

By: Michael Fabey

Airline executives acknowledged they were offering deep discounts in the first few weeks of 2009 to make up for the drop in business and first-class travel brought on by the recession, but carrier bosses said those fare sales were fleeting.

The discounts are aimed at the leisure market, which had remained strong in the economic downturn, the executives said. However, the aggressive pricing had cut into yields, making the cheaper rates impossible to maintain for very long.

While executives are pleased by the strength of the leisure market, the discounting and yield cuts (coupled with the uncertain economy) have made it difficult to gauge how they might fare in the first quarter, let alone the rest of 2009.

"Leisure demand remained surprisingly resilient throughout 2008," US Airways President Scott Kirby told analysts during an earnings conference call in January. "Coming into 2009, leisure demand, at least as measured by volume or bookings data, remained similarly strong in 2009."

However, the airlines have released no data showing how strong the demand has been or how far yields have fallen. January is normally a very heavy month with few fare sales, Kirby said. But the sour economy has changed that. This year saw more aggressive pricing in January, which meant lower yields.

"The industry is pricing leisure travel more aggressively at the moment," Kirby said. "It's encouraging that booking volumes remain strong, so long as that could lead to a better pricing environment down the road."

Continental President Jeff Smisek told analysts, "We started seeing some weakness in leisure yields, as well. During peak periods, leisure yields are holding up relatively well, but we're seeing negative pressure on leisure yields and traffic in the nonpeak period. This is driving deeper industry fare discounts in particular markets as well as sale fares with travel bases extended through May, instead of March like we'd typically see at this time of year."

Discounting strategy questioned

Aviation experts said such discounts could be counterproductive in the long run, especially with the nine leading U.S. carriers reporting about \$14.4 billion in losses for 2008.

"Discounting, that's not the best way to generate demand," said Raphael Bejar, CEO of AirSavings.net, which specializes in fuel and ancillary purchases for airlines. "It's better to focus on providing service. People are looking to buy the right service for the right price."

Most airline executives agree, at least in theory.

People are either going to travel or not, Delta President Edward Bastian told analysts. The question, he said, is whether lower fares will stimulate more travel.

"What we're seeing is that the slightly lower fares don't seem to be driving the decision process, so I don't think you'll see fare structures that are significantly lower than last year's level."

Travel buyers themselves are helping the airlines. Even with the cheaper fares, travelers are waiting to buy their tickets at the last possible moment, even though that means they might get less of a discount.

Bastian told analysts, "We're seeing the demand curve move much closer to the day of departure, which actually means that the leisure traveler is paying slightly more than he did last year," because they're passing up advance-purchase discounts.



People appear to be falling into two camps, Bastian said: People who are unsure about their future or are unemployed and are not traveling, and people who feel comfortable in their future and feel secure and are traveling but are planning a little bit closer in. What the airlines are really looking for, executives told analysts, is a more stable and reliable revenue stream. The carriers continue to bank on extra fees and other related ancillary revenue to boost their bottom lines.

"We continue to be encouraged by our a la carte revenue initiatives and still expect to generate \$400 million to \$500 million in a la carte revenues in 2009," Kirby said. "A la carte revenues also benefit domestic, short-haul carriers like US Airways the most, since we have a higher number of domestic boardings relative to our size. We're the shortest-haul carrier with the exception of Southwest."

With the exception of Southwest, too, airline executives said, there's no stopping the unbundling and rebundling craze. In the end, they said, passengers would benefit because they might wind up with lower base fares and pay only for the services they want. "The basic cost should come down a lot," said Sam Jain, CEO of online travel booking site CheapOAir. "Some just want the lowest cost, and you might have a customer who wants a little luxury."

