

Air New Zealand: Out-Sourcing Maintenance[©]

National flag carrier, Air New Zealand's fleet includes 19 wide-body Boeing 747s, 767s, and 777s. Air New Zealand Engineering Services (ANZES) provided heavy maintenance of Air New Zealand's wide-body Boeing fleet.

Heavy maintenance is detailed work in a hangar, and requires an aircraft to be out of service for more than two days. It is usually classified as either "C" or "D" checks, which are scheduled every 12 to 18 months and five to six years respectively.

ANZES wide-body heavy maintenance business comprises airframe maintenance at Auckland and Christchurch, and engine maintenance at Manukau, south of Auckland. Heavy maintenance of engines for narrow body jets and turboprop aircraft is out-sourced.

ANZES's wide-body heavy maintenance business is relatively inefficient as it services only Air New Zealand and no other airlines. In 2002-03, ANZES had provided heavy maintenance for Qantas, but the contract was only temporary. Future prospects were poor as newer generations of wide-body aircraft coming into service required substantially less maintenance.

In October 2005, Air New Zealand announced that it would out-source all heavy maintenance of wide-body airframes and engines to providers in Europe and Asia. Management calculated that out-sourcing would save NZ\$100 million over five years. ANZES would lay off 617 personnel at the Auckland, Christchurch, and Manukau bases.

ANZES engineers are represented by the Aviation and Marine Engineers Association, and its technical workers by the Engineering, Printing and Manufacturing Union. Following Air New Zealand's announcement, the Association and Union commissioned consultants Ferrier Hodgson to propose alternatives that would save jobs.

In early December 2005, Ferrier Hodgson and the unions presented Air New Zealand with proposals to reduce ANZES's costs by NZ\$ 90 million over five years. Employees agreed to substantial changes in work practices, including more flexible shifts, requiring workers to take time off in lieu instead of being paid overtime, and new categories of staff. Under the proposals, lay-offs would be reduced to 300.

Air New Zealand Group General Manager of Ventures Craig Sinclair welcomed the proposal but cautioned, "does that change give us the

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competitiveness we need to be able to go up against the big guys in Asia and Europe and win customers that we don't have now?"¹

On December 19, 2005, Air New Zealand announced that it would go ahead to out-source heavy maintenance of wide-body engines. It dismissed 110 personnel at Manukau. However, in response to the unions' proposal, Air New Zealand postponed any decision on wide-body airframe maintenance until February 2006.

Air New Zealand Chief Executive Rob Fyfe remarked that some jobs at Auckland and Christchurch could be saved if unions would reduce costs even further, "If the unions and their members are able to commit to extensive across-the-board labour reform ..., there may be an opportunity to retain some wide-body airframe maintenance in-house".²

Aviation and Marine Engineers Association national secretary George Ryde described the out-sourcing of maintenance as "lunatic".³ However, he conceded that workers had not been hopeful about retaining the engine maintenance work.

Mr Rob Fyfe rejected suggestions that outsourcing would compromise safety, "For many years Air New Zealand has out-sourced various component, engine and airframe maintenance work to organisations in Europe and Asia without safety issues being raised. Recent questioning over the outsourcing proposal is nothing more than scaremongering."⁴

¹ "Union out to save 300 Air New Zealand jobs", *New Zealand Herald*, December 9, 2005.

² "Air New Zealand cuts 110 engine jobs", *The Press, Christchurch*, December 20, 2005, A3.

³ "Air New Zealand cuts 110 engine jobs", *ibid.*

⁴ "Air New Zealand axes 110 engineering jobs", *tvnz.co.nz*, December 19, 2005.

Questions

1. Suppose that the unions are uncertain whether Air New Zealand is serious about out-sourcing wide-body *airframe* maintenance. Use a game in extensive form beginning from an uncertain initial node with two branches – “Air New Zealand is serious” and “Air New Zealand is not serious”. At the end of each branch, the unions have two choices – “offer concessions in wages and work practices” and “do not offer”. The unions must make a choice without knowing whether Air New Zealand is or is not serious. So, the unions must make the *same choice* at the two branches.
 - a. How does the probability that Air New Zealand is serious affect the unions’ choice of whether to offer concessions?
 - b. How would Air New Zealand’s decision to out-source wide-body *engine* work affect the unions’ belief that Air New Zealand is serious about out-sourcing wide-body *airframe* work?
2. New Zealand suffers from the geographical disadvantage of being at the end of most air-routes, where air traffic is relatively low. Air New Zealand’s fleet is smaller than those of Asian carriers Cathay Pacific and Singapore Airlines and European carriers British Airways and Deutsche Lufthansa. Use the concept of scale economies to explain why ANZES’s wide-body aircraft maintenance operations are relatively inefficient.
3. Chief Executive Rob Fyfe spoke of retaining “some wide-body maintenance in-house”, while Mr Craig Sinclair referred to competing for third-party maintenance service. Compare the price that Air New Zealand would pay for in-house maintenance with the price that other airlines would pay ANZES for such service.