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By Helen Massy-Beresford

European Carriers Search For Profits At The Margins

This article is based upon a report issued by IdeaWorksCompany.

PARIS—European airlines, struggling with tight margins as ticket prices fall, and fears of terrorist attacks take their toll on leisure travel demand, are getting creative when it comes to the all-important ancillary revenues—and for many, a digital push is helping give them an edge.

A recent report by consultancy IdeaWorksCompany emphasized the importance of mobile applications for airlines looking to make the most of ancillary revenues, citing United Nations statistics that estimate the world's population at about 7.4 billion—and that there are also nearly 7.4 billion mobile subscriptions worldwide.

Bobby Healy, chief technology officer of travel technology platform CarTrawler, which commissioned the IdeaWorksCompany report, says the digital drive offers opportunities for airlines—but also comes with costs. “Without exception, the airlines need to have mobile web, Android and Apple iOS as well as desktop channels—that is nearly tripling the effort of building user interfaces,” he says.

As targeting ancillary revenues through mobile devices grows in importance, many airlines are choosing to keep control over that development instead of outsourcing.

“We have been seeing in the past 2–3 years more airlines treating it as a core skill for strategic reasons,” Healy says. “Most of the airlines that want to protect the flexibility of their business model [take] in house the user interface part of it, and that pattern will continue.”

Kenny Jacobs, Ryanair chief marketing officer, says the airline decided to develop its own app in house, through its Ryanair IT/Labs digital hub, which it set up in 2014, for three reasons: “To keep the costs down; to move at speed; and because we think we have a fairly good list of ideas—we are trying to build something new,” Jacobs said.

The commitment appears to be paying off, with the carrier's app cited as the most advanced of those reviewed for the airline, whose ancillary revenues accounted for 24% of overall revenues in 2016. Ryanair wants that proportion to grow to “30% or better in the next few years,” Jacobs said.

One current area of focus is tailoring offers and communications to specific customer segments, he said, for example, tailoring offers to “silver surfers,” families with young children or families with teenagers. “We have been doing that on our website for the past 6 months with good returns, and we’re going to start doing it on the app,” he said.

Air France, another airline whose app was singled out for praise by the report, also develops its own app, available on iOS and Android. “The Air France app and mobile services for our customers are constantly improved, resulting in growing numbers of customers buying tickets and ancillary services through their mobile [divces],” said Vincent Fillon, Air France’s digital general manager for mobile applications.

Across its airlines—Air France, KLM, HOP! and Transavia—the Air France-KLM group offers a range of options, including seat choices in economy; upgrades; additional baggage allowance; lounge access; onboard sales of duty-free goods; drinks and meals; baggage delivery; travel insurance; city transfers; and “buy now, pay later” options for fare-freezing.

“By far the, most important in terms of numbers and revenue are seating products, paid upgrades and additional hold-baggage allowance[s], which will continue to represent the vast majority of these revenues for the years to come,” said Frederic Gonnaud, the group’s vice president for retail and ancillaries.

Finnair has also said it wants to boost its revenues by €500 million (\$526 million) by the end of 2019, helped by ancillary sales including new revenue streams, such as advance seat reservations and excess baggage fees. All of the airline’s Airbus fleet is set to have Wi-Fi installed by 2018, giving customers access to more priced features and better onboard shopping capabilities.

For the Air France-KLM group, revenues from paid options and services bought by passengers alongside their air tickets rose 12% in 2016 to €515 million, while overall passenger revenue was down 4.2%. The group does not communicate overall ancillary revenues, of which these paid options are just a part.

The group is investing in being able to sell paid options to customers through various channels. “In this respect, yearly, multimillions of euros are currently invested into ‘behind the scenes’ core systems—catalog, quotas and inventory management, fare-filing, media and content management—and also in ‘front end’ systems like the apps,” said Frederic Gonnaud, the group’s vice president for retail and ancillaries. He noted that apps are only a small part of the overall investment.

“Ancillary revenues are expected to continue to grow in the future thanks to our continuous efforts in pricing management, distribution and also the implementation of new options,” Gonnaud added.

Jimmy von Korff, CEO and cofounder of wireless inflight entertainment platform Immfly, believes his company's technology can also help airlines maximize ancillary revenues.

"The airline ticket is just a small portion of a passenger's budget, and I think airlines want more and more to be a travel brand, rather than just a transportation brand," von Korff said. "They are targeting more parts of that budget and selling more relevant things, such as hire cars or checked-in bags. Amid a price war, with low, low margins, these things are the key to generating positive returns for airline investors."

Immfly's system, which is in operation on Iberia Express, Volotea and XL Airways aircraft, is straightforward to install onboard—for Boeing 737-800 and Airbus A320-family jets it can be done overnight, without disrupting operations. As well as generating more revenues in the short term, in the longer term it can help airlines get to know their customers better by gathering data and obtaining their feedback.

For Iberia Express, Immfly provides media including Spanish and international newspapers, movies and TV shows, as well as interactive travel guides and offers on transit tickets, museums and excursions.

"Immfly's focus is on opening up a new digital touchpoint for the airline, through which they can offer new things onboard which are relevant for the passenger," Von Korff added. "Having a digital touchpoint onboard also opens up opportunities pre- and post-flight. If you know you are going to have special entertainment onboard through this platform, you can sell access to premium content. You can provide exclusive offers for the destination such as entry to a museum or an event connected with the airline."

Jay Sorensen, president for product, partnership and marketing practice at IdeaWorksCompany (and the report's author), believes that with a wide variety of options, offers and goods already available to buy through airline apps, opportunities for future revenue growth will be focused on better pricing.

"Generally, I am impressed by how much is available in the apps compared with the online environment. Airlines are going to get better at managing the pricing—when demand is high, increasing the price and when demand is low, decreasing the price. Using price management to stimulate demand is going to be an area of growth," Sorensen said.