performance metric that measures the efficiency with which an airline fills its available seats. Simply put, it's the occupancy of the flight. More specifically, it is the ratio of the number of revenue passenger miles (RPMs) to the number of available seat miles (ASMs). SkyJet's is presently 90%
- If the interviewee asks for the cost breakdown, share that the data will come later and move to the first question
- Competitors: Competes primarily with other regional airlines such as Delta Connection, and United Express, as well as low-cost carriers like Southwest and JetBlue

- Hubs: Major hubs include Chicago, San Francisco, and Los Angeles

Question 1 (Structuring)

How would you structure your approach to the question?

Additional information

- We want the interviewee to gain a holistic perspective of a cost reduction strategy, and so if they focus their answer on only one lever of the structure (e.g., they just brainstorm ideas for cost savings), prompt them to think about the other lever (e.g., “How might they go about prioritizing the most attractive option? Where should they look first?”)
- Note: the example answer provided is likely more detailed than a candidate will provide, but the interviewer should review the whole set of options after the fact to get a sense of general cost reduction strategies and how to think about them

Possible answer

1. *First, understand our current cost structure to understand the biggest cost opportunities*
 - a. *Breakdown of our cost structure*
 - b. *Show values over time to see changes*
 - c. *Comparison of our cost structure (e.g., costs as a % of revenue) versus competitors*
2. *Second, brainstorm cost management opportunities*
 - a. *Variable Cost Management Strategies*
 - *Fuel Cost Improvements*
 - *Price (Fuel Hedging): Lock in fuel prices through hedging contracts to manage price volatility*
 - *Utilization (Reduced Consumption):*
 - (a) *Fleet Modernization: Invest in more fuel-efficient aircraft to reduce fuel consumption per mile*
 - (b) *Operational Adjustments: Implement fuel-saving practices such as optimized flight paths, reduced taxi times, and weight reduction measures (e.g., lighter materials for seats)*
 - *Labor Cost Management*
 - *Crew Scheduling Optimization: Use advanced software to create more efficient schedules, reducing overtime and increasing productivity*
 - *Cross-Training Staff: Cross-train employees to perform multiple roles, allowing for more flexible staffing and better utilization of labor during peak and off-peak times*

- *Maintenance Cost Reduction*
 - *Predictive Maintenance: Use data analytics and predictive maintenance technologies to prevent breakdowns and reduce unscheduled maintenance*
 - *Supplier Negotiations: Negotiate better terms with maintenance, repair, and overhaul (MRO) providers*
- b. *Fixed Cost Improvement Strategies*
 - *Aircraft Leasing and Ownership*
 - *Lease Renegotiations: Renegotiate aircraft leasing contracts to achieve lower rates or more favorable terms*
 - *Fleet Standardization: Standardize the fleet to a smaller variety of aircraft types to reduce training, maintenance, and spare parts costs*
 - *Administrative and General Expenses*
 - *Office Space Optimization: Implement remote working policies to reduce the need for large office spaces, lowering rent and utility costs*
 - *Shared Services: Consolidate back-office functions (e.g., HR, finance) into shared service centers to achieve economies of scale*
 - *Airport and Handling Fees*
 - *Hub Optimization: Optimize the use of airport hubs to maximize efficiency and negotiate lower fees with airports based on volume*
 - *Route Rationalization: Review and adjust the network to focus on more profitable routes, potentially reducing the number of less profitable flights*
- 3. *Third, determine which option is most attractive*
 - a. *Cost impact*
 - b. *Impact to brand*
 - c. *Impact to revenue*

Question 2 (Data analysis)

The client would like your support in understanding the biggest cost opportunities (share Exhibit 1). They pulled the following set of financials for you to analyze.

What insights can you draw from the following numbers? What would you want to investigate further?

Guidance for interviewer

- A strong candidate should answer both questions thoroughly, giving both facts (what the data is) and insights (what the data means)
- If the candidate does not notice the increase in Sales & Marketing, prompt them further until they notice it

Possible answer

1. Key insights

- a. Profit growth has slowed
 - i. Profit growth has slowed in the last 2 years following 2 years of steady growth between 2020 – 2022
 - ii. This is due to changes in the cost structure, as revenue growth has remained consistent
- b. Sales & Marketing as a % of revenue has increased materially
 - i. Increases in Sales & Marketing has been the cause for the slowdown in profit growth, as it has increased to +\$50M in growth YoY
- c. The largest drivers of cost are fuel costs and labor costs, and while those have increased, they have increased at a slower rate than revenue, so they are unlikely to be part of the problem

2. Next steps

- a. Understand why Sales & Marketing has increased materially and why there hasn't been a resulting increase in revenue
- b. Benchmark all of our costs, but in particular our fuel and labor costs, vs. competitors to determine if there is opportunity for optimization

Exhibit 1: Skyjet Financial Overview (Last 5 Years)

Metrics (\$M)	Y-4	Y-3	Y-2	Y-1	Y-0
Revenue	2000	2150	2300	2450	2600
Fuel Costs	500	530	560	590	620
Labor Costs	400	420	440	460	480
Maintenance Costs	200	215	230	245	260
Leasing & Ownership	250	265	280	295	310
In-flight Service Costs	100	105	110	115	120
Sales & Marketing	100	110	120	180	230
Admin & General Expenses	70	75	80	85	90
Total Costs	1620	1720	1820	1970	2110
Profit	380	430	480	480	490

Private copy of Thai Nguyen
 (thaicnh0729@gmail.com)
 Copy and Sharing Prohibited.

Question 3 (Numeracy & Creativity)

The client agrees that the increase in Sales & Marketing cost is concerning. They are interested in your opinion and the hard data to back up a Sales & Marketing investigation.

They would like you to do a rough calculation Sales & Marketing's share of overall revenue in Y-4 and Y-0, as well as a brainstorm of potential reasons for this shift.

Guidance for interviewer

- A strong candidate manages the complexity of hearing two separate questions and answers independently and keeps track of both
- Ensure the candidate is aware they do not need exact numbers, just rough ballpark values (to test the concepts). This case has the candidate perform two separate, smaller number calculations versus one larger one. Note if you are confident with the candidates numeracy or need more time, skip one of them and simply provide the candidate with the output

Possible answer

1. *Run the calculation :*

- a. *Determine what % of revenue Sales & Marketing makes up*
 - i. *Y-4 (Sales & Marketing) / Revenue, or $100 / 2000 = 5\%$*
 - ii. *Y-0: (Sales & Marketing) / Revenue, or $230 / 2600 = 8.8\%$, round to 9%*
- b. *Evaluation:*
 - i. *This is a huge increase, nearly doubling the share of revenue spent on Sales & Marketing*

2. *Second, brainstorm explanations*

- a. *Promotional Campaigns and Customer Acquisition*
 - i. *Aggressive Promotional Offers: To improve load factors and increase market share, SkyJet may have launched aggressive promotional campaigns, offering discounts, loyalty programs, or other incentives*
- b. *Brand Repositioning or Rebranding*
 - i. *Rebranding Campaign: SkyJet might have undertaken a major rebranding initiative to refresh its image, align with changing market trends, or appeal to a new demographic*
- c. *Increased Competition*

Question 4 (Data Analysis)

A deep-dive into the Sales & Marketing efforts revealed that in Y-1 and Y-0, SkyJet decided to amp up their Sales & Marketing efforts. They launched a campaign called “Are You Sure?” that would extend an offer to any customers who didn’t complete their purchase when buying flights from SkyJet online. This offer would be in the form of an e-mail with a small flight discount, as well as a ‘kick-back’ food & beverage voucher for any restaurant in the airport

In order to better understand the impact of this campaign, the team pulled a set of key metrics for Skyjet.

What insights about the campaign can you pull from Exhibit 2? Has the campaign been effective?

Guidance for interviewer

- If the interviewee is unclear how the promotion works, describe the process step by step. Essentially, if a customer has put a ticket in their basket and closes their browser, SkyJet would send an e-mail that provides a code for a \$50 food & beverage voucher for any restaurant in the departing airport if the customer purchases the ticket, as well as a \$10 discount on the flight. Note that a strong candidate may still need some guidance understanding the structure of the offer
- A strong candidate will keep the case goal of cost savings in mind, and should evaluate whether or not the campaign has been effective. They should identify that removing this campaign could be an option for reducing costs
- A very strong candidate links the data from the previous exhibit (flat revenue growth) to this exhibit, instead of just getting the cost insight. As well, they recognize the ticket discount as a ‘revenue opportunity’ and the food & beverage voucher as a ‘cost opportunity’
- This exhibit should test being able to filter through and understand what is/isn’t relevant data

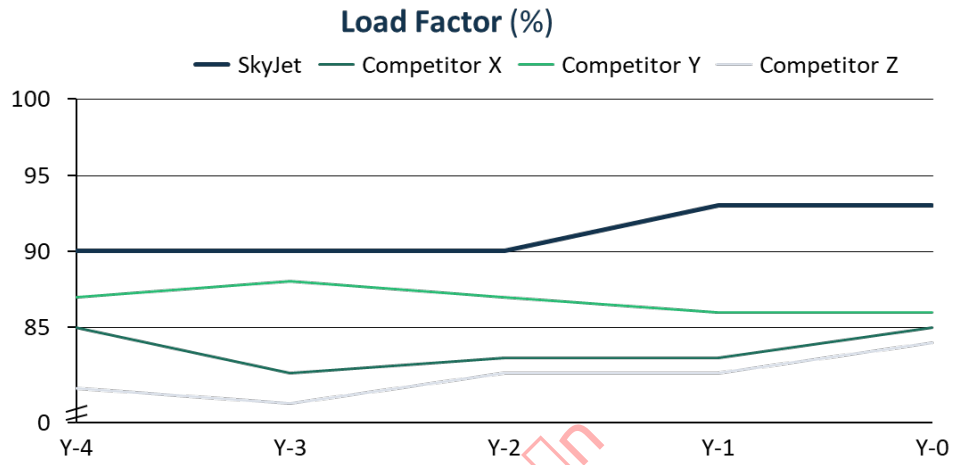
Possible answer

1. *The campaign resulted in an increase in load factor, increasing from ~90% to ~93% from 2022 to 2024*
2. *The decrease in ticket price means that, although the total number of customers increased, total revenue didn't increase as a result of this campaign. This would indicate that the campaign has been costly but ineffective*
3. *Both the decrease in ticket price AND the food & beverage voucher led to a material decrease in average margin per customer, but the main cost optimization opportunity comes from the food & beverage voucher*

*In summary, SkyJet should re-evaluate this prom
bottom line*

Private copy of Thái Nguyễn
(thaicnh0729@gmail.com)
Copy and Sharing Prohibited.

Exhibit 2:



SkyJet Avg. Ticket Price	\$234.00	\$239.00	\$235.00	\$230.00	\$229.00
SkyJet Avg. Margin per Ticket	\$65.00	\$70.00	\$62.00	\$48.00	\$49.00

Private copy of Thái Nguyên
 (thaicnh0729@gmail.com)
 Copy and Sharing Prohibited.

Question 5 (Numeracy)

The client agrees that there are issues with the 'Are You Sure' campaign and they want to understand the cost savings associated with cancelling the program. Assume that the client is not interested in the revenue uplift, or ticket discount portion of the program.

They provide the following data:

- SkyJet expects to sell 11M tickets in 2025
- 50% of these tickets will be sold online
- 20% of the tickets sold online will be through the 'Are You Sure?' campaign
- The food & beverage voucher was for \$50
- 80% of customers redeemed their voucher

Based on this data, how much would SkyJet save from cancelling the 'Are You Sure' campaign?

Guidance for interviewer

- The following numbers should be calculated fairly quickly and a strong candidate will structure, calculate quickly, and provide insights

Possible answer

- Calculate how many 'Are You Sure' vouchers were issued
 - a. $[11,000,000 * 50% * 20\%] = 1,100,000$
- Incorporate how many were redeemed
 - a. $[1,100,000 * 80\%] = 880,000$
- Incorporate the cost per redemption
 - a. $[880,000 * \$50] = \$44M$
- Share insight
 - a. This figure surpasses the initial goal set by the client of \$40M in cost savings

Question 6 (Synthesis)

The project is wrapping up and it is time to share out your final findings and recommendation to the client. Please summarize your cost reduction strategy recommendation.

Guidance for interviewer

- If the candidate soars through the case too quickly/easily, ask them a brainstorming/creativity question. For example, “How might the team revise the ‘Are You Sure?’ campaign to make it more successful?”

Possible answer

- *Ultimately, I would recommend that SkyJet cancel their ‘Are You Sure?’ Sales & Marketing campaign for*
 - *First, SkyJet would see \$44M in annual savings from cancelling the campaign, which surpasses the client’s target*
 - *Second, the campaign was reducing overall profitability, as revenue stayed flat due to decreasing ticket prices, despite the increase in load factor, and costs were increasing due to the food and beverage voucher*
- *In terms of next steps, I would:*
 - *Evaluate whether there is opportunity to run the ‘Are You Sure?’ campaign without such steep discounts to flight prices and vouchers,*
 - *Investigate other large cost items in SkyJet’s structure, such as fuel and labor costs, to determine if there is opportunity for further cost savings*

Need to improve your numeracy?

Practice daily with our Calculations and Case Math drills

