

May 31, 2010

## Airline Reward Programs Pay Off Less Frequently

Business Day Section

By Joe Sharkey

*This article is based upon a report issued by IdeaWorks.*

FOR participants in frequent-flier programs, more miles are chasing fewer seats, and the problem is likely to get worse.

In April, the five so-called legacy carriers (Delta, United, American, Continental and US Airways) averaged domestic load factors of 85 percent, which measures how many seats on airplanes are occupied by paying customers.

Southwest Airlines reported a load factor of 78.8 percent in April. That brought the overall average down a bit for the top six carriers. But no matter how you do the math and as every frequent flier knows, an empty seat is as rare a sight as a free meal on most domestic flights.

Randy Peterson, the frequent-flier mileage program expert, says members of airline loyalty programs worldwide are sitting on a monster-size cache of at least nine trillion frequent-flier miles.

Meanwhile, both business and leisure travel demand is rebounding, and airfares are rising. For anyone looking to cash in miles for a free ticket, how do these numbers add up?

Not so well, according to a recent survey by the IdeaWorks and ezRez Software. Researchers made 6,160 inquiries seeking rewards on the Web sites of 22 frequent-flier programs during February and March. The inquiries sought a variety of long-haul and short-haul trips.

The survey received considerable media attention since it was released last month, nearly all of it focused on which airlines delivered best on reward travel. In general, requests for short-haul travel scored best, which is one of several reasons that Southwest Airlines came out on top, delivering on 99.3 percent of inquiries.

The domestic legacy carriers, which have far more complicated frequent-flier programs, fared far worse. Of those five, Continental was best, at 71.4 percent. United came next, at 68.6 percent, then American (57.9 percent), Delta (12.9 percent) and US Airways (10.7 percent).

Fewer mileage-award tickets are available. Continental, for example, awarded 1.3 million mileage tickets in 2009, representing 6 percent of its total miles flown, down from 1.6 million in 2008 and 8.5 percent of miles flown.

The rankings got wide attention, as I said. The implications did not.

Deals that airlines make with credit card companies are the bedrock of most big frequent-flier programs. Banks that issue airline-branded credit cards have paid billions to those airlines in exchange for huge amounts of frequent-flier miles. The credit cards are then marketed to customers accumulating mileage with every purchase they make. Where airline frequent-flier programs once were built on miles actually flown, most are now overwhelmingly built on miles generated by consumer purchases of all sorts.

Revenue generated by selling miles to credit card companies became “piggy banks” as airline scrambled desperately for revenue, said Jay Sorensen, the president of IdeaWorks. “The airlines have been treating this like crack cocaine to satisfy their needs. But they’re not taking the money and investing that back into the programs to help fix the reward issue,” he said.

He says the system worked well before this because airlines could manage the line between free and paid tickets. “That was when you could make more seats available to your frequent-flier program because you believed those seats wouldn’t be sold for revenue. So frequent-flier members got the leftovers,” Mr. Sorensen said.

Now, there are more miles chasing fewer rewards seats. “The days of 65 percent load factors, which even then generated profits, are gone. We are now in a higher load-factor, lower-fare environment,” he said.

Besides dissatisfaction about the general decline in availability, frequent-flier members are increasingly unhappy about the higher number of miles required to grab any reward seat, and the growing trend of airlines slapping fees on those supposedly free tickets.

So what’s ahead? I’m looking at a system that’s plagued with diminishing rewards, growing desperation of credit card companies to get people to sign up, and staggering amounts of money bet on the assumption that travelers will continue to have faith in these frequent-flier programs.

With all that, I wonder if this is another great big economic bubble that’s bound to burst?

“Most definitely,” Mr. Sorensen said.