

Profit zones

ANCILLARY REVENUE | PART I

Definition: Revenue beyond the sale of tickets that is generated by direct sales to passengers, or indirectly as a part of the travel experience. *Definition from the 2009 Ancillary Revenue and à la Carte Guide by IdeaWorks, sponsored by ezRez*

text Richard Williams

Just a decade ago, nobody had heard of Ancillary Revenue (AR). But in 2008 airlines generated €7.68 billion from this business line. This was against a yield in 2006 of €1.72 billion (an increase of 346%), and against a background of spiralling fuel costs, global financial crisis and health scares. In fact, it's likely that several airlines owed their continued existence to it.

It's hardly surprising that a host of companies have grown up around this sector, all seeking to

help airlines maximise their profits from it. After all, what used to be incremental revenue is now regarded as part of the core business.

The challenge that airlines face now is how to grow their AR by maximising current initiatives and exploring new ones, without alienating customers or losing new ones to the competition. Options that provide real value to the customer, delivered in ways that make the most of new technology and reduce cost, are likely winners.

As Travel Buddy, the mobile content and systems operator, puts it: "The companies that



Merchandising opportunities



succeed in the travel industry will be those who figure out how to serve their customers better whilst learning how to decrease actual personal interaction."

The 2009 Ancillary Revenue and à la Carte Guide by IdeaWorks, sponsored by software company ezRez, lists the top five airlines in terms of percentage of revenue derived from AR. Top is Allegiant with 22.7%, followed by Ryanair with 19.3%, easyJet with 15.5%, Jet2com, and Vueling. Companies such as Allegiant, United, Aer Lingus and American Airways doubled their euros per customer revenue over the previous year.

As defined in the Guide, broadly AR can be divided into three categories: à la carte features; commission-based products; and frequent-flyer activities. A la carte features include 1) onboard sales of food and beverages, 2) checking of baggage and excess baggage, 3) assigned seats or upgraded seats, 4) call centre support for reservations, 5) fees for payment made by credit card, 6) early boarding, 7) priority check-in, and 8) onboard amenities e.g. blankets.

The second category is made up of commissions. These are earned by airlines on the sale of hotel accommodation, car rental and travel insurance, and other travel items such as excursions and transfers. The commission-based category is mainly generated by the airline's website, but also by the sale of duty free and other products, and fees for onboard internet.

The frequent-flyer category mainly consists of the sale of miles or points to programme partners such as hotels and car rental companies, co-branded credit cards, online shops, retailers, and communication services.

The strong recent performance of United and

American in the AR market was partly driven by the move to checked baggage charging, which became the industry norm in the US in 2008. Seemingly overnight, checked baggage became the major contributor to AR. It is now spreading from the US domestic market to international routes. Delta forecasts €75 million annually from a new €37.50 second bag checking fee on international flights. Continental and US Airways announced in August 2009 that they were matching this fee on transatlantic flights.

Checked baggage fees will affect alliance partners. As Jay Sorensen, president of IdeaWorks and author of the Guide, says: "It won't be long before British Airways, Qantas, and Japan Airlines start charging fees for checked baggage. Why? Because it makes perfect economic sense and the precedent established by oneworld partner American Airlines will be too hard to ignore."

Other big revenue earners are charging for seat upgrades. Vueling Airlines goes even further by charging for four categories of seats, even the basic one. The Duo Seat sells for €30 and provides extra room by keeping an empty middle seat between two passengers in the first few rows. The XL Seat sells for €13 and uses exit rows with extra legroom. Seat Optimum at €5 gives you reserved seating ahead of exit rows, while €3 gets you Seat Basic for the remaining seats behind.

In a literal interpretation of à la carte services, some airlines, such as Hawaiian Airlines and Air Berlin, are asking customers to pay extra to upgrade to a better meal. In a related move, Air Baltic, Jetstar, and AirAsia X have replaced complimentary food with buy-on-board and pre-order services on long-haul flights.

Technology such as Air Meals' AM-1 software



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Jay Sorensen, IdeaWorks

enables passengers to book their meals online when they book their ticket. They can also order kids' activity kits, magazines and entertainment products. Adam Bauer, of Air Meals, claims that by using AM-1, carriers and caterers can expect a 10-15 per cent volume increase over buy-on-board programmes, as well as higher profit margins.

He explains the different retailing models for on-board purchasing: cart/cash; handsets; in-flight entertainment (IFE); and IFEC (when connected to the internet). "Currently, the handset approach is in vogue, with IFEC at very early stages (Virgin's RED was the pioneer). For handsets, types of products typically sold are food and beverage and growing are ex-flight such as Heathrow Express and Disneyland. It seems there is a movement underway with the handset model to optimise with data analysis. That is sales/take rates as well as on-board inventory management towards waste reduction.

"Regarding IFEC, with aircraft increasingly connected to the internet, what becomes possible is an expansion in types of services the passenger can purchase, and a web style shopping experience. Passengers view and purchase food and beverages from their seatback IFE, iPhone or laptop. Passengers similarly order ex-flight services (e.g. ground transportation, duty free, destination content) with real-time booking into a global network of third-party services providers."

In the commission category, travel insurance is profitable. EasyJet, for example, earned €32.4 million on travel insurance commissions during 2008. This revenue may be under threat, however, because travellers are wising up to the idea of taking out an annual multi-trip policy.

In the third category, frequent-flyer programmes work well for carriers with a co-branded credit card. United Airlines' Mileage Plus programme, with its Visa credit card, for example, contributed approximately €525 million to revenue in 2008. Smaller carriers can benefit from frequent-flyer programmes by partnering with a provider.

Loylogic, for example, has developed into a loyalty points 'earn and burn' solutions provider. Its earn solutions include EarnMall(tm), where members can earn points shopping online with merchants worldwide, and EarnShop(tm), which is a shop with special deals earning lots of points.

These solutions provide AR from the kickback on purchases with participating merchants.

Robert Moerland, sales and marketing director, explains how the programme also increases flight sales and miles sales revenue: "Rewards are the carrot of a loyalty programme. An attractive rewards offering and exciting redemptions options such as raffles and auctions, combined with the full flexibility to spend any amount of miles in combination with cash, will increase member engagement. It provides the incentive to choose a particular airline over a competing airline when buying flights, to use the programme's co-brand credit/debit card, and to choose to purchase from a programme partner - all with the purpose of accruing more miles. This increased activity leads to higher flights sales and also enhances the inherent value of these miles to sell to partners."

Frequent-flyer programmes are popular because they appear to deliver more for less. Charging for basic seats, meals, and baggage are moves in the opposite direction. Isn't this revolution in air travel likely to encounter some customer resistance? Allegiant offered this counter-argument in its 2007 Annual Report: "We believe by offering a simple base product at an attractive low fare we can drive demand and generate incremental revenue as customers pay additional amounts for conveniences they value."

OK, but by offering a range of other services don't airlines risk distracting passengers from the main purchase, which is the flight? Tina Fitch, ceo of ezRez, doesn't think so: "Consumers want more choice and more value, and whether an airline chooses to add ancillary travel or merchandising



Commission on non-airline ticket sales



A web-style shopping experience



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Adam Bauer, Air Meals



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Raphael Bejar, ceo, Airsavings

options to their website, the additional options should benefit most consumers. At ezRez, we have witnessed several airline clients add hotels, rental cars, trip activities and insurance to their core flight offering. The most successful airlines make these ancillary products relevant to their customers’ search habits and present them as a value-add, not a distraction.”

We asked Raphael Bejar, ceo of Airsavings, the AR solutions provider, to highlight some trends for us. He said that the benefit of fee-based ancillaries is waning and that commission-based AR will eventually surpass fee-based compulsory charges as the engine of non-seat revenue growth for airlines. These include the booking-path-based Big Three of hotel reservation, car rental and trip insurance, but look out for innovative ancillary services such as in-cabin mobile phone usage and online private event retailing (incorporated with loyalty programmes) plus commissions reaped from non-flight services.

Says Bejar: “Ryanair, for example, earned nearly €242 million in non-flight sales in 2007, a figure which does not include compulsory charges such as checked baggage fees. In-cabin wifi has been

a visible ancillary revenue initiative that many airlines have had success with, including Virgin America, Delta and Air Tran.”

One new company offers the Holy Grail, a service that benefits the customer while also acting as a catalyst for the airline to gather information about him. Satisfly is a passenger profiling solution that rates customers according to their General Profile, but also on their Flight Preferences and intended behaviour. Those who want to enjoy a drink and a chat and a meal or watch every movie available will not necessarily mix well with those who want to sleep. So their Intelligent Seating system auto-fills the seating, maximising compatibility of neighbours.

Sergio Mello, ceo of Satisfly, says: “In a short-term perspective, Intelligent Seating may be sold as an additional service. Compatibility with seat neighbours is perceived as a value added feature. Our surveys reveal that 40% of passengers would pay a premium for it. However, in the long run another factor proves beneficial to airlines. Now most of the ancillary propositions are commercialised without prior market segmentation. This leaves a great space for improvement in terms of sales conversion. Satisfly has the ultimate goal to provide airlines with the customer intelligence needed to implement deeper segmentation, all the way to one-to-one marketing execution.

“Besides delivering non-targeted advertising, airlines stick to traditional touchpoint-based communication models. So they only market at predefined moments in time or when the interaction is initiated by the customer. The future will see an increased ability to predict the right moment to offer the right product. Be it an

Listening to customers



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Robert Moerland, sales and marketing director, Loylogic



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Sergio Mello, ceo, Satisfly

insurance policy or a honeymoon package, real-time intelligence enables airlines to achieve the maximum return. This is the reason why Satisfly is designed to provide airlines with a stream of real-time and predictive intelligence.”

Another operation relies heavily on new mobile technology for its effectiveness. In a recent White Paper, Travel Buddy points out that airlines have two points of contact with passengers: when they book and when they travel. But if the airline takes a mobile number they have access to the customer while he is away on the trip. They also know where he is, and for how long. This is also the time when he is going to need information, products and entertainment - and he is in spending mode.

The customer can access a range of services by typing words such as ITINERARY, FLIGHT, WEATHER, SKI, EVENTS etc. into his mobile. As well as services such as airport parking, transfers, priority boarding, mobile check-in, he can get important travel information and emergency updates, all without the airline having to provide a one-to-one service. There is also the opportunity to offer mobile discount vouchers, e.g. for sun cream, sports clothes, equipment hire, restaurant vouchers and event tickets.

The essence of the offering is that it is Timely, Area specific, and Personal/Profiled. All the products and services that have migrated onto the Internet can now be accessed on the mobile phone, with the advantage that the customer will have it with him on holiday. This seems to tick all the boxes, using new technology to save costs, providing extra services, and generating almost limitless opportunities for Ancillary Revenue.

- www.ideaworkscompany.com
- www.ezrez.com/airlines
- www.loylogic.com
- www.travelbuddy.co.uk
- www.air-meals.com
- www.satisfly.com
- www.earnmiles.etihadguest.com
- www.airsavings.net



ANCILLARY REVENUE | PART II

A further feature on Ancillary Revenue will run in the June issue of *OnBoard Hospitality* covering the technology available to airlines to assist them and their crew with onboard sales and management. Email your editorial with details of any news ideas and products to jo.austin@onboardhospitality.com

Jo Austin talks to Christopher Parsons, a UK supplier to the airlines, about the simple ways he helps airlines to increase their profits

OBH How can lottery scratch-card sales make a difference?

A: “We provide airlines (mostly in Europe and Scandinavia) with generic or personalised scratch cards for sale onboard. The prize can be anything from a credit voucher towards an onboard duty free product to a Jaguar – as featured by one of our airline clients! We tailor the game to what an airline wants. It can promote income or just be a fun factor. We sit down with the airline and work out how they want to drive onboard sales.

Q: How much revenue can you expect to bring in for your airline clients?

A: One airline could sell a million cards a year for

£1 on which they should expect to make a profit in excess of 50% after paying for game and prize! One of our Scandinavian airline clients sold 1.2 cards to every passenger. Just work that one out!

Q. Tell me about your crew motivation courses

A: We have a good team of ex-airline employees who visit our airline clients and train their crew on onboard sales. If crew members are motivated they can sell anything! One of our clients said that our training had enabled their crew to double their onboard sales.

Q. Why should passengers crave your new smokeless product?

A: Since smoking has been banned on all aircraft and at most airports, smokers have suffered. Smokeless is a packet of 10 cigarettes which gives the smoker a nicotine rush and a cigarette flavour without having to light up. It is not a product for giving up smoking but a substitute which enables smokers to do so onboard. It is currently being sold on short haul flights and making good profits for those airlines and would obviously be ideally suited to smokers flying long haul. We have world rights on the product and it is already on sale with Ryanair, easyJet and bmi baby. We are also appointing distributors worldwide although I think it might be a problem with US carriers.
www.travelcards.eu.com