



## What price loyalty?

*IdeaWorks contributed information to this article - - see italics.*

Frequent-flyer programmes range from simple air miles reward schemes to elaborate partnerships. Do they have a place in the business model of the low-cost carrier?

Loyalty programmes have long been a distinguishing feature of a full-service carrier, along with business lounges, complimentary in-flight food and entertainment and, often, membership of a global alliance. But where legacy carriers have been busily subtracting or charging for such luxuries, their low-cost rivals are adding the offerings they see as most valuable to their customers.

One such offering is a frequent-flyer programme (FFP), which low-cost carriers are creating as they see the additional costs involved justified by capturing more traffic and adding revenue, as well as a means of gathering information on regular travellers, according to Tony Clarke, director of specialist loyalty marketing agency ICLP. The business traveller seems to be the catalyst. "When an airline moves into the business travel market a loyalty programme becomes essential," says Ravindra Bhagwanani of FFP consultancy Global Flight Management.

The first such programme was set up as long ago as 1987, when Southwest Airlines established its award scheme. This was not because it necessarily wanted to, but rather that it felt legacy carriers' programmes were siphoning business travel away.

It opted for a scheme that would reward and retain loyal customers. "Our Rapid Rewards programme is very simple, just like us. We offer free tickets based on the number of trips taken, not miles flown. If we have an open seat and you have a ticket, we welcome you on board. There is nothing complex about it," says Southwest. Now all US low-fare players have loyalty programmes, from JetBlue's trueBlue to Frontier's EarlyReturns.

*There is, however, an increasing problem over availability – the opportunity to redeem air miles once they have been accrued, says Jay Sorensen at US loyalty services consultancy IdeaWorks. He explains that, for example, as US carriers have seen load factors rise to record levels, this has squeezed out the traveller trying to redeem points. The net result is that the level of reward travel overall has*

***dropped, according to Sorensen, who warns of a “perfect storm brewing”, where the value of a carrier’s FFP is of a higher value than the airline itself.***

Clarke agrees: “Air miles have a cash value. As passengers fail to reach redemption levels, all miles in circulation show up on a carrier’s balance sheets as a liability.”

“The biggest gripe we found from frequent flyers was having a huge number of points but not being able to use them. This also then becomes the airlines’ problem in having to deal with the liability so no-one was happy,” says Virgin Blue chief executive Brett Godfrey.

Bhagwanani insists: “An FFP must be looked at as a financial liability.” In the case of Virgin Blue, members’ points are backed by a Trust structure, in which the Velocity scheme is operated by Velocity Rewards as trustee of the Loyalty Trust.

In Europe German low-cost carriers are leading the way. Air Berlin was the first, relaunching its scheme as “Top Bonus” in July 2004. It operates its own programme, simplifying processes as much as possible. The carrier has 23 partners through which travellers can earn air miles, as well as a Mastercard credit card, on which travellers earn an air mile for every euro spent.

### **Extra benefits**

Air Berlin chooses to offer additional benefits to its frequent flyers with extra baggage allowances and on-board shopping discounts. In addition, silver and gold cardholders can select their seats in advance. According to Thorsten Scherzer, manager distribution systems and loyalty programme at Air Berlin, the carrier uses the scheme to steer traffic towards less popular or recently opened routes, such as its new domestic routes within the UK.

Wherever a seat is available, frequent-flyer miles can be redeemed. “It is important to have an honest programme,” he says. The traveller can get a “free ticket, when they want and to where they want in a way that reduces complexity”. He says the Air Berlin programme is not designed to be a revenue generator, but is important for the carrier’s relationship with its high-yield customers who have shown that they value priority check-in and seat allocation that come with membership of the scheme.

***With its strong business traveller base, easyJet is the carrier that first comes to mind when considering which of Europe’s other low-cost leaders is ripe for an FFP. According to Sorensen: “When easyJet starts a programme that will be a real step change in Europe.” Car hire, hotels and cruises are already offered on its website, and it has “all the elements of a delicious loyalty programme”, he says.***

EasyJet, however, is keeping its powder dry for now. The carrier says it has considered setting up an FFP but insists: “We have a principle of making things as efficient and simple as possible. Any such scheme would bring with it additional administration such

as a special projects team.” It adds that there has not been a particularly high level of interest from business travellers and says there are other innovations it would prefer to offer before a loyalty programme.

***Ryanair, Europe’s largest low-cost carrier, has also shunned the loyalty programme concept, although it does operate a credit card programme that, says Sorensen, is very rewarding to the consumer. He adds: “Ryanair’s paranoia about costs has served it well, but it could still benefit from a frequent-flyer programme as a revenue centre.”***

Bhagwanani says carriers are making a mistake if they look at FFPs purely from a cost perspective but rather what they can bring in terms of revenue, adding that they can have the indirect effect of increasing yields. He insists any such scheme should be looked at from a long-term perspective.

He sees an increasing trend towards outsourcing such schemes, both in terms of software and call centre support on an ongoing basis. For example, Virgin Blue’s operating partner in its new Velocity programme is Carlson Marketing Group. According to Godfrey: “At a system level essentially we operate the front-end website and redemptions, and they run the backend programme that manages the points and interfaces with partners. They are also our marketing partner, helping manage customer segmentation and communications.”

## **Business focus**

Germanwings is the latest European low-cost carrier to set up an FFP, which brand director Andreas Engel claims is the first such internet-based scheme. He says the carrier’s FFP is in response to the increasing number of business travellers at its Cologne hub, especially on services to cities in central Europe such as Budapest, Prague and Zagreb.

The mushrooming Asian low-cost market would lend itself to a loyalty scheme, believes Sorensen. Travellers there expect a higher standard of onboard service such as seat allocation, something which goes well with a loyalty programme, he adds.

However, Kathleen Tan, executive vice-president commercial at AirAsia, insists the Malaysian no-frills carrier has no plans to join the FFP community. “We don’t want to go that route,” she says. “At the moment we want to stay really focused on our model. The key is to keep the model simple,” she adds, and getting into an FFP means adding headcount and complexity, which is something it will not do.

Australia’s Virgin Blue set up its Velocity programme in November last year and has a clear vision of what it expects from it. “There are three broad streams of benefits for Virgin Blue,” says Godfrey. “Firstly, unlike traditional low-cost airlines, we have always competed head to head with a legacy carrier – not just on the same city pairs but to the same airports and even to the same terminal. High-yielding business travellers will

happily forego boxed meals and surly service, but they hold frequent-flyer points and lounge membership dear and we need both to be in the game. We expect the increase in yield and load factor to more than offset the costs of operating the programme and supplying the reward seats," he explains.

***Sorensen sums up the FFP like this: "It is first and foremost designed to keep people loyal to your brand, allow you to talk to your customers and is a vehicle by which you can increase travel activity."*** Put like that, it looks like something more and more low-cost carriers could be signing up for in future.

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