

Finding New Things to Unbundle

By Michelle McDonald
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FINDING NEW THINGS TO UNBUNDLE

Ancillary revenues are a growth business if additional opportunities can be identified

By Michele McDonald

IN THE QUEST FOR NEW ANCILLARY REVENUE streams, “there’s not much more unexplored territory,” says Jay Sorensen, CEO of IdeaWorks, a consulting company that focuses on ancillary opportunities and estimates 2010 industry ancillary revenues at \$22.6 billion. “I think we’ve seen examples of everything that can happen.”

But those examples are concentrated in two types of airlines, he says: Network carriers in the US and low-cost carriers everywhere else. The concept has a lot of growth ahead of it, and many airlines that are already in the game have a long way to go in fine-tuning their strategies.

The low-hanging fruit—checked-bag fees—has been plucked by both camps, Sorensen says, and he predicts this will spread to full-service airlines around the globe via an unexpected source: The three major alliances. “The US was a test case for bag fees. US airlines implemented them across the board and the world did not end,” he says. “Initially, the alliances were impediments to such fees, but once an airline adopts it, it spreads for matters of consistency.”

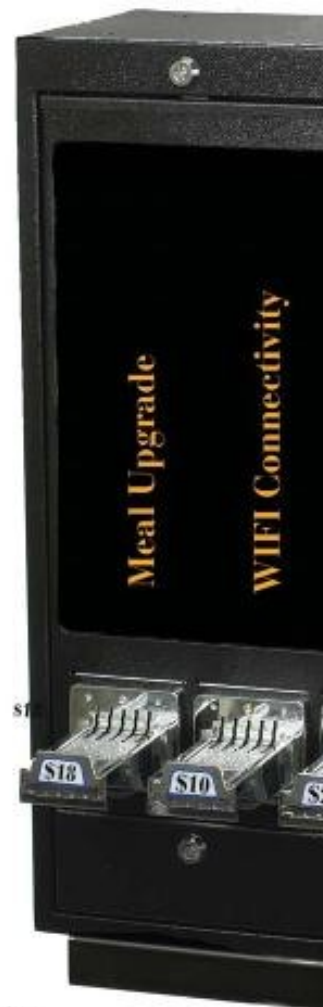
Henry Harteveldt, principal travel analyst for Forrester Research, agrees that US carriers “have disassembled the product as much as they can.” Much of that dismantling was not appealing to travelers. Now, he says, it is time to figure out: “How do we let people craft an experience to their liking that still fits into the airline’s budget?”

Both Harteveldt and Sorensen suggest that the way to passengers’ hearts may be through their stomachs. Food will be the next frontier, Sorensen says. The days of free food in economy cabins—already a memory on most North American airlines’ domestic flights—are numbered even on

transoceanic flights, he believes. But its replacement won’t be the typical buy-on-board snack box designed for a longer shelf life than any food product should have, or a sandwich selection that may run out when the food cart is halfway down the aisle.

Rather, he says, the new version will be pre-ordered, and that’s the key: The airline will know exactly how many passengers have ordered a meal so there will be no waste. The food will be prepared to order, not mass-produced to appear on several flights until it is sold. “For too long, food has been cost-cut to death,” he says. “What a refreshing change it will be when an airline has a product passengers will like. Consumers will be better served than when they were living off the charity of an airline.”

Some airlines already are experimenting with pre-ordered food. KLM, for example, is testing an “a la carte menu” on flights from Amsterdam to 10 long-haul destinations. The options include a Japanese dinner of sushi, chicken with steamed rice and vegetables and a specialty salad; an Italian pasta meal with traditional sides; an organic chicken-and-veggie feast, and Indonesian rijstafel, a favorite among the Dutch. Each meal costs €15, or about \$19.50. For now, economy class passengers can still opt for the free meal, but Sorensen believes the pre-ordered meal will become the norm.





Paying, in fact, can take the pain out of a trip. On a one-stop trip from Barcelona to Istanbul aboard a "full-service" carrier, he was served a bag of potato chips and a cup of table wine. "Had I flown easyJet, I would have paid, but I would have been happier," he says.

Harteveldt notes that United Airlines is offering reserved meal "upgrades"—business class-style brunches—on transcontinental flights for \$19. Essentially, he says, the carrier is allowing coach passengers to "buy your way into an elite-like experience." And on some transatlantic flights from San Francisco it is testing reserved premium meals, also for \$19, with a choice of grilled tenderloin, grilled chicken or cheese tortellini.

easyJet sells an extensive array of snacks, beverages, regional specialties and Starbucks-style meals from a bright, cheery laminated menu. And that's an important feature, Sorensen says. The menu, unlike the unattractive cardboard box emblazoned with an airline logo that flies the US skies, is designed to sell the food.

Raphael Bejar, CEO of AirSavings, a Paris-based company that creates ancillary products for airlines to sell, says it's essen-

tial that passengers see the value of what they are buying. Unbundling airline services "doesn't create value," and carriers have reached the point "where they can't unbundle anymore," he says. To boost revenues, "they must increase the size of each fee unless they create that value."

The latest in AirSavings' product line is Genius365, a concierge service that was designed for business travelers but also is finding popularity among vacationing families, Bejar says. The service can be sold within the airline booking path and the carrier earns a commission. The offering provides a hotel, restaurant and event locator; booking of reliable and reasonable taxi services; access to a physician in an emergency; assistance with rebooking of appointments if travel is disrupted, and other services. "When people are stressed, they want help," he says, and they are willing to pay for it. Although the minimum purchase is for seven days, some travelers are paying the full rate for shorter trips.

AirSavings also offers "bundled services." Airlines can earn high-margin commissions on travel insurance, but sales in Europe have dropped since the EU required websites to switch from "opt-out" to "opt-in" sales tactics. In addition, travelers often are reluctant to buy a product that ideally will not be used. So AirSavings spiced up its insurance offering by adding 30 min. of free Wi-Fi connectivity that is deducted by the second, allowing travelers to use it at whatever intervals and in whichever locations they wish. The result is an increase in "the perceived value of an existing product whose conversion rate has been falling," Bejar says.

The mobile channel, which finally has taken off with the advent of the iPhone, offers new opportunities for ancillary revenues, according to TravelBuddy Commercial Director Jason Rivolta. The UK-based provider of white-label mobile solutions says a little incremental revenue can add up if a product is priced for maximum volume.

Airlines typically get calls from customers with questions in the week before a flight and those calls add costs, he says. TravelBuddy can provide a bundle of text messages that anticipate those questions and provide the answers, as well as a destination weather forecast and other information. If the service is priced at \$2 and offered in the booking path or at check-in, he says, "You get a 15%-20% opt-in. We take 50 cents and the airline gets a profit of \$1.50."

Rivolta notes that between the outbound and inbound flights, airlines "lose" their customers. "They've got a load of money in their pockets and the airline gets nothing." The mobile channel can change that. TravelBuddy produces destination guides that can be included in an SMS pack. Airlines can offer branded guides that furnish a new mobile ad opportunity in much the same way that inflight magazines carry ads.

Within the guide, a carrier can offer its own upsells. The setup also allows customers to buy show tickets, helicopter rides and other activities through the mobile guide. "When they spend, we get a commission and we split it with the airline," he says. He claims the marketing possibilities are endless. An airline could arrange to deliver a branded mobile guide to a passenger upon arrival in a major city and include a personal welcome message from the mayor, for example.

Something New GuestLogix, a company that focuses on onboard retail sales, also sees opportunities for airlines in the mobile channel. But they must be conscious of the fact that



they have to do it right, says Executive VP-New Markets and Products Brett Proud. "What's the point of having an app if you just replicate your website? If airlines can find a way to offer travelers something in addition—a concierge service, say—they can realize the true opportunity and take advantage of the entire journey." Cathay Pacific Airways, for example, doesn't just sell duty-free goods onboard, he says, it sells home delivery of purchased items.

But the biggest thing this year, Rivolta says, is that "airlines are finally starting to realize that the ancillary revenue opportunity lies way beyond things like priority boarding or checking bags. There are lots of other touch points, such as the gate or the lounge or even ground transportation." The goal is to come up with a product or service that can be monetized and add value, he says.

One of the oldest forms of ancillary revenue, the cross-selling of other travel components such as hotels and rental cars, is still underexplored, according to a new study commissioned by Amadeus and undertaken by Forrester

Consulting. Airlines expect the percentage of their revenues generated by ancillary services to double in the next five years, according to the study. Third-party ancillary services, which account for 10% of total ancillary revenues, will generate 13% by 2015.

One of the advantages of cross-selling is that it does not alienate the passenger. "A la carte services are seen by travelers as fees for services that were previously included. This is not the case with third-party ancillary services," says the study, titled "Cross Sell Your Way to Profit." Hotels and car rentals are products that the customer needs and wants.

Airlines are getting the message, says Bobby Healy, CTO of CarTrawler, a company that provides a car rental platform for airline websites. "Our message hasn't changed much, but we're seeing more adoption, even in emerging countries," he says. While initial interest came from LCCs, customers now include hybrid and traditional carriers.

Are airlines putting too many eggs in the ancillary basket? Last fall, Stelios Haji-Ioannou battled with easyJet when

the carrier's ancillary revenue crept up beyond 20% of total revenues; the agreement with Haji-Ioannou's easyJet Group set a limit of 25% so that the airline would not cannibalize other services sold by the group.

More recently, US Airways President Scott Kirby said ancillary revenues would account for 100% of the carrier's 2010 profits.

Harteveldt doesn't believe it's a healthy situation. While acknowledging that "ancillary services are the reason we have not had more financial bloodshed" in the industry, this is indicative of an uncomfortable truth: "The message is that you aren't developing a brand that resonates with a core group of customers. Either that or you don't know how to price your product." At any store, similar products in broad categories, whether shirts or cereals, are "priced all over the place," he says. "In some cases there are tangible benefits, in others intangible benefits."

An airline that offers a better product ought to be able to use cosmetics giant L'Oreal's tagline, he says: "We cost more, but you're worth it." **ATW**

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