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No-bag-fees strategy could help Southwest in the long run

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IdeaWorks contributed information to this article - - see italics.

While airlines continue to rack up even more revenue by charging higher checked-baggage fees, Southwest remains resolved to let bags fly free, saying it has enabled the carrier to capture market share from its competitors.

And a recent report analyzing the baggage-fee bonanza suggests that while Southwest might be forgoing hundreds of millions of dollars in immediate cash, the low-cost carrier's strategy promises to pay off in the long run as fed-up passengers make the switch to avoid paying the extra baggage charges.

"Southwest hopes its consumer-friendly policy will deliver big market share gains," the consultancy IdeaWorks said in a report released Jan. 20. "Meanwhile, the rest of the airline industry hopes it is far from the tipping point where fee hikes bring diminishing returns and no longer deliver gushers of money."

The report said it appeared that airlines are likely correct about that, at least in the very near term.

"Successive fee hikes yielding ever-increasing revenue is the clearest proof of success," the report said.

Airlines are willing to put up with the anecdotal backlash because the baggage fees for them, so far, have made good financial sense.

IdeaWorks estimated that Delta, American, Continental, United and US Airways would together realize annual baggage fee revenue of about \$1.76 billion.

Southwest would stand to pocket \$732 million annually if it initiated a baggage fee, IdeaWorks estimated.

But, IdeaWorks warned, "Corporate hubris may push the industry to some sort of tipping point. Southwest's management (and its investors) should expect and require healthy market share gains from its bold product positioning endeavor."

Southwest said that's already happening.

"It is very clear we are seeing a share shift," CEO Gary Kelly told analysts during this month's earnings call. "Somewhere between half a million and \$1 million worth of additional customers. I hope [other airlines] charge \$100 per bag. That would be terrific. We would have 100% load factors. It would be great."

Kelly added, "We reduced capacity 8% in the fourth quarter, and at the same time we grew our passengers."