



# Taking Off, Into Clearer Skies

**A year-end review of Ancillary Revenues and  
the Airline Industry in 2010, and projections for 2011**

By Raphael Bejar, CEO of Airsavings



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*“It’s been so long since I’ve written anything as positive as the following, it almost feels like a secret. So I will say it quietly. 2010 was a good year for airlines. And if fuel prices don’t skyrocket, 2011 is looking rather good, too.”*

In 2010, the big legacy carriers such as Delta, AMR Corp. and US Airways Groups are profitable for the first time in years. High-flying low cost carriers (LCCs), which were particularly hurt by the drop in demand that accompanied the Great Recession, are also posting gains: Ryanair increased its profits 17% in the first half of its fiscal 2010 and Easyjet posted strong third quarter earnings. In the US, Delta forecasts it will have its first fourth-quarter profit in ten years and AMR, parent company of American Airlines, reported its first profitable third-quarter since 2007.

Yes, some of this success is attributable to a bounce-back from historic lows in 2008 and early 2009. Fuel prices were stable (and low as well), particularly compared to the mid-2000s. But larger factors are at work that suggest that the industry’s performance in 2010 can be repeated in 2011, and perhaps set the airline industry back on a path of sustained operational and financial health.

In short, there is cause for optimism.

So what are those factors that drove airlines’ success in 2010? And what strategies should airlines pursue in order to ensure these record profits continue in 2011?

## Capacity

One answer is increased flights. Many airlines have added more flight options in 2010 in order to be able to sell more fares. Increasing capacity is no real innovation in a time of increasing demand, but there are indications that the industry has done so more responsibly this year, particularly following the sustained capacity cuts within the industry spanning from 2008 to late 2009. An airline analyst with CRT Capital Management Group[1] cites the modest orders for new aircraft along with lack of expansion into unprofitable routes as examples of the airline industry’s new, more responsible approach to raising capacity.

This sort of measured capacity building has allowed airlines to hold costs down relative to demand, putting them in a good position to make profits. It has also allowed them to use excess cash to deleverage, improving their debt positions.

Capacity, in this context, is essentially an expense-side consideration. On the top half of the P&L, however, another shift in approach that has been slowly taking hold in the industry has officially, at the close of 2010 and the beginning of 2011, become standard practice.

## The All-Important Ancillaries

It's no secret that airlines have increased their ancillary offerings over the years. Fees of all kinds have become the norm in the industry, with every airline - both legacy and LCC alike - unbundling the fare and charging for things that used to be free. These have each, in their way, fuelled airlines' increasing reliance on non-fare-based revenue streams.

The challenge for airlines today is how to implement these ancillaries in ways that increase revenues, while improving the customer flight experience. More and more airlines are meeting this challenge, finding sustainable ancillary revenue streams by identifying high-demand offerings and turning passengers into consumers. Three of the most important aspects of ancillary revenue development that will affect airlines most in the coming year (and, similarly, have driven the successes they've had last year) are loyalty, preventative and insurance options and value-added bundling (yes, bundling... more on this below!).

## Increasing Customer Loyalty Increases Profits

Most airlines implement customer rewards programs to promote customer loyalty, yet over the past decade few airlines could point to these programs as reliable revenue generators. Loyalty programs not only offer airlines a way of establishing a core group of clientele, they are attractive to passengers, who can earn anything from seat upgrades, discounts, cash back or other merchandise. Airlines can even partner with hotels and other retailers to expand their loyalty program offerings. According to study by Ideaworks and ezRez Software, there are currently about 100 million Americans who participate in one or more of existing airline programs. Today, the airline industry collectively earns \$10 billion by selling add-on mileage points through frequent flyer programs. And, according to a study conducted by Infosys, memberships are growing at 13% per year, much faster than the growth of the airline industry as a whole.

Moreover, loyalty programs are easily integrated with other ancillary offerings. Innovative ancillaries like private event retailing and concierge services sync nicely with loyalty programs and loyalty programs provide fertile, preexisting customer markets for such initiatives.

## Providing Peace of Mind

Insurance is a highly effective way for airlines to increase revenue as they provide a valuable service to customers and because the policies carry a high profit margin for airlines. But unlike the insurance policies of the past, airline-provided insurance can cover anything from bad weather to lost baggage to flight cancellation. Some weather protection, for instance, allows travelers to protect their travel investment against weather disruption and receive an automated pay-out in case of bad weather, while creating attractive commissions as a new revenue stream for airlines, OTAs and travel distributors. This process can be as simple and straightforward as a consumer buying the weather protection, and if more rain than average falls in their destination during their trip (or if less sunshine is recorded), a predetermined amount of money is automatically paid to them.

Travel insurance and protection provides an optional service to the customer and is an alternative to simply implementing fees for things like luggage, which often (and does) leave consumers feeling cheated.

## Adding Value

Rather than pursuing every new ancillary offering as a for-fee service, some airlines are revisiting the notion of bundling products and services – to great effect. Pairing high-demand products and services with high-margin (if less popular) ones has allowed airlines to meet consumer expectations while maintaining the profitability of their ancillary revenue programs.

A good example of this is the linking of travel insurance with complimentary WiFi access. Travel insurance is a high-profit offering that while useful, has declined in consumer adoption since 2008; whereas WiFi is increasingly an expectation among consumers, and the provision of it being offered for free in conjunction with another service is perceived as added value. Innovative approaches like these are changing the ancillary revenue landscape and leading the industry toward sustainable profitability.

## Booking Path, Mobile, Lounge Access

While the three previous aspects of ancillary revenues are the fundamental building blocks of the great airline industry revenue shift, three more-specific aspects are poised for further refinement in 2011.

Airlines have long acknowledged that the booking path is perhaps the most lucrative environment for ancillary revenue initiatives, but the proliferation of third-party booking sites and OTAs have limited the effectiveness of the booking path for many airlines. Look for airlines to further bolster their online presences in 2011 and fight to reclaim booking share from third-party sites.

Another forward-thinking ancillary option is flight notification via text message. With great potential in the European, Asian and US markets and where cell phone penetration is high, SMS itineraries are ideal as either a value-add or an ancillary revenue opportunity. For an airline looking to enhance its brand image, SMS is an innovative component of a consumer-centric marketing strategy.

There's also the ancillary service of offering customers access to airport lounges. Lounge access has traditionally been provided as a value-add in connection with a loyalty program. Now, many LCCs and mid-sized carriers are offering partial or one-day access as an ancillary service with great results.

## Looking forward

Yes, airlines have had a good year. Capacity discipline, a focus on ancillary revenues, and external factors have combined to provide carriers around the globe with strong profits. Fundamental shifts in the operating model, including the widespread adoption of ancillary revenue development strategies, bode well for the industry and hint at a period of sustainable profitability.

The industry is cyclical, however, and still very much at the mercy of fixed operating costs like fuel and labor. Airlines seem to have realized this, and are investing in sustainable revenue streams that are not subject to the volatility so recently experienced. After all, 2008 (and the lessons we as an industry had to learn to survive) are never far from our minds.

But for right now, things look rather good for the airline industry. Raise your glass (of champagne I hope!) to the future success of the industry and the continued change that will set carriers globally up for future success.

*“Here’s to clearer skies and better times for airlines in 2011.”*

Raphael Bejar, CEO Airsavings

December, 2010



*Helping airlines create revenue and stay competitive since 2001*

### **About Airsavings – Ancillary Revenue Solutions for Global Carriers**

Airsavings specializes in facilitating the two fundamental operational imperatives of the airline industry: cost reduction and revenue generation.

As the air travel industry has become more competitive and more reliant on emerging technology at both the front end (sales and distribution) and the back end (procurement and purchasing), Airsavings has helped airlines maintain their competitive edge and begin to evolve toward a new, e-commerce operating model. By assisting airlines in unbundling their core services and providing a speedy, cost effective platform on which to offer ancillary services, the company allows its clients to swiftly and easily develop alternative revenue streams. And by employing one of Europe’s most successful group buying systems, Airsavings helps member airlines obtain competitive pricing on critical goods and services.

**Raphael Bejar** is CEO and founder of Airsavings, based in France with offices in Singapore. Bejar has more than 15 years airline industry experience and founded Airsavings in 2001 to meet the unique and growing needs of low cost and mid sized airlines, combining innovative group buying techniques with web services technology to provide ancillary revenue solutions to those airlines. Its group buying expertise, combined with the knowledge of airline internet booking engines, has uniquely positioned Airsavings in the area of ancillary revenues - now a vital lifeline for airlines. Airsavings proprietary industry platform called AirlinePlus, enables carriers to deliver a multitude of ancillary services found most useful and with the greatest potential for mass adoption and profitability.

**For more information, please visit [www.airsavings.net](http://www.airsavings.net).**

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