



Money

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COVER STORY

Midsized lines like Alaska Air stick to niches

Airline works so well that it might attract buyers

Braniff's \$3.5B jet deal, **Page 7B**

By
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USA TODAY

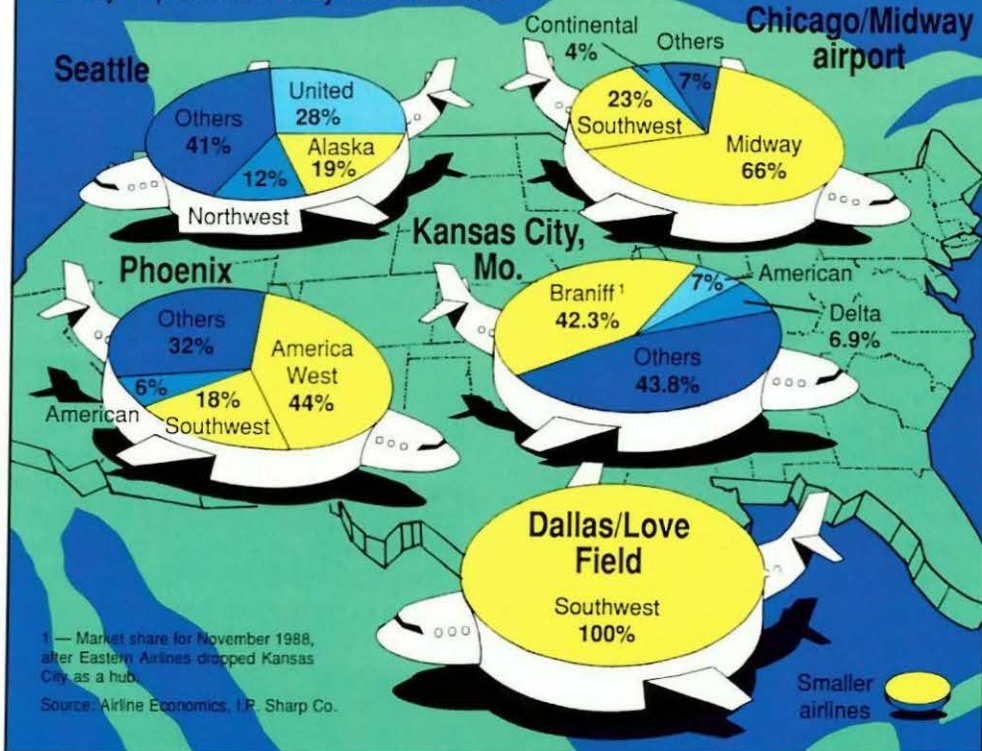
SEATTLE—For 16 years, Alaska Airlines has done nearly everything right.

Each year has been profitable — even the ones when most of the bigger airlines were losing money. The airline carries more than four times as many passengers as it did 16 years ago, many of whom rave about flight meals and service. Wednesday, Alaska said it carried 4.9 million passengers in 1988, up 23% from 1987. So, what's Alaska Chairman Bruce Kennedy got to worry about?

Plenty. Having a healthy balance sheet and happy passengers no longer guarantee survival for medium-sized airlines such as Alaska. In the decade since the industry's deregulation, airlines have thrived by carving out niches — route systems underserved or avoided entirely by the major airlines. Seattle-based Alaska, for instance, flies primarily between Alaska and cities in five Western States. Another niche airline, Midway, has built its route system around Chicago's Midway Airport. Aloha and Hawaiian found success by ferrying passengers from Hawaiian island to Hawaiian island or between the islands and

Airlines pick their spots

Smaller airlines have survived deregulation by building niches, often dominating airports underserved by major airlines. A look at Jan.-Sept. 1988 market shares for key airports served by niche airlines:



By Bob Laird USA TODAY



BRUCE KENNEDY: Alaska Air chief is wary of major airlines.

the West Coast. Now these airlines face the tough task of protecting their turf and growing without getting in the way of the eight airline giants who control 90% of the market.

"They could drive us out of business in a fairly short time if they put their minds to it," Kennedy says. "As long

as we are a fairly benign competitor, they may well delay the day that they decide that's something they want to do."

He hopes. Recent history isn't very encouraging. The number of medium-sized airlines — smaller than majors but bigger than commuters —

COVER STORY**Alaska Air flies
where giants don't****Continued from 1B**

has shrunk to seven from 15 since 1985. Many of the mid-sized airlines that once gave the major airlines competitive fits — such as People Express, Pacific Southwest, Frontier, Air California — have been bought by the giants. Takeover talk still swirls around most of the survivors, even though some analysts say congressional pressure is likely to force the federal government to take a tougher stance on airline mergers.

Besides Alaska, the group includes America West, Aloha, Braniff, Hawaiian, Midway and Southwest. Last summer, a group of investors bought 80% of Braniff, which Wednesday announced plans to acquire up to 100 new jets for \$3.5 billion. Japan Air Lines has federal approval to buy up to 20% of Hawaiian. America West is 20% owned by Ansett, an Australian transportation company.

Some of these airlines someday may qualify as major airlines — by the federal government's definition, that's an airline with \$1 billion or more in annual sales — but there's a wide gap between them and the current majors. Alaska's parent company, Alaska Air Group, had sales of \$709 million in 1987 vs. Pan Am Corp.'s \$6.2 billion, the smallest of the eight major airline companies.

Kennedy takes the threat of an unwanted suitor seriously. Alaska has hired Bruce Wasserstein and Joseph Perella — two of Wall Street's leading mergers and acquisitions specialists — to formulate defense strategy. That may be a smart move — Trans World Airlines Chairman Carl Icahn has said he'd like to buy another airline. "We're not for sale," Kennedy says. "On my watch, I don't want to see the airline go out of existence . . . I want to pass Alaska Airlines on to somebody else with the company intact."

Kennedy, a boyish-looking 49, knows something about takeovers. He and a business partner, Ronald Cosgrave, led a board revolt against

former Chairman Charles Willis in 1972 when Alaska was on the brink of collapse. Willis wasn't a great businessman, but he was colorful. Willis — "Uncle Charlie" to some employees — decorated his office like a Gay '90s saloon complete with swinging doors, a moose head on the wall and beer on tap. He helped pioneer in-flight movies in the 1940s — using a projector and a home movie screen on board planes. Flight attendants served passengers coffee from golden Russian samovars.

Alaska still does things you don't see on any other airline. A smiling Eskimo adorns the tail of each plane. One flight attendant routinely draws chuckles from passengers when he imitates Ronald Reagan or Elvis Presley during pre-flight announcements. The airline also goes to great lengths to please passengers. Alaska spends more on in-flight meals than nearly any other big airline — about \$6.70 per passenger vs. an average of \$4.11 for the 10 major airlines. Champagne and wine are complimentary. Coach-class seats in its 46 jets have about two inches more legroom than in competitors' planes. Customers appreciate the difference. In a September USA TODAY poll of frequent business travelers, Alaska Airlines ranked first among airlines, garnering more "excellent" ratings than any competitor. "I fly them whenever I can," says Dain Bosworth Inc. analyst William Whitlow of Seattle. "This is a service business, and those guys epitomize good service."

Alaska Air has carefully stayed within its Northwestern niche. The leading airline on the Alaska-to-mainland routes, it has expanded cautiously within Alaska and five Western states. It has avoided taking on the giants on such routes as Seattle to Chicago. "David is not going to slay Goliath, and we're not going to try," says Harry Lehr, vice president of planning.

One rare daring move came in November, however, when Alaska launched its first international service — from Seattle to Mazatlán and Puerto Vallarta, Mexico. Analysts say it was a good move because the Mexico service — popular in the winter — offers a seasonal counterbalance to the airline's heavy traffic

north to Alaska in the summer. "Putting those nearly idle planes to work during the winter months in Mexico should only help to improve Alaska's annual profitability," says David Sylvester, Kidder Peabody & Co. analyst.

The airline also tries to use its smaller size to its advantage when it does compete against the major airlines in the West. When Alaska increased flights to California last year, for instance, it exploited its distinction as the West Coast's last regional airline. (Airlines based elsewhere bought all the others.) "We said, 'We'd like to be your hometown airline,'" Kennedy says. "The West Coast looks a lot different from Atlanta (Delta's hometown) than it does out here." In a display of corporate humor, Alaska even painted sunglasses on its trademark Eskimo logo.

Another key to Alaska's success is that management doesn't hesitate to dump a bad idea. Take Jet America, a small Los Angeles-based airline that Alaska bought for \$30.7 million in 1986. Its niche was flying coast-to-coast, but increasing competition from major airlines made it unprofitable. Alaska sacked Jet America about a year later and redeployed the planes on profitable routes.

Despite Alaska's enviable track record, analysts are divided on its long-term outlook. Whitlow says he expects to see it taken over one day because it's so successful. But Sylvester says that's unlikely, at least in the next two years. Alaska's Seattle-Alaska niche is too remote geographically to interest other airlines, he says. Sylvester also believes government approval of more airline mergers is "a long shot." Sylvester says Alaska's stock, which closed Wednesday at \$20 3/4, is worth buying if it dips to \$17 a share.

Managers take one day at a time. "All of our energies are directed to making the next six to 12 months successful," says Raymond Vecchi, chief operating officer. "If we do that, the long term will take care of itself."

"We operate under what I like to call a state of siege," he says. "It keeps us alert and sharp."