

“Selling Canada: Fresh Perspectives on the Quest for New Service”

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Campbell Wilson, Vice President Canada, Singapore Airlines

Thank you, Garth. And, if I can add, my thanks to Jim and the rest of the CAC team for the opportunity to be with you today. It's Singapore Airlines' honour to be here and to share the stage with such an illustrious group.

I've been asked to address the following points:

- What is Singapore Airlines' growth strategy,
- How does Singapore Airlines select new routes. What do we look for and how do we go about developing them.

But before I proceed to these topics, there's a more fundamental question to be addressed: why is SIA's opinion of any value, and why should it hold any interest for you?

It may seem somewhat strange for an airline that serves a single point in Canada, and just thrice weekly at that, to be addressing this conference. There are plenty of foreign carriers with larger Canadian footprints than Singapore Airlines.

As I will explain later, Singapore Airlines relatively small presence here is not a matter of choice.

But why Singapore Airlines, here, at this conference?

I'm sure you're all aware, even if only tangentially, that Singapore Airlines has long been at the forefront of customer service. Back in the 1970s we were the first airline to offer complementary drinks, free headsets and a choice of meals to passengers in all classes of travel. In the early 1990s we pioneered personal television screens in every seat and were the first to offer audio and video on demand. Today, our onboard products again set the standard for space and comfort – an entertainment system with 1000 choices and inbuilt business software in Economy class, a business class seat nearly three feet wide, and a 23-inch personal television in first class

For these, amongst many other reasons, we've been recognized with numerous rewards, including Business Traveller magazine's "best airline" for 15 consecutive years, and Conde Nast Traveler's "best international airline" for 18 of the past 19.

But it's not all about service.

Singapore Airlines, a publicly listed company, is the world's largest airline by market capitalisation. In an industry that has, in aggregate, destroyed more wealth than it's ever created, Singapore Airlines has been profitable every single year, consistently posting annual profits in excess of a billion dollars and with market-leading returns on capital.

In terms of international revenue passenger kilometers, we rank fourth. In the 1990s we were the largest operator of the Boeing

747-400 aircraft and currently have the world's largest fleet of Boeing 777s (a prescient conversion, I might add, given the trend in the price of fuel). The smallest aircraft in our fleet is an A340.

Singapore Airlines has a consistent track record of success. But we're probably a little biased. So I'll simply refer you to 19 March 2007's Fortune Magazine, which contained their annual list of the world's 50 most admired companies – reproduced here.

Singapore Airlines is number 17 - not just the highest ranked airline, the *only* airline on the list.

So that's why Singapore Airlines' opinions may be considered as carrying some modicum of credibility and, given our small presence here, considerable potential for Canadian airports.

But here's the thing: there is no secret to our success. In listening to Singapore Airlines' growth strategy and approach to new markets, you may feel that it's insultingly simple. It's not meant to sound that way and I apologise in advance if it does. It's just that the airline business is just that, a business. Business is, fundamentally, about adequately compensating the businesses' owners. All other decisions are subservient to that. As long as this objective is clear and shared, all else should fall into place.

That is the "end" we pursue, whether a decision relates to fleet, product, network, finances or – yes – the level of service we choose to provide our customers. A modern and frequently renewed fleet lowers fuel burn & maintenance costs, affords negotiating strength with manufacturers and allows good resale value, facilitates regular upgrading of onboard product and minimises environment-related risks to the business from things such as noise and particulate emissions. A high level of service provides branding benefits and a bulwark against commoditization, whilst a good brand, product and physical environment, coupled with high expectations, engenders an enhanced sense of loyalty and commitment from staff and customers alike, reducing advertising requirements and enabling higher yields and market share.

It all comes back to the business.

In aviation, however, there seem to be more than the usual distractions. James Strong, the former CEO of Australia's Qantas probably put it best when he said "the problem with airlines, as businesses, is that they're often full of people driven mad by the smell of avgas."

So let's clear the air.

Firstly, then, what is our growth strategy? We aim to grow, in terms of capacity, by 4 to 6% annually. This plan has obviously been affected by the delay in delivery of the Airbus A380 - for which we're the first customer - but we'll catch up.

Why do we want to grow? Not just for its own sake, or because it's expected of us by our shareholders, but because it's vital to our long-term survival.

Costs don't stay still, so revenue can't either. The steady inflation that so powerfully affects input costs seems to have little influence on airfares. Employees age with an organization and, sometimes, get paid more even as their productivity declines. If revenue stays still, we're going backwards.

Size confers influence, negotiating strength and economies of scale, all critical to success in this brutal industry. Properly managed growth should also enhance network effects, which in turn facilitates more growth. Do we mind that more than 80 airlines serve Singapore? Not at all – besides spurring us to continually improve our product and control costs, they contribute to Singapore's hub and economic strength, which in turn benefits us. As well as transfer traffic, their presence attracts numerous caterers, ground handlers, maintenance companies and so on – who in turn provide a large pool of expertise and enough competition to help keep our own costs in check.

Fundamentally, demand for travel is itself growing: between 1995 and 2005, scheduled international ASK's of all IATA airlines **doubled**. In the longer term, therefore, size determines what place one will take at the table when, as must eventually happen, the archaic ownership restrictions governing this industry change and consolidation can occur more freely.

So that's *why* we grow. What about the *how*?

We aim to add capacity in line with market demand – too much capacity obviously lowers yields and affects the economic return. As I hope I've by now made clear, this is the exact antithesis of our desire. Indeed, our history gives numerous examples of starting service at twice or thrice weekly, then adding incrementally over a period of years as demand – and our own market development efforts – allows, precisely to avoid excess capacity.

We prefer to meet demand via adding *frequency*, which most improves customer choice. Where additional frequency isn't possible due to slot or other constraints, a change of gauge may be the only option. But the market profile must be correct; we are not, for example, going to deploy an A380 on a route unless it will make money. Yes, the A380 boasts lower per seat costs than a B744 – assuming Airbus' 555-seat baseline. But in terms of total trip cost it's considerably more expensive to operate. And when you consider that Singapore Airlines' A380s will have fewer than 480 seats, a lot of the claimed per seat cost reduction evaporates. Furthermore, we've ordered fewer A380s - 19 - than the number of B744s currently in our fleet - 23. Thus, our A380s are clearly

destined for established high-frequently – yet constrained B744 routes - the London's, the Sydney's – and not for developing markets.

Opportunities for growth arise in two ways:

- the market, or aircraft technology, reaches a point where a service becomes viable,
- regulatory impediments are eased.

Aircraft technology is a periodic game changer. The B777 – especially the 200ER - opened up a number of opportunities for airlines, ourselves included. Many of our European services converted to non-stop, as did Johannesburg and Cape Town in South Africa and Christchurch, New Zealand. For the record, we studied Singapore-Vancouver non-stop as well, but sadly, it's just a little too far. The Westbound payload restriction would drown the flight in red ink.

The B787 and A350, with yet lower costs, look set to initiate another game change in the next few years – which is probably why the 787 order book alone already tops 500. Destinations that were too small to be viable suddenly become so. This should be keeping some of you awake at night with excitement!

Sometimes, however, reality doesn't live up to the promise. You are seeing this right now in the ultra-long range market from South East and West Asia to North America. Aircraft that appeared to offer a compelling proposition when launched, such as the Airbus A340-500 in 1998, or the 777-200LR a few years later, no longer appear so attractive following a 400% increase in the price of fuel. There has been much speculation about the future of Thai Airways' non-stop flights between Bangkok and the USA; Thai has publicly admitted that the flights have incurred significant losses. Our own non-stop services to the USA, despite huge markets in Los Angeles and New York coupled with high load factors and yields, are marginal. Vancouver and Toronto, smaller less established and less high-yielding markets, would assuredly lose money.

In short, there's a reason why just 72 ultra-long range aircraft have been ordered despite being available for nearly a decade. Serious expansion in ultra-long range routes of 17, 18 or more hours must therefore await a future chapter in aircraft technology.

Regulatory impediments require little explanation. Some countries still feel the need to dictate the level of choice offered to their own people and businesses. Fortunately, this mentality is, slowly but surely, heading toward extinction. But as we're taking about growth here, we should not lose sight of the fact that overregulation inhibits our growth, your growth, the growth of related businesses, the growth of tourism and the growth of choice. In today's world, more than ever, it behooves us to heed the words of Thomas Jefferson; "travel is fatal to ignorance, bigotry and narrow-mindedness".

Presuming we *can* mount a new service, then, what do we look for? In two words: economic value. As a publicly listed company, we have a duty to adequately compensate our shareholders – 10% of whom live in North America, by the way, so you may well be sitting next to one.

Our cost of capital is around 8%; if we don't exceed that, we're destroying the funds with which we've been entrusted. Any route that cannot, in steady state, positively contribute to economic value has no place in our network. Therefore, the first – and essentially only – consideration when assessing a new destination is “will it add value?”

How do we assess that?

Clearly, a prospective destination must be attractive to the type of passenger we want to carry. We make no apologies for serving the upper end of the market in both business and economy; our investment in product, in an effort to command high yields, requires nothing less.

All sorts of data go into assessing this – booking and uplift data, fare and yield information, industry, governmental, United Nations and other reports, trade and financial records, demographic profiles and trends, analysis of similar routes, deconstruction of other airlines' results, monitoring of developments in other industries and even good old first hand observation. If the majority of passengers boarding some flight from Singapore to Doha appears to be Filipina, why so? Is there an opportunity for us?

Some airports already assist in this process by collating relevant data and regularly updating airline network planning departments – and not just the vice presidents. Speaking as a former network planner, I can assure you that when one is responsible for assessing all the potential new destinations in an entire *continent* – or even *two* continents – anything that helps sort the wheat from the chaff is welcome!

You would nevertheless be surprised how few airports bother to do this, or fail to acknowledge that ideas or solutions occasionally float up from the bottom rather than descend from the top.

And, speaking for distant carriers, don't presume much knowledge of your home market – the analyst may be 25 years old, 2 years out of university and have never set foot on your soil. Until inspired to investigate further, how are they to know that the Toronto urban area's population is, for example, 20% larger than Houston or Dallas and 50% larger than Seattle (all of whose airports, by the way, are in regular contact with Singapore). It is in your interests to provide that inspiration!

Beyond raw market size, we look at the market's structure and competition. Is our catchment area well served already, or do we offer something new? Can we forge a mutually-beneficial relationship with a home carrier, expanding the destinations, benefits and choice available to passengers of both airlines? Is the

regulatory environment conducive to long-term operations and does it offer prospects for growth – are we, in short, welcome?

After crunching all this data, and factoring in competition, capacity and schedules, we'll have an idea of the size of the market relevant to us, and the likely yield we'll enjoy. The next assessment is whether the cost side of the equation can be made to work.

What does that mean to this audience? Most obviously, *your* charges need to be fair. There are many opinions on what constitutes “fair”, and I'll not dig too deep into this can of worms. But, if the best run airlines in the world are barely creating economic value for their owners, and collectively doing exactly the opposite, it goes without saying that every cost element in the supply chain is important to us, and affects the provision of service or frequency.

Cost control must therefore be important to our suppliers, too. By all means, invest in your product. But how many waterfalls does an airport really need? Which will result in more service – yet another sculpture, or better de-icing capacity so that airlines can be confident that they won't incur costly delays during inclement weather?

There should be fairness in other ground services, too. Whilst this is often beyond airport control, you should be aware of the implications and where you *can* facilitate competition, you should. I can assure you that Singapore Airlines has, at least once, elected not to serve an airport – and country – out of concern that there were too few fuel, catering, ground-handling or accommodation suppliers to ensure a competitive market. After investing time, money and our reputation in a new route, we do not want to be held hostage.

Incentives and co-operative marketing support to defray start-up costs of a new route can tip the balance where economics and alternatives are close, or resources scarce. Melbourne Australia, for example, has been very successful enticing carriers ahead of Sydney, and a number of airports south of the border are active in this area too. Unlike airlines, airports and suppliers almost certainly earn a profit from an inaugural flight, and put much less at risk. For airports, a successful new route not only means a new revenue stream, the increased transfer volume boosts the airport's network effect and therefore attractiveness to airlines. This, in turn, spurs the consideration of new routes in a virtuous cycle. Helping to underwrite some of that risk would therefore appear to make sound commercial sense.

The other key contribution airports can make is with regard to policy. Obviously, in Canada's case policy – in the form of crown rents - is a significant factor in your – and therefore our - costs. I am preaching to the converted in this area, I know, but just because the argument is well worn doesn't mean that it's wrong. It is a weight around the ankle of all sectors of Canadian aviation, and plays firmly into the hands of your southern friends.

Regardless of the *facts*, the established international *perception* that Toronto is the world's most expensive airport cannot be helpful to either Toronto or to Canada's quest for new business. A casual observer might be forgiven for thinking, if Canada's main airport is so costly, what does that say about the cost of doing other business? Of living here? Of vacationing here?

More broadly, airports have a vested interest in international air policy.

Clearly, there are many ways to serve a market. As mentioned, given our focus on the customer, Singapore Airlines' preference is always to operate non-stop, provided that it's viable to do so.

Non-stop flights are, unfortunately, not always viable. For one, it can take time to build up a market of sufficient size to sustain non-stop flights, and operating a loss-making service in the interim can be impossible to justify. In other scenarios, the state of technology or external factors may preclude such operations, such as mentioned earlier in context of ultra-long range flights.

Until technology advances further – or fuel price falls considerably for a sustained period - some markets, particularly distant ones, will require an intermediate stop. That's not to say that one-stop services will be with us forever. I've already given a few examples of Singapore Airlines' converting such flights to non-stop when technology permitted. There are many others, in our backyard as well as elsewhere, for instance Emirates' non-stop flights to Australia after establishing the Dubai-Australia route via Singapore.

But let's be clear: until technology catches up, often the choice is not between non-stop and one stop service. It's between one-stop and no service at all.

So now that I've detailed what we look for in a new market, perhaps we should turn the looking glass around. What would make a market unattractive?

Uncertainty of service. Having invested in a route, can we be sure that we'll continue to be welcome? Is, for example, a requirement to apply, every 12 months, for a temporary operating permit just to maintain operations a positive or negative indicator?

Lack of flexibility to consider additional frequency to meet market demand, provide a credible service for the consumer or to adequately amortise fixed costs across is another damper.

We've already established the rationale and requirement for growth, our focus on viability and on the consumer, and explained our measured approach to capacity injection. Let us also be clear that "ability to grow" does *not* equate to "open skies"; far from it. But if a destination allows no expansion *whatsoever*, does one accept the status quo forever or review the options? If non-stop flights remain unviable, and a proximate alternative to a constrained destination, perhaps just over the border in a more

liberal regime, offers that ability, wouldn't that be tempting? And, once change is effected, would it make more or less sense to duplicate operations across two cities rather than consolidating at one? Which one – the location where one remains constrained, or the location that allows growth to occur?

In the case of Canada, Singapore Airlines currently operate to Vancouver three times per week, via Seoul, as we have done for nearly two decades. Our average annual load factor on the route now exceeds 90%, and our traffic catchment – South East and West Asia – is inadequately served.

In an industry where 80% load factor is considered essentially "full", 90% would suggest that more capacity was warranted – perhaps should even be encouraged. Regrettably, the terms of our temporary operating permit cap us at three times weekly, so, with non-stop flights using current generation aircraft unviable, we're stuck.

Because of the high load factors to Vancouver, SIA currently funnels significant Canadian traffic through our US gateways, San Francisco, Los Angeles and New York. Geographically, Vancouver is better placed than it's West Coast US rivals to be a hub for traffic from Asia into North America – and even South America, given prevailing visa and transit restrictions in the US. Toronto, too, could be a much stronger air traffic hub and provide better competition to JFK or O'Hare.

That much of our traffic is now carried via the US is not only inconvenient for our customers, it comes at the direct expense of the Canadian traveler, inbound tourists, Canadian airports and the Canadian business community. Just by virtue of choice, traffic transferring to Canada at a US airport is less likely to travel on a Canadian carrier than would have been the case at a Canadian airport. Is this serving Canada's interests?

To give you a sense of scale: in the last ten years, the number of Singaporeans visiting Canada has increased by 24% - which is, of course, why flights are now full. You may think that 24% growth is good, and in many respects it is. But compare this: during the same ten year period, the number of Singaporeans visiting the USA, which doesn't place any restriction on flights from Singapore, increased *135%*.

A sobering reminder of what could have been. Or, more positively, of what could *yet* be.

In fact, let me give you another comparison. Christchurch, New Zealand, a city of 350 thousand people, hosts a daily non-stop flight from Singapore, 11 hours flying time away – despite being quite close to much larger hub airports at Auckland, Sydney and Melbourne. Besides Vancouver and Toronto, 10 other Canadian cities boast larger populations than Christchurch – including Montreal, Ottawa, Calgary, Edmonton, Quebec City, Winnipeg and Hamilton. In comparison, how well connected are you?

Over the past two decades Singapore Airlines has demonstrated our commitment to the Canadian market and helped establish more demand than capacity can accommodate. We've worked hand in hand with our partners stakeholders in various areas. However, our ability to accommodate incremental Canadian travelers and potential inbound tourists from Singapore and South East Asia is now all-but exhausted. We, too, are therefore currently on a quest for new service. It's necessary for growth and makes good business sense to all concerned.

We *like* it here. We *want* to grow here.

If only we're allowed.

In *your* quest for new service, then, you don't have to look very far.

Thank you.