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Price Competition Leads to Profit Warning From Ryanair

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Abstract (Article Summary)

Ryanair reported its third-quarter results a week ahead of schedule to avoid coinciding with an expected negative ruling from the European Commission on whether the airline accepted illegal subsidies from a state-owned airport at Charleroi, outside Brussels. Newspapers reported on Wednesday that the European transportation commissioner, Loyola de Palacio, would rule against Ryanair, forcing it to repay from 3 million to 13 million euros (\$3.8 million to \$16.4 million) in discounted charges, mostly landing fees. The rebuff would undermine Ryanair's strategy of negotiating favorable deals with secondary airports, often state-owned.

In the quarter that ended in December, Ryanair's after-tax profits rose 10 percent over the period in 2002, to 47.5 million euros (\$60 million), not including a charge of 6.6 million euros for retiring some planes early. Revenue was up 37 percent, to 255 million euros (\$322 million). Passenger numbers jumped 54 percent, to 6.1 million, pushing Ryanair ahead of easyJet as Europe's biggest budget airline.

[Michael O'Leary], chief of Ryanair, at a news conference Jan. 14, when the airline disclosed its plans to double passenger numbers. (Photo by European Pressphoto Agency)(pg. W1); Ryanair passengers arriving in December at Charleroi airport in Belgium, where the airline is being accused of taking illegal discounts. (Photo by Bloomberg News)(pg. W7)

Full Text (859 words)

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Ryanair, the low-fare Irish carrier, warned on Wednesday that profit in its financial year ending in March could be down as much as 10 percent as its revenue per passenger plummets.

Ryanair said that it expected to post net income of 215 million euros, or \$272 million, at the close of its financial year. The airline had a net profit of 217.3 million euros in the first three quarters, so the profit warning also signaled that the company expects to see a loss -- its first -- in the current quarter.

Ryanair said that it expected revenue per passenger to slide 25 percent to 30 percent in the current quarter over the year-ago period. The constant need to cut ticket prices was responsible, the airline said, now that large state-owned airlines are copying its low-fares strategy.

"We don't have an explanation for the yield decline," Michael O'Leary, chief executive of Ryanair, said in a conference call. "We speculate that there's intense price competition."

The profit warning, the airline's first, prompted some analysts to say that the brash carrier, which is modeled on Southwest Airlines in the United States, has reached the end of its rapid expansion. Shares in Ryanair fell 28 percent on the Irish stock exchange, to 4.86 euros (\$6.14), their lowest level since October 2001, and 30 percent, to 4.70 euros, in London.

Ryanair reported its third-quarter results a week ahead of schedule to avoid coinciding with an expected negative ruling from the European Commission on whether the airline accepted illegal subsidies from a state-owned airport at Charleroi, outside Brussels. Newspapers reported on Wednesday that the European transportation commissioner, Loyola de Palacio, would rule against Ryanair, forcing it to repay from 3 million to 13 million euros (\$3.8 million to \$16.4 million) in discounted charges, mostly landing fees. The rebuff would undermine Ryanair's strategy of negotiating favorable deals with secondary airports, often state-owned.

Revenue per passenger is falling as Ryanair continues to add capacity and cut fares -- in the last quarter, ticket prices dropped 11 percent from a year ago -- in the face of increased competition. For passengers in an industry where there is little customer loyalty, flying will become even cheaper, analysts say.

Mr. O'Leary said that he expected the fall in revenue per passenger to ease, starting in April, and promised that Ryanair would "always offer the lowest fares in all markets."

Ryanair's average ticket price is 39 euros (\$49). John Mattimoe, an analyst at Merrion Capital in Dublin, said, "There's only so much in absolute terms that that can go down."

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Figures that robust, and Ryanair's previously uninterrupted growth in quarterly profit, are unlikely to be repeated in the short term. In a conference call, Mr. O'Leary said that Ryanair was facing six months to a year of uncertainty.

"Ultimately this isn't something that could just go away," said Kevin McConnell, head equity analyst at Bloxham Stockbrokers in Dublin. "We're seeing more and more entrants to the low-cost area."

Ryanair remains well positioned to compete against newer entrants, analysts said. EasyJet, its closest rival, has per-passenger costs that are 40 to 50 percent higher than Ryanair's, Mr. Mattimoe said.

In the conference call, Mr. O'Leary tried to forestall any attacks on his aggressive strategy.

"There will be a lot of analysis that says we grew too fast, that 60 percent capacity growth this year was much too much," he said. "To which I would answer, well, we did 55 percent capacity growth last year and we did a 59 percent increase in profits."

Ryanair recently established new hubs outside Rome and Barcelona, and half the airline's 146 routes are less than a year old. From May onward, its capacity will grow 20 percent a year instead of 50 percent, Mr. O'Leary said.

Even if the profit warning does not signal a weakness in Ryanair's business model or a failure stemming from its rapid expansion, analysts said the airline was likely to face a period of more modest performance until, as it hopes, its new competitors drop out of the market.

"This is something that has caught them off guard," Mr. McConnell said. "This is the first chink in the armor."

[Photograph]

Michael O'Leary, chief of Ryanair, at a news conference Jan. 14, when the airline disclosed its plans to double passenger numbers. (Photo by European Pressphoto Agency)(pg. W1); Ryanair passengers arriving in December at Charleroi airport in Belgium, where the airline is being accused of taking illegal discounts. (Photo by Bloomberg News)(pg. W7)

[Graph]

"Profit Warning"

Ryanair's share price on the London exchange tumbled yesterday on news that profit for its current fiscal year is expected to decrease by 10 percent.

Graph tracks Ryanair's daily closing share price since Jan. 5.

Yesterday: 4.70

(Source by Bloomberg Financial Markets)

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