

AIRLINE PASSENGER EXPERIENCE

OFFICIAL PUBLICATION OF THE AIRLINE PASSENGER EXPERIENCE ASSOCIATION

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GOING THE EXTRA MILE

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Airline loyalty schemes are making significant revenue gains through credit card partnerships. But will selling perks to non-flyers leave elite road warriors feeling peeved?

WORDS BY LORI RANSON IN WASHINGTON DC

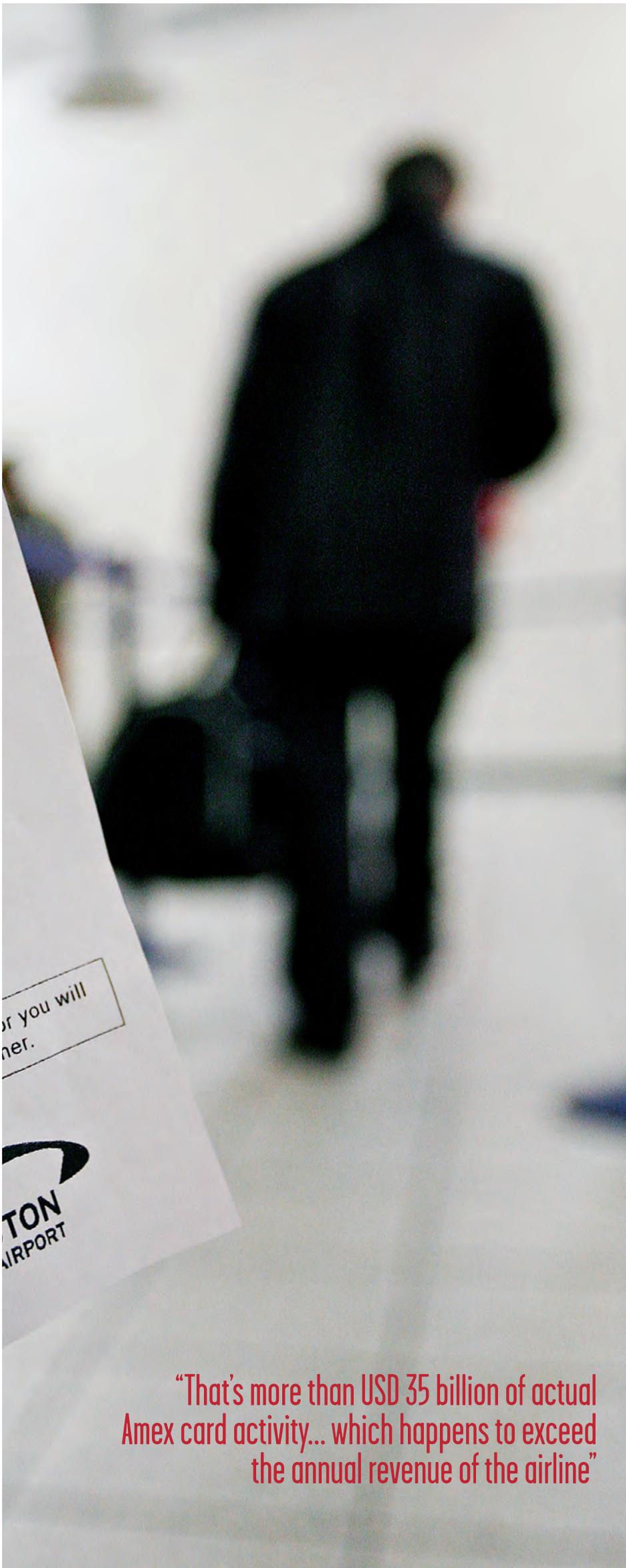
AIRLINE FREQUENT flyer programmes have been transformed from simple schemes developed to identify loyal customers into complex entities producing significant revenues. But as more customers build up miles, airlines face the delicate balance of ensuring that they don't spill revenue as passengers line up to receive their just rewards.

What's more, some frequent flyers believe their elite status is being diluted by the onslaught of those who pay for perks instead of earning them – a situation resulting from the product unbundling and new wave of merchandising by carriers.

All these changes are occurring against a backdrop of airlines trying to determine the best communication outlets for engaging with their frequent flyers; their attempts to lure customers into airline-created online forums have been largely unsuccessful.

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“That’s more than USD 35 billion of actual Amex card activity... which happens to exceed the annual revenue of the airline”

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BANKING ON LOYALTY

Consultancy IdeaWorks estimates that United Airlines recorded USD three billion in revenue from its frequent-flyer programme during 2010, while Delta Air Lines enjoyed USD 1.6 billion in revenue derived from its SkyMiles loyalty programme.

Airlines have achieved much of the staggering revenue they garner from frequent-flyer activity by forging deep and complex relationships with banks. Together, they offer powerful co-branded credit cards, which allow consumers to rack up miles for redemption of a wide variety of products. Banks have stepped in to help airlines bolster their coffers through loans of pre-purchased miles.

“Banks have a lot of influence in what happens with frequent flyer programmes,” says IdeaWorks president for product, partnership and marketing practice Jay Sorensen. As such, frequent flyer programmes “have become a significant component of the consumer banking industry”, he concludes in IdeaWorks’ analysis of frequent flyer programmes, *Loyalty by the Billions*.

American Express’s 2010 annual report reveals just how significant is its business with airlines. For instance, the company revealed that its co-branded Delta SkyMiles credit card accounted for about five per cent of its billed business of USD 713.3 billion worldwide. “That’s more than USD 35 billion of actual Amex card activity... which happens to exceed the annual revenue of the airline,” said American Express.

IdeaWorks, meanwhile, notes that the vast majority of the 114 billion miles sold by American Airlines in 2010 were purchased by Citibank, which is the primary issuer of credit cards in the carrier’s AAdvantage programme, and the bank likely paid more than USD one billion for the miles accrued by cardholders.

Mingled with the credit-card activity is a significant amount of airline miles and points bought by hotel chains, car rental companies and retailers, says IdeaWorks. “These partners may lack the buying power of banks, but their participation adds benefits for consumers.”

Frequent-flyer expert and editor of InsideFlyer Randy Petersen estimates that 60 to 70 per cent of miles earned by customers stem from non-transportation sources, and the reality is that airline loyalty programmes have in essence become travel loyalty programmes. But IdeaWorks concludes that if airlines have a broad range of partners in their loyalty programmes, “accruing miles through travelling and shopping makes a programme more valuable to the member”.

A new tier of elite-style credit cards has evolved that could further enhances airline revenues. American and Citi Cards in 2011 debuted the “Executive AAdvantage World Elite MasterCard” that fetches a USD 450 annual fee in exchange for annual perks that include Admirals Club membership for immediate family and up to two travelling guests, priority check-in, security screening and boarding regardless of the ticket price paid. Cardholders also enjoy waived baggage fees for domestic checked bags and up to eight companions travelling under the same itinerary and 10,000 AAdvantage elite qualifying miles after the first purchase of USD 40,000 within a calendar year.

“Programme members enjoy more choices and can opt to pay an annual fee for services they value,” says IdeaWorks. “Airlines can use co-branded credit cards as a new platform to sell annual subscriptions for à-la-carte services.”

DILUTION AND REVENUE SPILL

Even as they reap the revenue benefits by partnering with credit card companies to co-brand their loyalty programmes, airlines are aggressively unbundling their products to upsell the perks enjoyed by elite flyers to any customer willing to pay for priority boarding, lounge access or expedited security.



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IdeaWorks' Sorensen remarks that, while there has been some grousing over that issue on comment boards in the frequent-flyer community, he doesn't believe there is a danger of revenue cannibalisation. United has roughly 1.6 million elite frequent-flyer members, says Petersen, and the passengers that frequently purchase the upsells are infrequent travellers. He notes that the number of upgrades sold wouldn't rival the number of elite passengers enjoying the free perks associated with their status.

The proliferation of à-la-carte sales has even made some elite passengers realise the value of the perks they enjoy free of charge, Sorensen explains. However, he says there is a risk of the

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JAY SORENSEN, IDEAWORKS

airline overselling priority security access and boarding, which could degrade the experience of the elite passenger.

One emerging risk for airlines as the number of frequent flyers grows is losing revenue from ticketed passengers in order to accommodate passengers using redemptions, says Hamlin Transportation president George Hamlin.

In the US, where average load factors are at 80 per cent, airlines have had to cut off more revenue-paying passengers as reward passengers line up to redeem free trips. Hamlin concludes there was more capacity in the system at the inception of frequent-flyer programmes when load factors averaged 60 per cent. He believes the higher number of travellers redeeming miles could actually hurt airline yields. Although airlines receive money up-front from banks through their co-branded credit card deals, he questions if airlines “would be better off not having done this”.

LOW FARE, HIGH REDEMPTION

Low-fare carriers are more likely to face an ever-growing number of passengers lining up for reward seats as they offer a higher level of seat redemption. IdeaWorks' third annual Switchfly Reward Seat Availability Survey shows that Southwest Airlines and Air Berlin were the most generous in allowing loyalty programme members to redeem seats, with every flight queried under the survey showing reward seat availability.

IdeaWorks based the survey on 6,680 booking queries made on the websites of 23 frequent-flyer programmes during March 2012 for travel from June through October. A minimum of two reward seats was required for each outbound and inbound reward reservation query.

Joining Southwest and Air Berlin in the carriers scoring highest for seat redemption were Brazil's Gol at 97.1 per cent, Lufthansa/Swiss/Austrian at 92.1 per cent and Singapore Airlines at 90.7 per cent. US Airways, Emirates and Delta rounded out the bottom of the list with seat reward availability at 33.6 per cent, 32.9 per cent and 27.1 per cent respectively.

AirTran Airways recorded a 40-point improvement year-over-year, bringing its redemption percentage to 87.1 per cent, which put the carrier in a tie with United Airlines for the seventh place spot. The survey concluded that AirTran's big jump “likely indicates that Southwest is applying its generous reward-allocation philosophy to the airline it acquired during 2011”.

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IMAGE © ALAMY

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In addition to moving up the rankings in seat reward availability, United also improved its allocation of reward travel in a shorter five to 15 day booking window.

Another element of the survey entailed 80 queries conducted on 13 April for departures from 17 April to 27 April on US carriers American, Delta, United and US Airways. United improved its position by 22.5 points year-over-year after showing 87.5 per cent availability of reward travel in a shorter window. Delta was at the bottom of the list with a 25 per cent redemption rate, a 17-point drop from the year before.

The seat redemption benefits that low-fare carriers offer is obviously popular with customers, but it does come at a price. The survey concludes that airlines that allocate meaningful inventory to seat redemption “do incur an opportunity cost for the seats not sold for cash”.

TRADING MILES FOR POINTS

One of the biggest stories within the frequent flyer community during the last 18 months was the introduction by Southwest of its Rapid Rewards 2.0, a loyalty programme that adopts the ever-growing trend of points accumulation rather than allowing customers to collect credits for award travel redemption.

The basics of the new Southwest programme allot a greater number of points for redemption to higher fare classes versus the old scheme of earning one credit per flight regardless of the price or distance. Under Rapid Rewards 1.0, passengers earning 16 credits were eligible for a free ticket. Customer reaction to the new programme was mixed, as some frequent leisure customers felt disadvantaged by the changes. But Southwest during the last few years has made a push to increase its business traveller mix, and IdeaWorks’ Sorensen says that ultimately, “airlines care more about high price fares. They want more of those people.”

SOCIAL CURRENCY

Although social media stewardship is a standard business practice for nearly all airlines, online forums seem to remain the most effective means for carriers to engage with their frequent flyers.

InsideFlyer’s Petersen remarks that Facebook and Twitter are largely reactionary outlets, allowing airlines to handle customer service issues or in some cases advertise various promotions to customers. American has separate Twitter and Facebook accounts for its AAdvantage loyalty programme, but as InsideFlyer declared, those accounts “are not meant as a channel for AAdvantage customer relations issues”.

It appears the most successful way airlines have managed to gauge their frequent travellers’ mood is by following or even participating in online forums such as FlyerTalk, Milepoint (both created by Petersen) and FrequentFlyer.com. Some airlines have employees who actively participate in those forums. Lufthansa, Delta and United are particularly active, while Continental, which merged with United in 2010, had been active in FlyerTalk for many years.

Airline experiments in launching these types of forums for themselves have largely failed. It’s true that JetBlue Airways has achieved some success with its TrueBlue community, but Air France, British Airways and Virgin Atlantic have abandoned their own attempts at social networking through branded websites.

Essentially, carriers that have built their own social branded networks to target frequent flyers and the broader passenger population at large have doubled back to traditional social media channels and the larger online frequent-flyer forums. Petersen points out that it costs airlines nothing to access the millions of posts from their respective loyalty members on larger forums. Delta appears to have struck the right balance between executing



“Airlines can use co-branded credit cards as a new platform to sell annual subscriptions for à-la-carte services”

IMAGE © ALAMY

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a strategy for traditional social media channels and engaging with frequent flyers in online forums. InsideFlyer notes the carrier dispatches its social media ambassadors on FlyerTalk to engage customers based on the topic of conversation such as e-commerce or mobile apps.

As trends in airline loyalty programmes continue to evolve, their relevance remains strong, says Soresen. The credit card partnerships forged between airlines and banks are irreversible. As IdeaWorks explains, airlines have used the money provided by banks through the sale of miles to boost battered balance sheets.

“Frequent flyer programmes have become products unto themselves,” concludes IdeaWorks. “The allure of elite status encourages members to concentrate their purchasing power with their programme of choice. This is accomplished by remaining loyal to an airline and its partners even when competitors offer a better combination of schedule convenience, service quality and price.”

SWITCHFLY REWARD SEAT AVAILABILITIES

BASED ON 6,680 REQUESTS MADE TO 23 FREQUENT FLYER WEBSITES IN MARCH, 2012 FOR TWO SEATS

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Overall Reward Availability				
Ranked High to Low, Seat Availability for June–October, 2012				
Rank	% Total Availability	Airline	Programme Name	Change from 2011 to 2012
1 (tie)	100.0%	Air Berlin	Topbonus	▲ 3.6 points
	100.0%	Southwest	Rapid Rewards	▲ 0.7 points
3	97.1%	GOL	SMILES	▼ 2.9 points
4	92.1%	Lufthansa/SWISS/Austrian	Miles & More	▲ 7.1 points
5	90.7%	Singapore Airlines	KrisFlyer	No change
6	90.0%	Virgin Australia	Velocity Rewards	▼ 1.4 points
7 (tie)	87.1%	AirTran Airways	A+ Rewards	▲ 40 points
	87.1%	United Airlines	MileagePlus	▲ 15.7 points
9	86.4%	JetBlue	TrueBlue	▲ 7.1 points
10	79.3%	British Airways	Executive Club	▲ 17.9 points
11 (tie)	78.6%	Air Canada	Aeroplan	▼ 3.5 points
	78.6%	LAN	LANPASS	▲ 2.9 points
	78.6%	Qantas	Frequent Flyer	▲ 3.6 points
14	70.7%	Cathay Pacific	Asia Miles	▲ 4.3 points
15	63.6%	Iberia	Iberia Plus	▼ 7.1 points
16	59.3%	Alaska Airlines	Mileage Plan	▼ 5 points
17	57.9%	SAS Scandinavian	EuroBonus	▲ 5 points
18	55.7%	Air France/KLM	Flying Blue	▼ 9.3 points
19	45.7%	American Airlines	AAdvantage	▼ 17.2 points
20	38.6%	Turkish Airlines	Miles&Smiles	▼ 10.7 points
21	33.6%	US Airways	Dividend Miles	▲ 7.9 points
22	32.9%	Emirates	Skywards	▼ 2.8 points
23	27.1%	Delta Airlines	SkyMiles	No change

Percentage of Total Availability = Percent of queries that result in outbound and return rewards seats.
Value-oriented airlines: Air Berlin, Southwest, GOL, Virgin Australia, AirTran Airways and JetBlue

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IMAGE © GETTY