

**MANAGERS' PERCEPTIONS ON BEST BUSINESS PRACTICES  
IN LOW COST CARRIERS INDUSTRY IN INDONESIA**

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بِسْمِ اللَّهِ الرَّحْمَنِ الرَّحِيمِ

*In the Name of Allâh, the Most Beneficent, the Most Merciful*

*Dedication*

*This thesis is dedicated to my parents, Hajji Mhd. Herwin Tjuatja Dharma and Hajjah Sudewi Hasan for their endless support, do'a and encouragement.*

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## LIST OF ABBREVIATIONS

ABP	Airline Business Performance
ACSI	American Customer Satisfaction Index
AEA	Association of European Airline
AMA	American Marketing Association
AQR	Airline Quality Rating
ASKs	Available Seat Kilometers
ATC	Air Traffic Control
CEO	Chief Executive Officer
CIT	Critical Incident Technique
DAPB	Disruptive Airline Passenger Behavior's incidents
DGCA	Indonesian Directorate General of Civil Aviation
EBIT	Earnings Before Interest And Taxes
EU	European Union
EPS	Earnings Per Share
FSC	Full Service Carrier
h <sup>2</sup>	Communality
HRD	Human Resource Development
ICAO	International Civil Aviation Organization
IDGCA	Indonesian Directorate General of Civil Aviation
ILO	International Labour Organization
IM	Internal Marketing
IPTN	Industri Pesawat Terbang Nusantara
ISME	Index of Service Marketing Excellence
ISO	International Standards Organization
ISQ	Internal Service Quality
Km	Kilometer
KMO	Kaiser-Meyer-Olkin
KNKT	National Transportation Safety Committee
KT (kts)	Knots
LCC	Low Cost Carrier
LCCT	Low Cost Carrier Terminal
RBV	Resource Based View
ROA	Return On Assets
ROE	Return On Equity
ROI	Return of Investment
ROCE	Return On Capital Employed
SOP	Standard Operating Procedure
SPSS	Statistical Package for Social Science
TDM	Total Design Method
TQM	Total Quality Management
USAAF	United States Army Air Forces
MSI	Marketing Science Institute
MITI	Ministry of International Trade and Industry
RITA	Research and Innovative Technology Administration

# **PANDANGAN PENGURUS MENGENAI AMALAN PERNIAGAAN TERBAIK DALAM INDUSTRI PENERBANGAN TAMBANG RENDAH DI INDONESIA**

## **ABSTRAK**

Objektif kajian ini dirangka untuk membangunkan model perniagaan terbaik bagi syarikat penerbangan tambang murah dengan menitikberatkan kecekapan dalaman dan luaran organisasi. Kaedah kajian triangulasi digunakan untuk memberi sumbangan kepada penemuan pengetahuan terkini dalam amalan-amalan perniagaan terbaik. Kajian dasar dilakukan untuk mendapat pandangan awal mengenai teori berkenaan dengan pembangunan model perniagaan terbaik. Untuk mendapatkan pandangan baru dalam pembangunan model, hasil kajian penandaaras memperoleh amalan perniagaan terbaik bagi dua syarikat penerbangan tambang murah dari enam wilayah kajian. Temu bual menerusi panggilan telefon dilakukan dengan pengurus berkenaan untuk meneroka pandangan mereka terhadap tafsiran kualiti perkhidmatan dalaman. Indonesia telah dipilih untuk penyesuaian penaksiran model yang dibina kerana negara tersebut telah disenaraikan sebagai salah satu negara yang mempunyai lebih daripada lima kemalangan nahas kapalterbang dalam beberapa tahun kebelakang. Tinjauan seterusnya telah dijalankan dan data diperolehi menerusi 209 set borang soal selidik yang diterima-pakai. Dapatan kajian mendapati bahawa pemasaran dalaman dan kualiti perkhidmatan dalaman mempunyai kaitan yang signifikan dengan prestasi syarikat penerbangan. Sinergi antara syarikat penerbangan tambang murah dengan pembekal menghasilkan perkhidmatan yang cemerlang dan memperkukuhkan prestasi syarikat penerbangan. Sebagai kesimpulan, dapatan kajian menunjukkan hasil kedua-dua penemuan kualitatif dan kuantitatif merupakan pelengkap antara satu sama lain.

# **MANAGERS' PERCEPTIONS ON BEST BUSINESS PRACTICES IN LOW COST CARRIERS INDUSTRY IN INDONESIA**

## **ABSTRACT**

The objective of the study was to develop a low-cost carriers' excellent business model, with the emphasis on the internal and external organizational competence. The triangulation methods were proposed to contribute to the body of knowledge and give a new insight for business practices. The research process started on the preliminary data gathering. To get a new insight on the theoretical model development, the present study provides benchmarking results on the two best low-cost carrier practices in the six regions. Further, international phone call interviews were conducted to explore the managers' perceptions and interpretations of the internal service quality. Indonesia has been chosen fit for the assessment of the model because it was listed as one of the countries that have more than five aircraft crashes in the last few years. A survey was conducted and the data obtained from 209 sets of usable questionnaires. In quantitative study, unit analysis is strategic business unit and resource based view serves as underlying theory. Based on quantitative findings, it is found that a positive relationship exists between internal marketing and internal service quality. The current study also finds that internal marketing and internal service quality are significantly related with airline business performance. The synergy between low-cost carrier and the supplier produces excellent service and strengthen airline business performance. The study is drawn to the conclusion that both qualitative and quantitative findings are complementing each other.

# CHAPTER ONE

## INTRODUCTION

### 1.1 Background of Study

The awareness and concern among citizens of any country have brought forward the focus to understand the increasing significance of the service industries' output that contributes to a country's economy. Johnston's study has revealed that the focus placed on the 1955 service sector contributes around 50 percent of the UK's gross domestic product and overtakes the product-based sector (Johnston, 2005). Additionally, Kotler (2003) has expressed the intention placed upon the occupational aspect, in which service jobs in the United States have accounted for 79 percent of all jobs and 74 percent of gross domestic products in 2003 (Kotler, 2003).

The United States Bureau of Labour Statistics reports that the service-producing sector will continue to be the dominant employment generator in the economy, adding about 14.6 million jobs through 2018, or 96 percent of the expected increase in total employment (Kotler & Keller, 2012). In particular, the service industry is a pivotal area, where it exchanges the rapid global changes with the attention placed upon the service sector as well as the issue of efficiency of service industries being addressed. In addition, the service sector is predicted to be among major drivers of the future growth (Lovelock, Wirtz, & Keh, 2002).

Business services actually generate more than half of total net of the employment growth in the European Union since the second half of the 1990s (Kox & Rubalcaba, 2007). For example, in the Asian region, the influence of the service sector has extended its area of activity to take over the manufacturing and agriculture,

with its influence expanded to affect more than a half of the country's economic growth. Moreover, reviewing the rest of the Asian countries' economic growth reveals that Singapore, South Korea, Taiwan, Hong Kong, Bangladesh, Pakistan, Sri Lanka and Philippine are experiencing the same affection in expanding the body of economic growth (Lovelock et al., 2002; Lovelock, Wirtz, Keh, & Lu, 2005).

Recently, Euromonitor International has reported that the Malaysian economy is growing and the service sector continues to have contributed 46.8 percent of total GDP in 2010. Indeed, the service sector thrives to be the key driver of growth in Malaysia's gross domestic product (Euromonitor International, 2011a). At the same time, the service sector has contributed 33.4 percent of Indonesia's GDP (Euromonitor International, 2011b), although Indonesia falls short from those countries that have been discussed above. Its service sector does not grow proportionally, yet it has decreased for the last five years. This study is worth to be explored to get better understanding on how the service sector has been developed, especially where the airline industry in Indonesia is concerned.

The increased body of the service sector contributes to the economy which has brought passionate researchers to explore the area of service marketing. Service marketing is recognized as a new discipline because the conventional marketing literature has not explored the unique characteristic of the services before. It has been proven by the shifting marketing definition recently. Service marketing is an interesting discipline which grows as fast as the service sector itself. Thereby, it is important to study service marketing in order for one to build sufficient body of knowledge in the era of service-lead growth. The airline has been categorized as part of the service industry. It is an object to be investigated in the current study. Therefore, the focus of the study is to explore airline services. This study is expected



to find out the extent to which the LCC's excellent business model works to achieve organizational goals.

## **1.2 The Emergence of the New Airline Models**

Airlines have been integral, as part of the transportation sector. The economic growth in many countries has been found to be supported by its air transportation system. It has been illustrated by the Research and Innovative Technology Administration (2008) in the United States, that one out of seven jobs is attached to the transportation industry. In addition, a proportion of almost 20 million people in 2002 are being employed in the transportation industry. The airline business is booming, as a matter of fact, and more air carriers have been innovated. The emerging new business model in the airline transportation industry is commonly known as the low-cost carrier that enables people to travel with affordable ticket prices. It is totally different from the full-service carrier. Specifically, according to Alves and Barbot (2007), the differences are expressed under three important corporate governable implications, between the full service carrier (FSC) and low cost carrier (LCC). Firstly, corporate mechanisms are costly as the FSC have larger boards. The LCC's business manages corporate governable structure in smaller boards, fewer committees and a smaller number of top executives.

Secondly, complex corporate governable structures of FSCs may slow down their decision-making process. This goes against the LCC's business model, but may fit FSCs as their structures rely a lot on code-share agreements, congested airports, the information technology, revenue management systems and other factors that lead them to a slower pace of adjustment. Finally, LCCs may save their corporate governable cost which in turn has to do with the agency's internal issues.

Consequently, it should be expected that these airlines have developed greater incentives for managers to maximize profits and achieve stakeholders' objectives (Alves & Barbot, 2007, p. 116). The low-cost airlines run on the principle of minimizing the costs of operations and maximizing sales' revenues. They strive to increase the market share, load factor and flight schedule on customers' value for money. The low-cost business does not mean that the LCC needs to sacrifice their services. The entrepreneur spirit, enthusiasm and service culture deliver an unrivalled customer service experience. The concept of LCC is upgrading the outcomes of excellent service experience.

The current LCC business model seeks to give more flexibility to the customers in terms of fulfilling what they want and when they are willing to pay for the services. The LCC service is extended to cater for additional services with low price charges. The current LCC business model makes money from the ancillary revenue which gains from non-ticket sources where in the past LCC gained income from ticket sources. In the Asian region, the AirAsia business growth is driven by ancillary income, which continues to rise to MYR44 per passenger, representing 18 percent of the total revenue for AirAsia. Ancillary revenue has increased to 81 percent for the Thai AirAsia and 31 percent for the Indonesia AirAsia (Air Transport World, 2010). Ryanair is an Irish low cost airline which has abolished airport check-in and replaced it with a fast bag drop for those passengers checking in bags (Ryanair, 2009). Passengers are also required to print their own boarding passes, if the customer arriving at the airport without a pre-printed online check-in will have to pay €40 for their boarding passes to be re-issued (Ryanair, 2011).

The current LCC model is different from the previous LCC business model since it has been introduced to the public with some limited services. The Economist

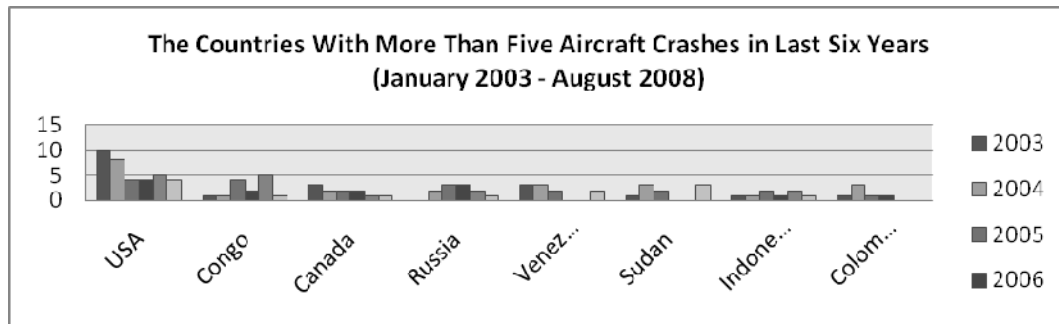
(2007) has criticised the LCC model, especially regarding how the Ryanair serves customers. The LCC is criticised to only place concern on how to make money without focusing on the aspect of the customer services. Ryanair's concept has seemingly lack vision, other than to make money since O'Leary (CEO of Ryanair) introduced the LCC business model. He states that, if Ryanair could have lower costs than anyone else, it could also have lower ticket prices. Similarly, if prices were low enough, it could fill seats on almost any route. However the LCC business model needs to weigh low costs equally with service quality. Four years ago, The Economist (2007) had predicted that an unstoppable business model would soon begin to evolve. Perhaps the LCC needs an excellent business model. The LCC excellent business model needs to emphasise equally on the aspects of safety, low cost and service quality. In fact, some of the LCC airlines have a successful experience in business, whereas some other companies have had to suffer from financial crises.

Recently, several academic papers have discussed the growth of the airline industry (Swan, 2007). In this respect, the findings suggest that the emerging airline models have increased the sense of competitiveness in the airlines industry. Although this industry is well-growing, not many researchers have recognized the misleading facts and statements about how the airline industry has been developed in recent decades. Swan (2007) argues that a number of venerable airlines have disappeared through mergers' processes or bankruptcy. He used the available seat kilometres (ASKs) to illustrate his argument. Swan (2007) concludes that forty percent of the airlines which flew in 1981 have no longer existed in the airline industry, meaning that thirty percent of the ASKs running in 2001 did not exist in 1981, and yet, new airlines were being created at the same time. Moreover, the airlines tend to be running in business or even tried to start up, come and go, meaning that some of those are

identified as small businesses whereas some have faced failure, unlike some others, which are considered as major players (Swan, 2007).

Airline competitiveness is being driven by cost reduction and cost efficiency. Narrowing this assertion down to the LCC model, AirAsia has been awarded the best of LCC airlines by SKYTRAX in 2010. One of the indicators is the low price. AirAsia has succeeded in the low price strategy aligned with efficiency and excellent service. Southwest Airlines and Ryanair are, leading other airlines in terms of the fares. Mostly, low price airlines have adopted the business model as the primary factor to be successful in the industry where they have been admired. The most important part in the success of an airline is placed upon its capability in terms of the efficacy of its management, employees, suppliers and customers. Therefore, the airline's capability will affect the reputation which is gradually established on the basis of reliability and quality of service. Low operating costs and cheap prices have been criticized by scholars and they argue that these are not sufficient to establish the long-term competitive advantage for the growth of a company (Lawton, 1999). This is due to the probable condition whereby the airline will neglect elements of safety and regular maintenance in order to cut costs as it seeks to provide lower fares as compared with the competitors.

Without such capability, the airline service will suffer the consequences. Figure 1.1 gives a clear perspective of aircraft crashes which indicates more than five aircraft crashes in eight countries from 2003 to 2008. The United States have the highest incidents of aircraft crashes among the other countries. The highest number of crashes is documented for chartered aircrafts. The aircraft crashes in the United States have the lowest level of fatalities. However, in other counties such Congo, Sudan, Indonesia and Colombia the airline crashes have the highest level of fatalities.



*Figure 1.1*  
 Countries with More Than Five Aircraft Crashes (scheduled and chartered airlines);  
 Source: Adapted From 100crash.com (2008)

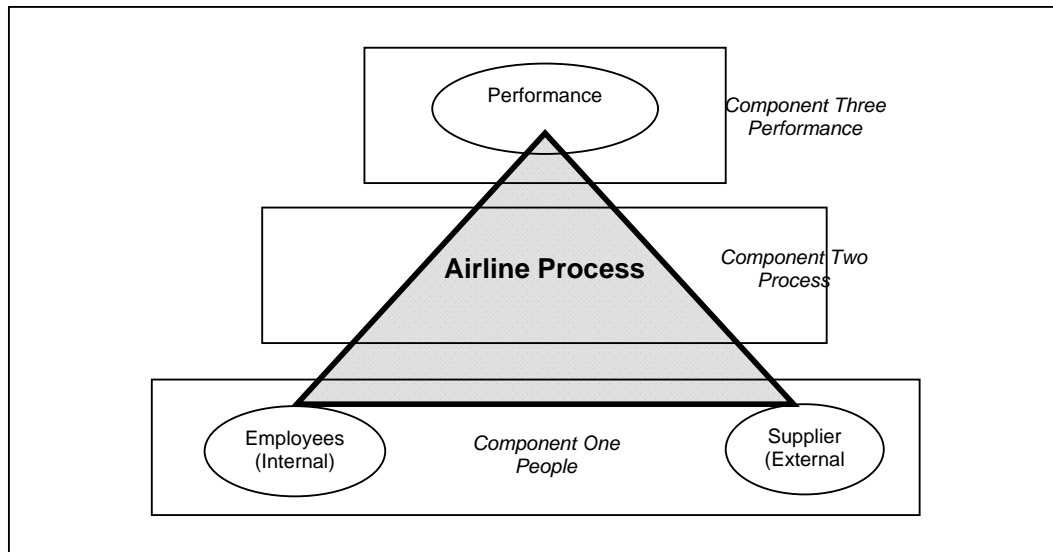
Aircraft accidents have been the cause to kill and injure thousands of people worldwide. More than 86 percent of fatal accidents and 80 percent of all accidents took place in developing countries during 1998 to 2007 (Boeing, 2008). Some countries listed in Figure 1.1 have adopted the LCC business models as major players in the airline industry. Unfortunately, aircraft crashes in those countries have proven that there is a misleading concept on how to operate a low-cost business model, since the LCCs have challenged to implement the low cost strategy to attract the customer with less consideration on the aspect of service quality. The LCC will gain the benefit from repeat customers who have used their service. Satisfied customers will remain loyal and will tell the family and friends about the LCC service quality that can be delighting to customers. The focus on lower cost is not adequate. It is something that is contrary to the concept of service marketing.

Table 1.1  
*The Worldwide Accident Summary Commercial Jet Fleet*  
*(Based on type of operation during 1998 - 2007)*

Type of operation	All Accidents	Fatal accidents	Onboard Fatalities*	Hull Loss Accidents
Scheduled	269	74	5,048	137
Charter	17	4	57	9
<b>Total Passenger</b>	<b>286</b>	<b>78</b>	<b>5,105</b>	<b>146</b>
Cargo	70	12	42	53
Maintenance test, training & demonstration	8	0	0	5
<b>Total Cargo &amp; demonstration</b>	<b>78</b>	<b>12</b>	<b>42</b>	<b>58</b>
<b>Totals</b>	<b>364</b>	<b>90</b>	<b>5147</b>	<b>204</b>
U.S. & Canadian operators	72	13	365	30
Rest of the world	292	77	4,782	174
<b>Totals</b>	<b>364</b>	<b>90</b>	<b>5147</b>	<b>204</b>

*\*External fatalities include on-ground fatalities as well as fatalities on other aircraft involved; Source: Boeing (2008)*

Obviously, the airline service quality will suffer when the employee pays less attention to the airline services' process. Those who fail in the airline business are associated with the higher rates of accident and incident (Rose, 1990). Moreover, operational problems such as the safety issue have been found to be correlated with those who have failed in the LCC business. Rose (1990) uses several data on 35 large scheduled passenger airlines in a particular period of time to investigate the effect of profitability on accident and incident rates. She finds out that lower profitability is correlated with higher rates of accidents and unfortunate incidents that have killed and injured thousands of people. Table 1.1 shows the worldwide accident's summary during 1998 to 2007 which includes all types of airline operations such as scheduled flights, air charters and low-cost carriers or full service carriers. The results reveal that more than 86 percent of fatal accidents and 80 percent from total accidents happen in several countries in the world. Indeed, the majority of those accidents have reportedly happened in the developing countries.



*Figure 1.2*  
 The Three Airline Development Components  
 Source: Fernando, Saad, Haron, and Zailani (2011)

The preliminary study was done through reading news, literatures and interviews on several key resources. The LCC was identified to have lacked the business service philosophy. The aircraft's accidents and incidents are reported to have happened because of human errors. This may be explained by the fact that the airline has executed minimal maintenance activities and in turn, is seemingly diverted by its offering of affordable ticket price. This is not the best practice, as ideally, the excellence in delivering service is produced from highly-skilled employees with sufficient knowledge and competence without neglecting the safety and security elements. Service excellence would be hard to achieve without support from internal and external suppliers. This is due to complex airline service processes. The external supplier has to improve the synergy with organization objectives. It will work in the LCC industry whereas the external supplier is an important part to deliver service excellence.

Shortly, the airline business has three P components that need to be concerned in order to hold out in the market. Figure 1.2 demonstrates the three airline

development components which consist of people, process and performance. To achieve the superior performance, an airline needs to develop the first component. It stands for internal and external people, namely employees and suppliers. It is argued that an airline's success will depend on how it manages service-oriented employees and excellent relationships with suppliers. If this condition is fulfilled, then the airline can move to another critical component. This component involves every detail of the airline process that extends from the way customers plan to travel until they leave the airport. In other words, the success of the third component depends on the second component. In the third component, the satisfaction of customers will make them continue to use the airline service and invite their colleagues. Here, the success of the airline service process will influence their financial and non-financial performances (Fernando, Saad & Haron, 2008a; Fernando et al., 2011).

### **1.3 Research Gap**

This study is conducted in an airline industry setting. The airline industry is chosen because of its significant contribution to the society as a whole. At the same time, the service quality that these airlines offer has been on the decline. Several procedures and researches have been conducted to find a research gap (e.g. observation, interview with key informants, literature review & exploratory study). Thus, the related literature has been found as well to fill the research gap. The mixed research methods are proposed to ensure some extensive research findings are obtained. However, this section will describe the details of the research gap. Although the airline industry has gained much attention recently, the scarcity of research in the area of airline management is an issue that challenges the researcher. Appelbaum and Fewster (2004) have reviewed the literature on empirical studies in the civil aviation industry.



The exact studies that relate to human resource management practices from an applied perspective have not been explored in literature. They argue that the review of literature has become a study of popular themes and contemporary problems in this industry.

Their arguments have received the support from previous researchers. Research in the airline industry is particularly difficult because airline managers are even more secretive and defensive about the academic research that highlights the way the airline business is run than those in other industries (Eaton, 2001). According to Thomas (1997), in reviewing the literature on international aviation, it is clear that researchers tend to analyse the macro-level of the industry. The topic of international commercial airline management suffers from a lack of theoretical and empirical work, and the scarcity of literature from a microeconomic perspective (Appelbaum & Fewster, 2004). According to the American Customer Satisfaction Index (ACSI), compared to four other industries (banks, stores, hotels, phone companies) between 1995 and 2000, airlines have shown the sharpest deterioration in customers' satisfaction (Lovelock & Wright, 2002). The superior service quality which is driven by the excellent employee's performance and human resource management (HRM), is arguably keeping low-cost carriers from flying high (Appelbaum & Fewster, 2004). Ostrowski, O'Brien and Gordon (1993) have stated that the delivery of high quality service becomes a marketing requirement as the competitive pressures on an air carriers have increased more than ever.

Service literature has suggested that attracting and retaining good employees will drive the survival of an organization over a long-period of time. Personnels are the most important assets of the organization and focus is maintained on the attraction, retention and development of the best employees. The airline needs to put

emphasis on the leadership training and the development of all levels within the Company (Comair's Culuka Annual Report, 2007). Hence, by having excited and passionate employees, a service organization is more likely to be able to deliver great quality services to customers. Sadly, not all theories in literature lean on service business practices. This might be indicative of the discrepancy between theory and practice. There is a need to conduct a more comprehensive study to link the current business practice and theory. Hanson and Grimmer (2007) have argued that the hybrid study which relates practice and theory in marketing are extremely limited. This work has been published after analyzing more than one thousand articles published from outstanding marketing journals. They have reviewed articles published between 1993 and 2002. It is thought to be worth mentioning here, that is natural that the people from the industry normally do qualitative study, although the academia prefers to conduct quantitative research.

Amidst the limited comprehensive study which makes insufficient literature in service marketing, this study has tried to develop the LCC excellent business model. The model will place emphasis on the internal and external organization competences. The particular issues on concept development are discussed. Internal Marketing (IM) places people on the centre stage to correspond to the organizational success. The IM has been suggested as a link to the specific strategy of developing competencies, which are in turn linked to each individual's intelligence, creativity, responsibilities and experiences. The IM does not only manage the individual, but also the collective group that makes up the organization (Ahmed & Rafiq, 2003).

IM is an unusually slippery concept, easy to visualize and yet exasperatingly difficult to operationalize (Ahmed & Rafiq, 2003). The IM construction requires further development and elaboration to distinguish it from similar HRM constructs

(Carruna & Calleya, 1998). According to Panigyrakis and Theodoridis (2009) there is an urgent need of confirmation and a cross validation of the IM scale or similar measurements in more contexts and cultures. IM's research is also required to establish the relationship between components of the IM mix and organizational competencies. There is a need to concentrate on the specific sectors in service organization (Ahmed, Rafiq & Saad, 2003). Thereby, the previous study had failed to find or maybe close, the gap between IM and business performance (Ahmed, et al. 2003).

The gap between IM and business performance exists because of the other factors in service literature that have not been fully explored yet. The current study proposes that the internal service quality (ISQ) functions as a mediator to fill in the gap. The ISQ creates the awareness among employees about the importance of focusing on the company's excellent service at all times. The fundamental theory of ISQ lies in the way a company evaluates a proper service delivery process. Unfortunately, the existing concept is not seemingly clear enough in explaining the true nature of ISQ.

Therefore, there is a need to re-think about the concept and the direction towards which the ISQ is heading. The ISQ is not only a copy-and-paste system from the external measurement of service quality. This is the way a company evaluates the quality of service internally before it is evaluated by their external customers (Fernando, Saad & Haron, 2008b). The ISQ construction development could also be considered. Thus, the importance in establishing a comprehensive view of performance measurements to indicate the overall health of a business needs to be highlighted. The organization outcome can then be more fully aligned with business strategy (McAdam & Bailie, 2002).

#### **1.4 Problem Statement**

Research in airline business is very critical. It is because the quality of airline service which is declining, unlike the growth of the industry itself, may be put under the limelight in this array of research. The previous studies have failed to uncover the LCC excellent model. Therefore, there is no schematic LCC excellent model available in the service marketing literature. This is necessary since the philosophy to run business services has been suggested through employees' capabilities. Employees will improve the quality of service to prevent service failure, sustain business, increase competitiveness and enhance performance. Natalisa and Subroto (2003) have found that service quality is very important in the domestic airlines in Indonesia. They suggest that the airline organization promotes IM activities and studies internal aspects of service quality. Natalisa and Subroto (2003) study service quality based on FSC. Schematic model is suggested in the logic of the service operations.

Therefore, to build the schematic model, there are two important suppliers to be considered in the airline success. The first is the internal supplier. A higher level of employee's capabilities is necessary to deliver excellent service to the customers. Hence, companies need to acquire, motivate, communicate, retain, empower and reward the skilful employees because the airline service's value lies on the heart of contented and satisfied employees. If they are happy and satisfied, then their performance in serving customers will definitely reflect these feelings. They will ensure the smooth-running of every single stage of the airline service processes, and with that, comes the genuine concern. The second is the external supplier. In the rapid growth of airline business, it is highly important to establish a long-term relationship with suppliers.

Airline service process is complex compared to other service industries. An airline will find it hard to compete with its competitors in the market if it makes high investment and other higher operational costs (e.g. web-integrated system, mobile phone application for check-in, maintenance, repair and overhaul (MRO), multi-sorting baggage handling system). To remain competitive, some of the low-cost airlines have even outsourced their airline processes to other parties. The outsourcing strategy is implemented in order to reduce the cost and this tends to affect the airline service quality. The managements should create close relationship with those parties as key suppliers to improve their airline service and communicate with them in order to show the pivotal nature of the quality of service for business competitiveness. During prior primary data-gathering, the researcher has asked the LCC manager the question “how could your company survive in this business”, and to which the LCC manager has commented:

*“To survive as a key player in this industry, we strive to minimize cost; enhance employees’ capability and technology as well. We realized that this industry is a high investment, hi-tech and full of hyper-competition. Working together with partners strongly helps to achieve company objectives” (PS-MB-03).*

If the airline service quality suffers, this will impact the company’s image and business performance. Subsequently, the company also notices the importance of partners in supporting the airline business since high quality supplier is a competitive weapon in the industry. Therefore, the airline needs to establish long-term relationships with internal and external suppliers, as this could be one way to reduce costs and improve service quality. Unfortunately, less attention has been paid to the LCC service process. Indeed, there has been no research model that will be able to discuss the synergy between internal and external suppliers in order to improve LCC business performance (Fernando et al., 2008a; Fernando et al., 2011).

This industry needs an excellent business model to survive. Indeed, there is not enough research done on this setting making it a challenge for the researcher to continue working on this study. The mixed research method has been argued as the best way to develop an excellent business model, and the synergy from the proposed model to build the LCC is an excellent model is tremendous. This includes the internal and external suppliers as the key performers. It has been argued that the LCC model will be helping the airlines to survive in the market, and as for the customers, through the implementation of such model, they will also be enjoying the high quality service with an affordable ticket price.

### **1.5 Research Questions**

This study would develop an excellent business model for the LCC. The validation of this model is needed to be tested in the LCC industry. Indonesia is chosen because it is listed as one of the countries that have more than five aircraft crashes in the last six years (Figure 1.1). This country also has experienced service quality problems in the LCC setting. Further discussions on Indonesia's airline industry would be provided in Chapter Two. The result is expected to produce a proposed model that fits and is ready to be tested in other settings. Based on the existing gaps in the literature review, the research questions posed by this study are as follow:

1. What are the internal and external key factors for an excellent business model among the best LCCs worldwide?
2. How is the actual manager's experience fare with regards to the ISQ measurement in LCC organizations?
3. What is LCCs' excellent business model?

4. What is the relationship between the IM and the ISQ in Indonesia's LCC industry?
5. What is the relationship between the IM and the airline business performance (ABP) in Indonesia's LCC industry?
6. What is the relationship between the ISQ and ABP in Indonesia's LCC industry?
7. Is the ISQ the missing link in the relationship between the IM and ABP in Indonesia's LCC industry?
8. What is the role of suppliers' relations in the ISQ and ABP's relationship in Indonesia's LCC industry?

#### **1.6 Research Objectives**

This study would present evidence that such excellent model of LCC exists and would provide empirical evidence to the alleged role of service marketing in the LCC setting. The objectives of this study are manifold. They are:

1. To determine the internal and external key drivers towards an excellent business model in the best LCCs worldwide
2. To gather the actual manager's experiences with regards to the ISQ measurement in LCC organizations
3. To develop an excellent business model for LCC
4. To identify the relationship between the IM and ISQ in Indonesia's LCC industry
5. To determine the relationship between the IM and ABP in Indonesia's LCC industry

6. To determine the relationship between the ISQ and ABP in Indonesia's LCC industry
7. To examine the moderating effect of suppliers' relations between the ISQ and ABP in Indonesia's LCC industry
8. To determine the mediating effect of the ISQ on the relationship between the IM and ABP in Indonesia's LCC industry

## **1.7 Significant of Study**

The study on service marketing is necessary to improve one's knowledge and understanding towards the LCC industry. The two most significant arguments for this study are:

### **1.7.1 Theoretical Significance**

This is a comprehensive study which combines both qualitative and quantitative research methods. It will make significant and lasting contributions to the body of knowledge in the service marketing area. Marketing scholars have identified this method as a relative paucity. The theoretical contribution of this study develops a new business model and extends the IM, ISQ and ABP theories. The new dimension has been suggested to have accommodated the IM's previous measurement by Ahmed et al. (2003). The attempt has been made to revisit the ISQ in order to understand and improve the concept from multiple perspectives. In addition, the ISQ model for service development is presented, which includes several stages such as the definition, objective and new measurement. The integrated measurement of the ABP is also proposed in this study.



### **1.7.2 Practical Significance**

The essence of this study changes from the traditional management perspective to the adoption of the service-marketing mindset. This result is also probably able to become one of the research pioneers in the LCC airline service industry. This approach is expected to produce a new excellent business model and enhance the ABP in the LCC industry. The research suggestions and implications for LCC managers are also provided. As an indication, the LCC manager who implements the LCC's excellent model has the opportunity to survive in the market. The findings will also suggest a deliberate shift towards transforming important employees' skills for the sake of the company's future and to ensure its success. The outputs of this model also provide a greater level of service and safety quality. Thus, the community will also enjoy the high level of quality service which is offered by these LCC organizations.

### **1.8 Scope of the Study**

This study focuses on a business strategy to provide excellent services. Superb service quality will enhance LCC business performance in the market place. Hence, the model is developed to be tested. Indonesia has been chosen for the assessment of the model fit. If this model is supported, then the future research can be employed in other settings to survive in the hyper competitive market. The research scope is the Indonesian commercial airlines, which cover 44 airlines registered with The Indonesian Directorate General of Civil Aviation (DGCA) in 2008. They are 17 scheduled and 27-chartered airlines including full service and low cost carriers (LCCs). Ten airlines were identified to practise a low-cost business model in the industry.

## 1.9 Description of Terminologies

In this section, working definitions of the principal variables will be described briefly. This is to ensure that a common understanding of the terms throughout the thesis can be derived. A more detailed definition will be supplied in the literature review section. These are major variables.

### **Predictor Variables:**

*Internal Marketing* is a philosophy for managing the organization's human resources based on a marketing perspective to build internal competencies for external success (George & Grönroos, 1989).

*Strategic reward* is new pay (Lawler, 1995; Zingheim & Schuster, 1995) that includes performance-based variable pay (individual and group based), skill-based pay (competency or knowledge based plans), broadbanding, team-based pay and recognition programs (Singh, 2002).

*Internal Communication* refers to the strategic management of interactions and relationships between stakeholders at all levels within organizations (Welch & Jackson, 2007)

*Training and Development*, Training aims to improve current work skills and behaviour, whereas development aims to increase abilities in relation to some future position or job, usually a managerial one (Dowling & Welch, 2004).

*Senior Leadership* refers to an organization's senior management group or team. In many organizations, this consists of the head of the organization and his or her direct reports (Harrawood, 2009).

*Empowerment* is the process to give staff real authority in their work to achieve continuous improvement and job satisfaction in an organisation's

performance for better quality products and customer service in order to remain competitive (Kinlaw, 1995).

**Mediating Variable:**

*Internal Service Quality* is a self service evaluation based on a marketing approach that involves monitoring and measuring inter-department performance in order to maintain service quality consistency (Fernando, Saad, & Haron, 2012).

*Employee competence* refers to individuals' ability and capacity to act in a wide variety of situations to create both tangible and intangible assets (Sveiby, 1997).

*Process* refers to the interaction with service personnel within that environment during the service performance (Bendall-Lyon & Powers, 2004).

*Safety* refers to the management of risk with the goal of eliminating, reducing, and or mitigating injury and loss because of accidents and incidents (NBAA, 2007).

*Punctuality* refers to the ability to perform the promised service dependably and accurately (Zeithaml, Pasuraman & Berry 1990).

**Moderator Variables:**

*Supplier Relations* are often discussed as a general concept, as most of the empirical studies look at specific aspects of managing supplier relations, such as collaboration and cooperation...(Field & Meile, 2008 p. 187)

**Criterion Variables:**

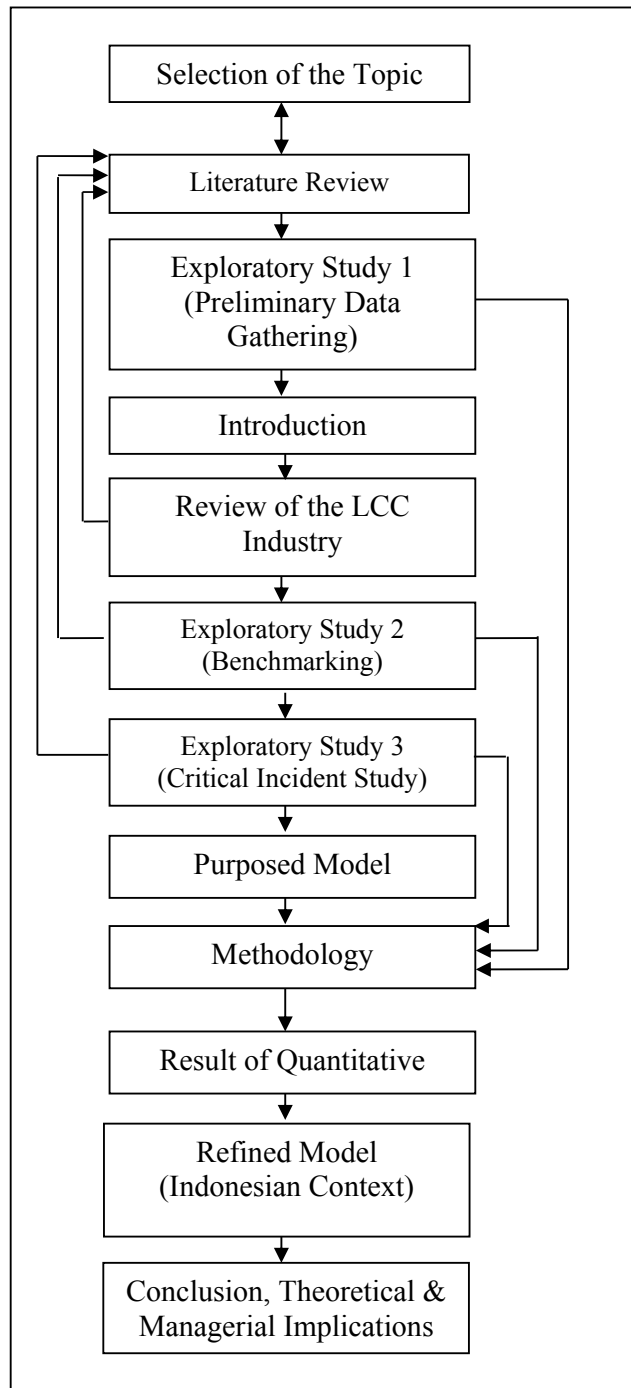
*A Scheduled Airline* is an airline that publishes a timetable and operates its service to a distinct schedule and sells to the public at large (Hayman, 2009).

*Business Performance* is the achievement of organizational goals related to profitability and growth in sales and markets share, as well as the accomplishments of general firms' strategic objectives (Hult, Robert, Hurley & Knight, 2004).

**1.10 Research Process**

This is a mixed research method also named triangulation. In social science research, the definition of triangulation is provided by Downward and Mearman (2007, pp.80) which implies combining together more than one set of insights in an investigation, and there are many early implicit uses. A triangulation research method is used to develop an excellent business model. A business model is defined as a strategy by which a firm builds and uses its resources to offer its customers a value (Afuah & Tucci, 2000).

Figure 1.3 shows the research process. To rephrase, this topic has been selected because of the importance of the air transportation services that has contributed to the country's economic distributions. There are three exploratory studies included, and the research process starts on the exploratory study one with regards to the airline industry. The preliminary data gathering is conducted through ample literature review and interviews. Based on that, the research gap is found and the research problem delineated. Subsequently, the process continues to review related services-related literature.



Source (author)

Figure 1.3  
Research Process

The emerging LCC industry growths shall be provided in the next stage. In addition, to get a better understanding of the LCC model, the Indonesian experience on the low cost airline service quality has been described. The interview results, on the future of the LCC industry has been done at the end of the industry review. Other than that, the exploratory studies two and three are also conducted to obtain some robust findings. The results of exploratory studies have presented the content analysis on the annual report (benchmarking) and international call-phone interviews. After that, the exploratory studies conclude with the discussion on the LCC failed business characteristics.

From the previous process and data, the theoretical development will then be explained. The theoretical development is developed from the existing literature. The theoretical framework names LCC as an excellent business model. The model itself is derived from literature and exploratory studies, although some arguments have claimed that this process is insufficient. There is a need for the model to be tested in the industry. Thus, the next stage has presented the detailed methods of the study on triangulation. The data analysis section has presented the quantitative results. The refined model in the Indonesian context is also presented. At the end of the study, the last section draws some conclusions and other theoretical and managerial implications.

### **1.11 Organization of the Chapter**

The thesis will be presented in the following manner. Chapter One consists of the introduction to the research. The overview of the literature study is discussed in Chapter Two. Chapter Three refers to LCC business practices and the said practices in Indonesia as well. Chapter Four contains the analysis on the qualitative study that

includes the data gained from the LCC worldwide, the benchmarking practice and manager's actual experiences on the internal service. Chapter Five deliberates on the theoretical development and research hypotheses. A review of previous studies, gap, benchmarking LCC worldwide practice and critical incident technique (CIT) analysis have also been identified which form the basis for the conceptual framework. What follows next is Chapter Six that contains the philosophy of the mixed method study, research design and methodology. This chapter takes into account the interview protocol, research approach, sampling design, data analysis, questionnaire development and administration. Chapter Seven analyses the quantitative data, presents the findings and interpretations. Finally, Chapter Eight discusses the inevitable research findings, conclusions, implications and suggestions for future research.