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Strategic Management Journal: Airline Strategies in Response to Fluctuating Avtur Prices: A Competitive Analysis of the Indonesian Aviation Industry

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Abstract: The airline industry in Indonesia faces complex challenges, including high ticket prices often attributed to the cost of aviation fuel. The article "Expensive Airplane Tickets! Are You Sure It's Because of Pertamina's Avtur?" from the SPP UPMS III Bulletin, edition 03/10/2024, sparked a discussion on the factors determining ticket prices, refuting the dominance of aviation fuel prices and highlighting the role of oligopolistic market structure, government tariff policies, and non-aviation fuel cost components. This journal will analyze these factors in depth using a strategic management approach, covering external environmental analysis, competitive industry dynamics, and strategies implemented by domestic airlines in response to fluctuation of aviation fuel prices. The analysis is enriched with data and case studies of several domestic airlines in Indonesia, providing a comprehensive overview of the competitive strategies adopted to achieve sustainability and profitability amidst intense competition and complex industry dynamics

Keywords: The aviation industry, jet fuel prices, oligopolistic market structure, competitive strategies, domestic airlines, Indonesia.

INTRODUCTION

The aviation industry constitutes a pivotal sector in Indonesia's economy, serving as a crucial link between the archipelago's islands and facilitating the mobility of people, tourism, and trade. Nevertheless, this industry grapples with numerous challenges, notably significant fluctuations in aviation fuel prices. As the largest component of airline operating costs, avtur prices are subject to the influences of global market dynamics, geopolitical factors, and government policies. A recent article from the SPP

UPMS III Bulletin has challenged the prevailing notion that Pertamina's avtur prices are the primary driver of high airfares in Indonesia. The article posits that other factors, such as the oligopolistic market structure, tariff policies, and non-avtur cost components, play significant roles.

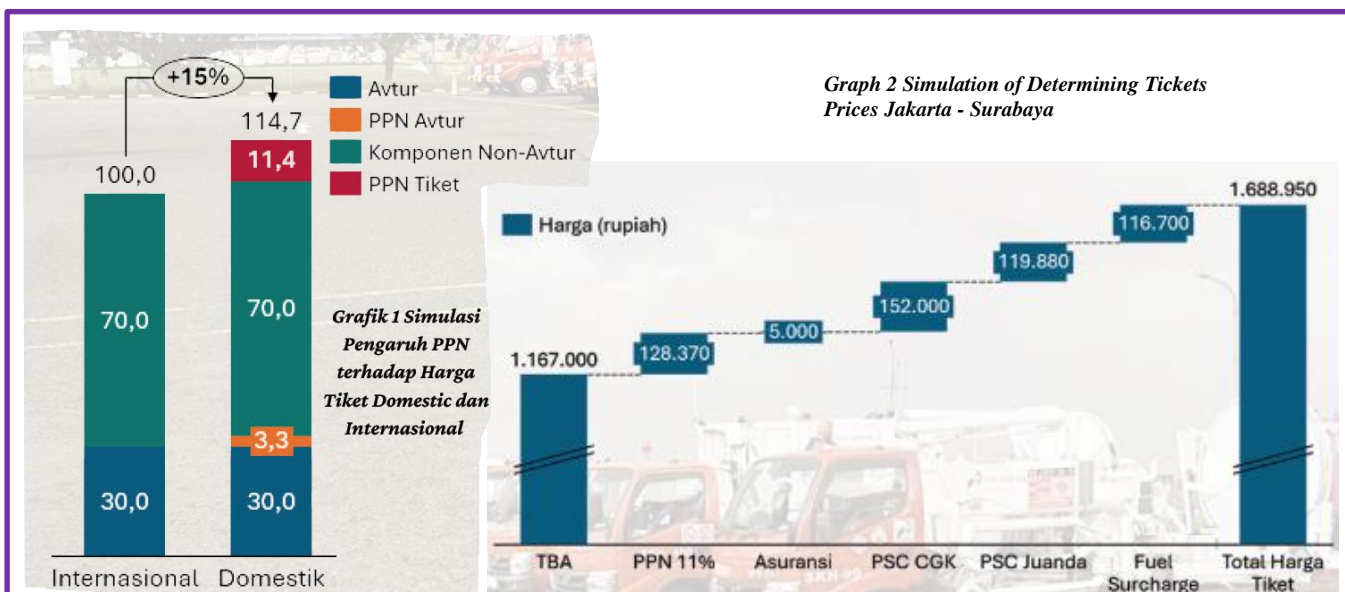
This journal endeavors to delve deeper into this analysis by employing a strategic management framework to evaluate the industry's external environment, map its competitive landscape, and scrutinize the strategies adopted by domestic airlines in response to fluctuating avtur prices. Case studies of several airlines will offer insights into their adaptive and innovative approaches to sustaining competitiveness and profitability in the face of industry challenges.

LITERATURE REVIEW AND HYPOTHESIS DEVELOPMENT

External Environment Analysis

The aviation industry is affected by various external factors that shape opportunities and challenges.

- **Economic Factors.** Indonesia's relatively stable economic growth is driving increased demand for aviation services. However, the volatility of the rupiah exchange rate against the US dollar affects airlines' operational costs, especially fuel purchases and aircraft leases which are generally in US dollars. Data from Bank Indonesia shows that the rupiah exchange rate against the US dollar fluctuated throughout 2024, with a weakening trend in the third quarter.
- **Political Factors.** Government policies, such as the setting of upper and lower tariff limits, VAT regulations, and tourism policies, have a direct impact on the aviation industry. The Minister of Transportation's Decree No. 106/2019 on Upper Limit Tariff (TBA) and Lower Limit Tariff (TBB) is a key regulatory instrument that affects airfare pricing.
- **Social Factors.** Increased public awareness of the importance of air connectivity, lifestyle changes, and the growth of the middle class are driving demand for aviation services. Tourist and business travel trends also contribute significantly to industry growth.
- **Technological Factors.** The development of information and communication technology (ICT) has revolutionized the aviation industry, making it easier to access online ticket booking, improving airline operational efficiency, and providing a better customer experience.



METHODS

Analysis of Industry Structure and Competitive Dynamics

The airline industry in Indonesia is characterized by an oligopoly market structure, where a few large airlines dominate the market share.

Characteristics of oligopoly in the Indonesian airline industry:

- Limited number of players. Garuda Indonesia, Lion Air Group, and Sriwijaya Air Group are the three largest airline groups that control most of the market share.
- Differentiated products. Airlines offer services with different levels of service, facilities, and prices, targeting diverse market segments.
- High barriers to entry. Large capital, complex licensing, and intense competition are barriers for new players to enter the airline industry.
- Interdependence. One airline's strategic decisions, such as pricing or opening new routes, can trigger reactions from other airlines.

Competitive dynamics in the industry are very high, driven by factors such as:

- Price Competition. Airlines compete by offering competitive ticket prices to attract customers, especially on popular routes.
- Network and Route Development. Airlines continue to expand their flight networks and open new routes, both domestically and internationally, to increase market share and connectivity.
- Service and Product Innovation. Airlines innovate by offering better services and products, such as loyalty programs, in-flight entertainment, and digital experiences that enhance customer satisfaction.
- Operational Efficiency. Airlines strive to improve operational efficiency through various means, such as flight route optimization, increasing load factors, using more efficient technology, and effective aircraft maintenance management.

To address the fluctuating price of aviation fuel, domestic airlines have adopted various strategies:

- Hedging Strategy. Some airlines hedge to protect themselves from fluctuations in the price of aviation fuel. Hedging is a financial instrument used to reduce the risk of changes in commodity prices in the future. Garuda Indonesia, for example, has implemented a hedging strategy for some of its fuel needs. However, the effectiveness of hedging depends on the airline's ability to predict the movement of aviation fuel prices and choose the right hedging instruments.
- Fuel Efficiency Strategy. Airlines implement various programs and technologies to optimize fuel consumption. Lion Air Group, for example, has rejuvenated its fleet with new, more fuel-efficient aircraft. Sriwijaya Air has also implemented a fuel saving program through route optimization and flight procedures.
- Revenue Diversification Strategy. Airlines do not only rely on ticket sales as a source of revenue. They also develop other sources of income, such as cargo, excess baggage services, in-flight food and beverage sales, and other additional services. Garuda Indonesia, for example, develops cargo services through its subsidiary, Garuda Indonesia Cargo.
- Negotiation with Suppliers. Airlines try to negotiate with Pertamina to get more competitive aviation fuel prices. However, as the sole provider of aviation fuel in Indonesia, Pertamina has a stronger bargaining position. Airlines can use collective strength through the airline association (Indonesia National Air Carriers Association / INACA) to improve their bargaining position in negotiations with Pertamina.

RESULT AND DISCUSSION

Financial Performance Data and Analysis

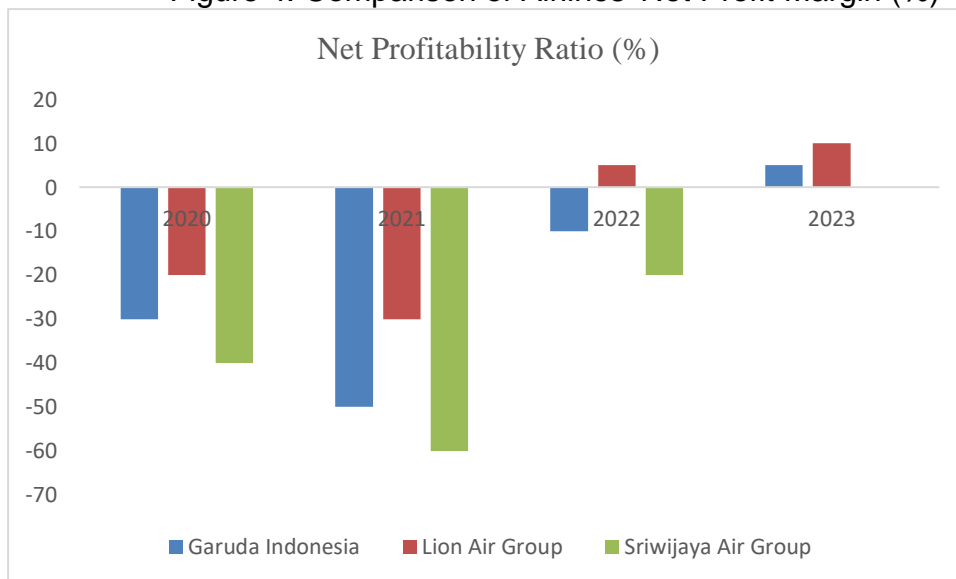
An analysis of domestic airline financial performance reveals how implemented strategies impact their profitability and sustainability. Financial data from annual reports can be used to analyze profitability, efficiency, and liquidity ratios.



Figure 3: Comparison of Airlines' Operating Revenue (in Trillions of Rupiah)

Source: Indonesia Stock Exchange website (www.idx.co.id)

Figure 4: Comparison of Airlines' Net Profit Margin (%)



Source: Indonesia Stock Exchange website (www.idx.co.id)

A financial data analysis indicates that:

- Garuda Indonesia has higher operating revenue compared to other airlines, but its

net profit margin remains fluctuating, influenced by factors such as price competition and exchange rate fluctuations.

- Lion Air Group records significant operating revenue with an affordable pricing strategy, but its net profit margin is relatively low due to thin profit margins.
- Sriwijaya Air Group has lower operating revenue and net profit margin compared to the other two airlines, reflecting challenges in competing in the mid-market segment.

CONCLUSIONS

The Indonesian aviation industry is a dynamic and competitive sector influenced by various external and internal factors. Fluctuating aviation fuel prices present a significant challenge to airlines. However, analysis shows that fuel costs are not the sole determinant of airfare. The oligopolistic market structure, government pricing policies, and non-fuel cost components also play a significant role.

Domestic airlines have adopted various strategies to address industry challenges, including hedging, fuel efficiency, revenue diversification, and supplier negotiations. Case studies of Garuda Indonesia, Lion Air Group, and Sriwijaya Air Group demonstrate the importance of selecting the right strategy aligned with market segments and company conditions to achieve sustainability and profitability.

Recommended Strategies for Airlines

- **Route and Network Optimization:** Airlines should optimize flight routes and develop more efficient networks to increase load factors and reduce operating costs. Data analysis of demand and flight patterns can be used to identify potential routes and optimize flight frequencies.
- **Enhanced Operational Efficiency:** Operational efficiency can be improved through various means, such as using more efficient technology, effective aircraft maintenance management, and increasing employee productivity. The implementation of digital technology, such as online booking systems and integrated flight management systems, can increase efficiency and reduce costs.
- **Service and Product Innovation:** Airlines need to continuously innovate in offering better services and products to enhance customer satisfaction and attract a broader market share. Innovation can be done in various aspects, such as developing loyalty programs, providing more attractive in-flight entertainment, and improving the overall customer experience.
- **Collaboration and Partnerships:** Collaborations with other airlines, airports, and other stakeholders can help airlines improve efficiency, expand networks, and access broader resources. Strategic partnerships can be done in various forms, such as code-sharing, joint ventures, and strategic alliances.

Recommended Government Policies

- **Competitive Pricing Policy:** The government needs to review the ceiling and floor price policies to create a healthier competitive climate and avoid potential price collusion among airlines. Tariff adjustments can be made periodically considering factors such as fuel prices, operating costs, and market conditions.
- **Industry Incentives and Support:** The government can provide incentives and support to airlines in the form of tax breaks, subsidies, and investment facilitation. These incentives can help airlines reduce operating costs and increase competitiveness.
- **Development of Aviation Infrastructure:** The government needs to continue

improving and developing aviation infrastructure, such as airports, air navigation, and other supporting facilities. Adequate infrastructure development will support the growth of the aviation industry and improve connectivity between regions.

- Improvement of Aviation Human Resources: The government needs to support the development of human resources in the aviation sector through quality education and training programs. Competent and qualified human resources will increase the competitiveness of the national aviation industry.

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