

Case analysis & Business Strategy

SRILANKAN AIR LINES



GRADUATE BUSINESS SCHOOL

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Assignment 2

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1.0 Cover Letter

23rd May 2023

C.D. Dissanayake
Business Consultant
Auckland, New Zealand

The Board of Directors
Sri Lankan Air Lines, Sri Lanka

Dear Sir,

**Analysis of Sri Lankan Airlines and Proposal on Five-year strategic plan to Improve
Financial Sustainability.**

While thanking the board of Directors of Sri Lankan Airlines for the opportunity provided to act as a consultant for the company, as requested by the board of directors of Sri Lankan Airlines I have studied the organization in detail with proper background in the first section of the report. During the second and third sections of the report, various theories have been applied along with the SWOT analysis, fishbone diagram on problem and root cause identification, Ansoff matrix, and Porter's generic strategy on identifying the strategic positioning of the company.

Accordingly, I have lined up the required strategic plan for a five-year time horizon along with the SMART objectives and developed a prototype plan of revenue and the profit expectation for the next five years where sequential variance analysis could be conducted to identify the success and gaps to address corrective actions while the strategic direction on the process over the five-year time horizon.

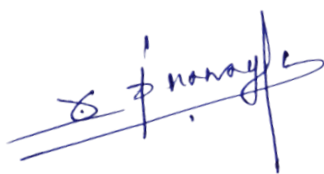
With the conclusion in section five, I have summarized the strategic plan with the required high-level approach and expected results to know when we reach the ultimate expected position.

Trust the proposed strategic plan and the study will provide you with an in-depth understanding of the current level of operation and the corrective actions required to turn around the identified financial loss-making sustainability issue situation of the company.

Should you need any further clarification please feel free to contact the undersigned.

Thank you.

Yours faithfully

A handwritten signature in blue ink, appearing to read 'S. P. Manoj', written over a horizontal line.

Business Consultant

2.0 Introduction

Sri Lankan Airlines is Sri Lanka's premium airline and it's the state airline of the country. In this study, the focus has been drawn to the sustainability issue with Sri Lankan Airlines in terms of financial sustainability. Sri Lankan Airlines is well known within the industry and has respectable records in terms of its quality, and service level. Due to various prospective reasons and situations within the country, Sri Lankan airlines are facing a turbulent situation in terms of financial sustainability and thereby losing their competitive position in the market which sustain for more than seven decades over history.

During this study, attention has been given to the current situation analysis and the reasons for continuous financial performance failures have been identified with reasons. A prospective five-year strategic plan has been proposed to overcome the current financial sustainability issue.

2.1 Background of the Organization

Sri Lankan Airlines (SLA) is established in the year 1979 before that it was named Air Ceylon and currently serves as the Sri Lankan National Airline, with hubs based in Katunayake Bandaranayake International Airport and Matthala Mahinda Rajapakse International Airport. SLA is the largest state-owned airline in Sri Lanka flying over 58 countries globally and over 112 destinations worldwide. SLA operates a 24-hour 365-day service globally. SLA currently serves the nation by using 24 air buses ranging from different airbus models. SLA is currently performing in the market winning many awards in the airline industry but not without its performance ups and downs which were inherited within SLA (Srilankan.com, 2023).

In 1998 Sri Lankan government privatize SLA by transferring its 43.63% shares to Emirates groups. Emirates took over the management and investment approach and started strategically approaching the management of SLA resulting in refitting the entire operational and strategic aspects. Though the new strategic initiatives have led to an increase in profitability due to the civil war in the country customers tend to move away to different optional airlines and four air buses were lost due to bomb attacks from LTTE. In 2010 SLA was bought back to Sri Lankan government from the emirates rising the ownership of the national state to 94%. In 2014 SLA became a partner of the one world alliance (Nagahawatte & Connell, 2016).

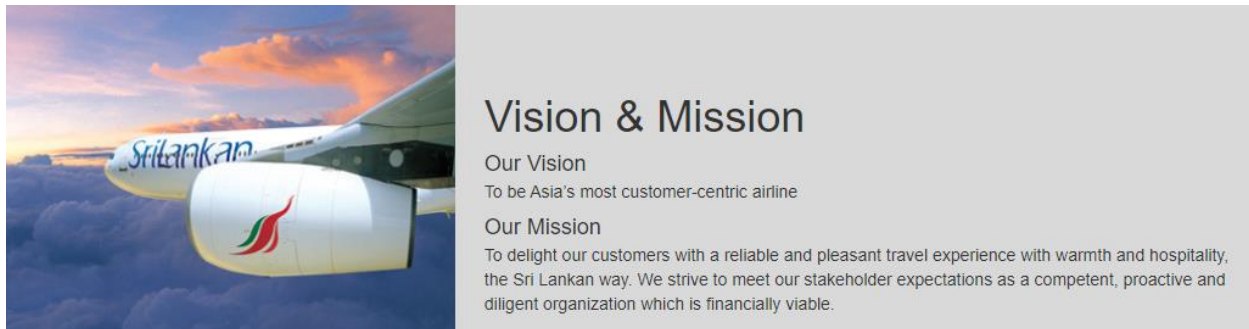


Figure 1 Vision and Mission - Sri Lankan Airlines (Source srilankan.com, 2023)

Over the past period, SLA has won many awards thanks to many factors irrespective of its macro-environmental issues faced within the industry and globally. Having a renowned brand name globally, SLA continuously faces loss-making over the past years has become an issue for SLA and this leads to sustainability issues for the SLA. Many stakeholders are concerned about the continuous loss-making nature of the organization and the strategic direction to overcome the loss-making situation will be discussed in detail with a suitable plan to overcome the same (Annual report, 2022).



Figure 2 Sri Lankan Airlines' current operation (Source: srilankan.com, 2023)

3.0 Sri Lankan Airlines Scenario Analysis

Over the past 10 years, the behavior of profitability of the SLA is captured in Figure 3, which elaborates on the overall loss-making nature of SLA throughout the period.

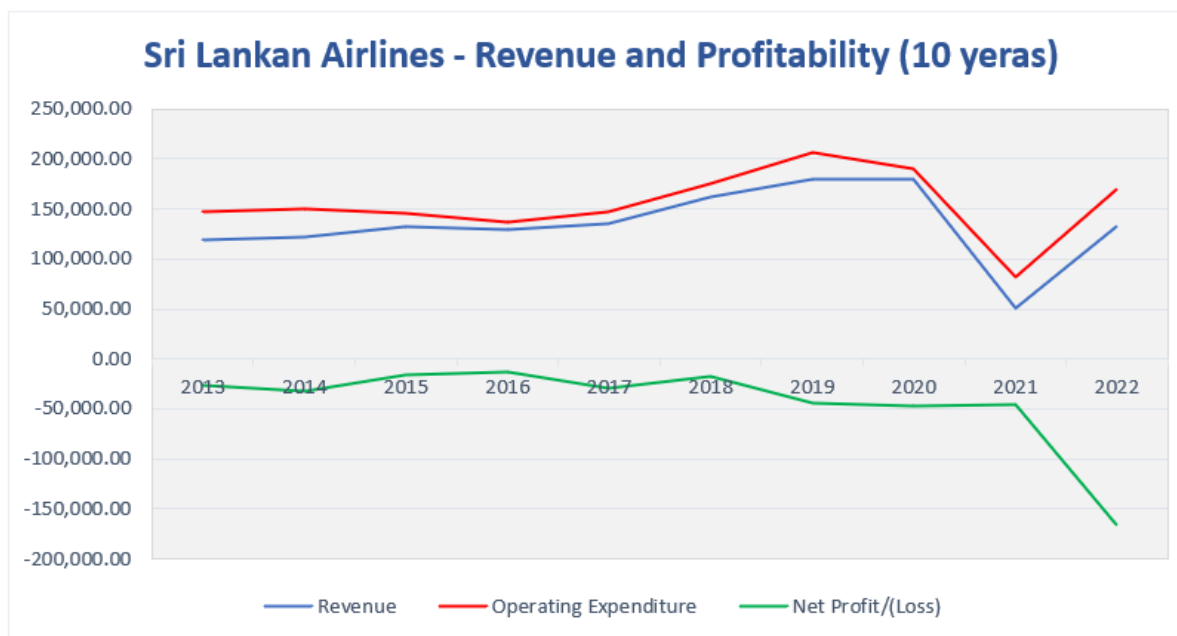


Figure 3 Sri Lankan Airlines Revenue and Profitability (Source: Annual report, 2022) Figures in RS Million

To arrive at the causes of loss making it is important to identify the factors contributing to the continuous losses (*SriLankanAirlines, 2023*).

	2022		2021		Variance	
	Value (LKR Mn)	Contr. %	Value (LKR Mn)	Contr. %	Value (LKR Mn)	%
Aircraft Fuel Cost	42,759	14%	10,569	9%	32,190	305%
Aircraft Maintenance and Overhaul Costs	23,088	8%	13,695	12%	9,393	69%
Employee Cost	17,416	6%	17,112	14%	304	2%
Airport, Enroute and Passenger Expenses	17,753	6%	7,308	6%	10,445	143%
Selling, Marketing and Advertising Expenses	7,250	2%	2,065	2%	5,185	251%
Crew Expenses	3,231	1%	1,680	1%	1,551	92%
Depreciation/Amortisation	14,656	5%	16,745	14%	(2,089)	(12%)
Other Operating Expenses	7,070	2%	6,936	6%	134	2%
Exchange Loss	34,730	12%	6,339	5%	28,391	448%
Operating Expenses	167,953	56%	82,449	70%	85,504	103%
Finance cost	22,904	8%	22,529	19%	173	1%
Exchange Loss on Interest bearing liabilities	107,881	36%	13,334	11%	89,994	675%
Finance Expenses	130,785	44%	35,864	30%	90,167	251%
Total Expenses	298,736	100%	118,314	100%	180,223	152%

Figure 4 Sri Lankan Airlines - expenditure detail 2021/2022 (Source: Annual report, 2022) Figures in RS Million

		Group 2022	Group 2021	Company 2022	Company 2021
Financial					
Revenue	LKR Mn	134,301.36	50,928.92	132,936.23	50,693.85
Operating Expenditure	LKR Mn	133,222.10	76,111.28	132,397.86	74,511.39
Operating Profit /(Loss) before Exchange Loss	LKR Mn	1,692.66	(8,120.21)	1,237.33	(3,188.89)
Loss for the Year	LKR Mn	(163,583.08)	(49,704.51)	(166,369.68)	(45,231.46)
Total Assets	LKR Mn	182,263.33	157,882.80	178,144.17	154,381.41
Shareholders' Funds	LKR Mn	(426,423.83)	(281,490.88)	(437,036.93)	(289,265.27)
Traffic					
Passenger Capacity	ASK Mn			10,144.12	3,816.40
Passengers carried	RPK Mn			4,968.59	748.13
Passenger Load Factor	%			48.98	19.60
Overall Capacity	ATK Mn			1,531.28	794.52
Overall Load carried	RTK Mn			847.33	312.26
Overall Load Factor	%			55.33	39.30
Staff Productivity					
Average strength	Nos.	6,849	6,981	5,833	5,965
Revenue per employee	LKR Mn	19.61	7.30	22.79	8.50
Aircraft Fleet					
Narrow body	Nos.			12	12
Wide body	Nos.			12	12
Aircraft In service at year end	Nos.			24	24

Figure 5 Sri Lankan Airlines Key Financial Highlights 2021/2022 (Source: Annual report, 2022) Figures in RS Million

Based on the above it is evident that the company is continuously making losses throughout the period and significant cost factors are causing a severe effect of the same loss-making factor. Also, the revenue of the company has no major improvements throughout the period though the company is expecting to increase its revenue and market presence positively.

Compared to the previous financial year operating expenses have risen 103% and financial expenses have risen 250% with an overall expense variance of 152% adverse effect on the company (SriLankanAirlines, 2023).

Increase in fuel Cost in compared to 2020/21	LKR Mn	contribution
Increase In fuel price	(17,565)	55%
Increase In volume	(11,872)	37%
weakening of the Sri Lanka Rupee against the US Dollar	(2,753)	9%

Figure 6 Fuel cost contribution 2021 vs 2022 (Source: Annual report, 2022)

Another major factor of cost contributor is an increase in fuel cost of 14% compared to last year of 9% while increasing the volume as well, another factor that affected is average fuel prices increase in the global market causing US \$ 2.25 per gallon.

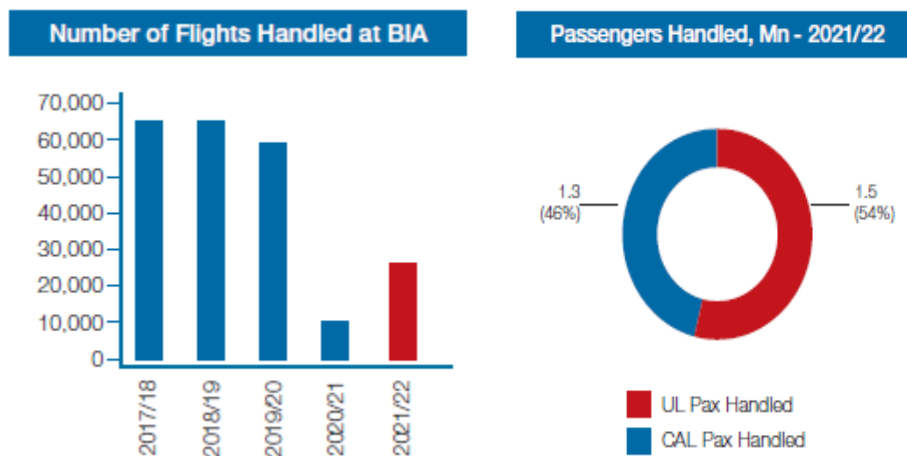


Figure 7 Number of flights/passengers handled at BIA (Source: Annual report, 2022)

Throughout the last 5 years period it is evident that the number of flights handled has come down within recent two years and several global factors also contributed to the same results due to Covid 19 pandemic and global economic conditions along with the Sri Lankan airlines' internal-centric strategic operational issues. In the year 2021/2022 BIA has handled 1.5 million UL pax, and 1.3 million CAL pax. Figure 8 Revenue/ Operating profit and net profit over five years (SriLankanAirlines, 2023).

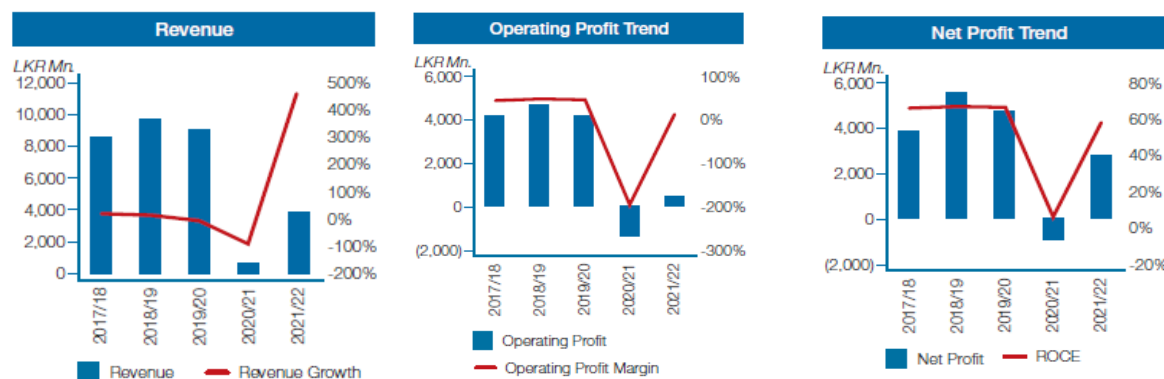


Figure 8 Revenue/ Operating profit and net profit over five years (Source: Annual report, 2022)

Over the five years revenue, operating profit, and net profit has fluctuated and the last two years have had a severe adverse effect in terms of profitability and revenue, many factors have contributed to the results including covid-19 pandemic and global economic condition (SriLankanAirlines, 2023).

By analyzing the financial and business trends over the past years it is evident that the company should consider its strategies and initiatives towards increasing its cost efficiency and profitability.

4.0 SWOT analysis

By analyzing the SLA, below Strengths, weaknesses, opportunities, and threats (SWOT) analysis has been carried out.

4.1 Strengths

1. Strong brand reputation over many decades – Sri Lankan Airlines has had a strong brand image since its inception in 1947 as Air Ceylon
2. High-quality service standards on customer service – The service quality of Sri Lankan Airlines has remarkable footage where it is famous for its high-quality service standards.
3. Flexible travel cost – Sri Lankan Airlines offers various flexible travel plans making its customers comfortable in selecting the airfare based on their budget.
4. Safety records on air travel – Over the past period Sri Lankan Airlines was famous for its safety measures on air travel.

5. Strong brand reputation in Sri Lankan hospitality management – Sri Lankan brand names always well blend with better hospitality management and it has won many awards for the best hospitality management.
6. Best quality trained staff with AITA qualification – Staff is well trained with qualifying as AITA trained staff.
7. Attractive food and beverage services – Sri Lankan food was considered as most attractive food and beverage in the airline industry over the last decades.

4.2 Weaknesses

1. Poorly maintained flights and air busses – though there are many improvements in infrastructure management SLA has many areas to improve along with the airports in Sri Lanka.
2. Many issues with delays and cancellations of flights – In the recent past many issues with flights cancellation and delays have occurred and resulted in a bad customer reputation.
3. Inability to generate profits throughout the period – Due to many internal reasons SLA faces high costs which leads to poor profitability and net losses over the past period.
4. High employment within Sri Lankan Airlines – High staff capacity is one of the major problems in SLA where much unacceptable employment occurs due to unnecessary political involvement.
5. Short-haul operations in flights.
6. High internal operational and maintenance costs – Maintenance costs and other expenses are very high in SLA.

4.3 Opportunities

1. Government involvement in airport development and airline development – Sri Lankan government is investing in many areas to improve the quality of the aviation industry in Sri Lanka.
2. Many tourism development projects – Sri Lankan tourism board with foreign ministry strategically focusing on increasing tourism in Sri Lanka.

3. Sri Lanka has been identified as the best tourist location – in the world by many leading alliances including Lonely Planet and Bloomberg magazine, which create opportunities for air travel.
4. Government focus on expansion and buying new air crafts – With new features enabled air crafts SLA has many opportunities to attract various customers for air travel.
5. Better technology – with many innovative features has been introduced to the travel and aviation industry enabling the more technical savvy digitally enabled services to enhance the customer experience and high-quality service delivery.
6. Better expansion opportunities - many tourists visit Sri Lanka due to high marketing strategies for tourism development. With globalization, many people visit countries other than their own country and the travel industry is facing high growth due to the increase in traveling in the community.

4.4 Threats

1. High fuel costs in the markets – with the current economic crisis in the global economy fuel cost is highly volatile and it affects the airline industry heavily.
2. Increase in wages and salaries of employees in the market – with high labor intensity wages and salaries are increasing due to inflation and this affects the profitability of the airline industry.
3. Poor political stability in the country – Sri Lanka political instability affects the state airline and its profitability as many unnecessary interventions, appointments, and cost restructuring is occurring due to heavy political influences over SLA.
4. Pandemic situation – Covid-19 pandemic and economic downturn in many economies worldwide and in Sri Lanka have adversely affected the airline industry creating threats to operation and sustainability.
5. Increase in competition in the Airline industry – The increase in domestic, budget, and many more offerings in the airline industry has created high competition among airline industries and certain price wars are also in existence.

4.5 Supporting Concepts

4.5.1 Fish bone Theory

Through the fish bone theory, we try to identify the root causes for the sustainability issue of profitability issue in SLA. Proper understanding of the root cause issues reasoning for financial sustainability can be identified through this study. Root cause of the issues are the factors contributing for core issue of financial instability (Dong-xia et al., 2012).

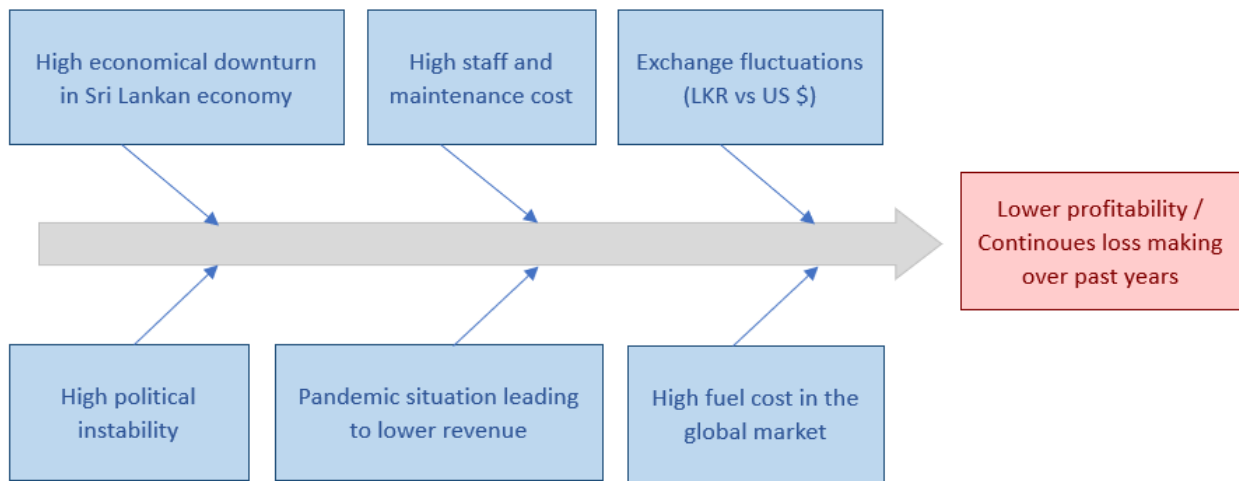


Figure 9 Fish bone Analysis - SLA

4.5.2 Ansoff Matrix

Based on the Ansoff product market matrix SLA will be focusing on a Diversification strategy as it is driving its operations towards new markets along with new service developments focusing on sales growth with existing as well as new customer base (Ansoff, 1957).

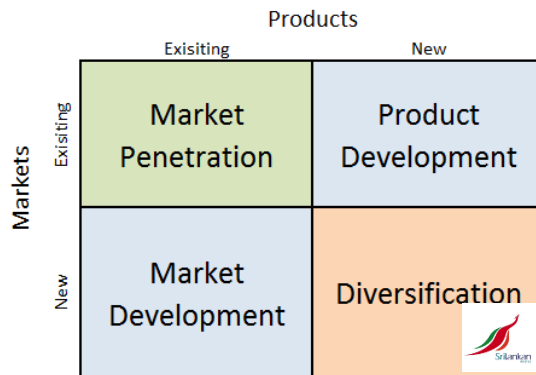


Figure 10 Ansoff matrix for SLA (Source: Smart Insight, 2023)

4.5.3 Potter's Generic Strategy

By analyzing generic strategy it is identified that SLA is driving towards differentiation focus where it has diversified focus groups and it approaches the focus market with a unique differentiation approach, few examples of its targets are Sri Lankans who travel abroad, business travelers, students, pilgrims, tourists, and based on the target market each strategy will be focused differentiate (Cambridge, 2023).

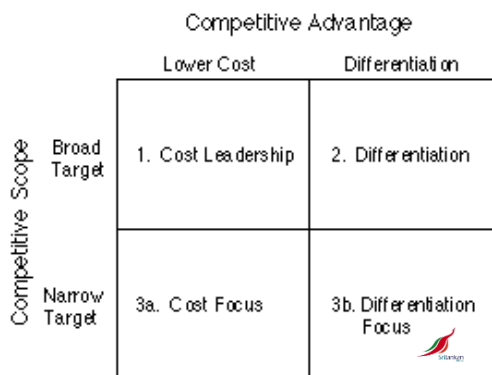


Figure 11 Potter's generic strategy (Source: Cambridge, 2023)

5.0 Strategic Plan

As analyzed using comprehensive SWOT analysis and with supporting theoretical studies it is identified that SLA is suffering from poor management practices in managing the airlines where due to high political influences proper strategic plan has not been applied throughout the period to make the organization profitable.

Though the organization had many strategic plans the operation of the plan has not been successful with a single aim of improving financial performance. Hence, I suggest the below plan for a 5-year period with SMART objectives to ensure sustainable growth for SLA.

Strategic Objective	KPI/ Recommended Action	Output attainability	Outcome measurement
High service quality and cost reduction.	Reduce and restructure staff costs by increasing value for money with high-quality service.	<ol style="list-style-type: none"> 1. Employee productivity will be improved while maintaining a lower cost. 2. Redundant unproductive employees and business units. 3. Outsource or divest lost making functions to a third party. 	An increase in cost efficiency leads to lower costs each time an aircraft flies to its destination, making per-trip profitability increase, resulting enhance in overall profitability.
Expanding the flight destinations and countries and diversifying services.	Introduce budget airlines with a partnership strategy aiming to offer low-cost on-time, a wide range of travel opportunities throughout the world. Should mainly focus on reducing the turnaround time, high travel frequency, and travel to more destinations.	1. Will result in expanding to many markets, with a wide variety of travel needs resulting in market expansion making more profits at a lesser cost.	Able to offer more products and services range by differentiating the customers based on focus differentiation, increasing profitability and market share with revenue growth, and reducing cost due to the low-cost approach on budget airlines.

<p>Improving the cost efficiency in aircraft maintenance and leasing cost through strategic partnerships with peers.</p>	<p>Strategic partnership with other airlines to offer more value-added services to the customer base.</p>	<ol style="list-style-type: none"> 1. Reduce fleet by outsourcing fleets from peer airlines 2. Offering more destinations and countries under the SLA arm to a variety of customers. 	<p>The high-quality service offered, and variety of destinations, enhance travel offerings worldwide improving profitability and reducing costs through strategic partnerships. Customers will long stand with SLA due to its variety of offerings which fulfill travel requirements at a reasonable cost.</p>
<p>Minimize the political influences on SLA operations and management practices</p>	<p>Avoid political interference in the operation of SLA and the recruitment policy at all levels including senior, middle, and tactical management. Appointment for any position should be based on the standard recruitment board appointment procedure with suitable people being</p>	<ol style="list-style-type: none"> 1. Suitable management and leadership will drive the organization in the best interest of the SLA. Employees and related parties will be more motivated with less political influence. 2. Clear strategic direction with proper vision in the best interest of the SLA 	<p>High performance leads to motivated staff and organizational performance improvement. Lower cost with required strategic direction avoiding the interest of political parties.</p> <p>Enhanced goodwill among the market creating super value</p>

	appointed to the required position which ensures smooth function at any level in the hierarchy.	and avoiding personal benefit culture within the organization and improving performance-driven culture.	creation and stakeholder and shareholder satisfaction.
SLA strategy to be linked with Sri Lankan tourism board strategies to create a unique value proposition for SLA.	The collaborative effort and strategic alliance with the Sri Lanka tourist board align both strategic objectives towards one direction of enhancing tourists to the country working with hands to increase revenue using the image of Sri Lankan heritage and beauty.	<ol style="list-style-type: none"> 1. Improving people traveling to Sri Lanka as tourists will increase revenue for both the tourist board and SLA. 2. Enhancing services will create more volume-driven revenue. 	The combined strategy will attract more tourists resulting in increasing revenue, With the release of travel bands after the pandemic will attract more tourists, and high revenue generation can achieve.
Entering into a Currency forward agreement in terms of fuel costing and maintenance.	Due to the highly turbulent nature of the exchange rate entering forward / Currency SWAP contracts with a financial institute to overcome exchange losses.	Well-managed foreign currency operation resulting in reduced and maintained costs without heavy fluctuations.	Reduction in for-ex losses and reduce fluctuations in foreign currency resulting in-less exchange losses.

With the above-highlighted strategic direction, SLA can achieve sustainability in profits and a high financial outcome.

5.1 Risk Factors

It is vital to concentrate on the risk factors when executing strategic goals where SLA is covered with many risk factors. Concerning political risk, SLA should try to minimize the adverse effect of politics as the country's political risk is high at this stage. The Sri Lankan economy is highly risky in terms of economic condition at the moment and careful economic analysis should carry out with the execution of strategy as credit, and interest rates always work with SLA. Legal risk is another factor to be considered as SLA should consider the legal aspect of the country and the organization when executing the strategies.

6.0 Conclusion

With the execution of a strategic plan, it is expected that the SLA will achieve its financial sustainability over the five years and it is expected that the net loss to be diminished by 25% over a four-year time horizon and revenue to increase at 15% rate with the new strategic introduction where at the end of the 5th year expecting to generate Rupees 267,382 Million revenue and make 10% net profit out of the revenue.

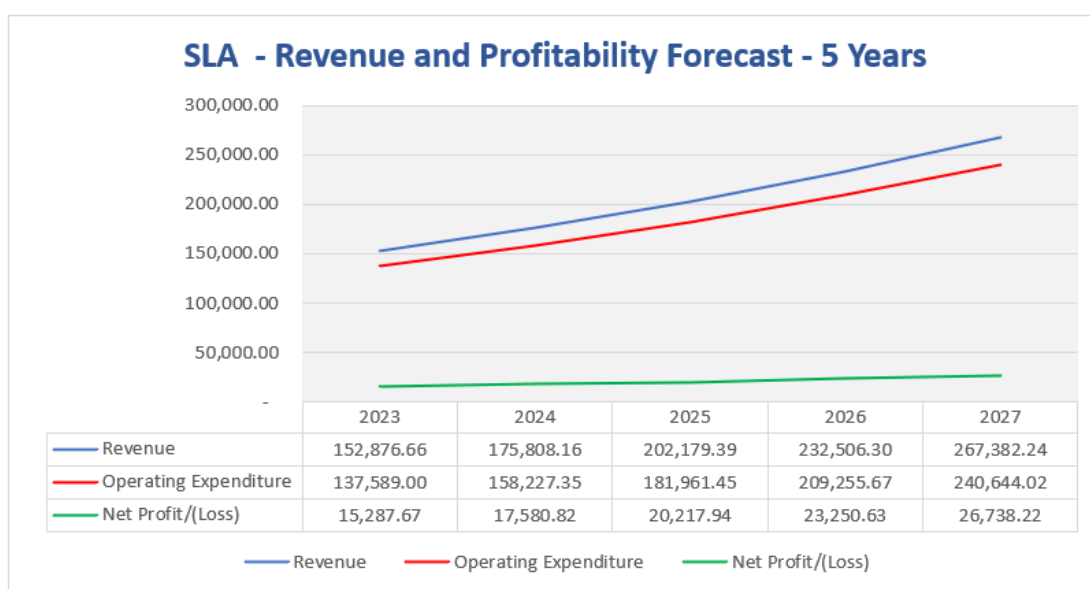


Figure 12 Financial forecast of SLA Figures in RS Million

The above graph depicts the expected revenue and profitability growth over the 5-year period where with relevant variance analysis over the five-year time horizon we can assess the progress and take any corrective actions if deviates from the plan. The financial forecast is based on the year 2023 and an incremental budgetary approach has been used to predict the future profitability prospects.

As the vision of SLA is to become the “most customer-centric airline in the Asian region” with the suggested strategic direction customer loyalty and awareness will be increased and a more diversified customer portfolio can be generated within five years resulting in high growth in revenue maintaining the cost at its maximum lower position.

The suggested strategies of collaboration with peers and strategic alliances will create more diversified revenue streams making the performance of the company the highest standard. The expected cost reduction methods of laying off the unwanted staff and business units and better staff training will lead to efficient cost management and increase the performance of the service delivery. Better management practices with less influence in the political sector will increase the productivity of the SLA, making the airline an efficient and effective service provider to the global world.

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