Ancillary Revenue Trends To Boost The Bottom Line

Jay Sorensen, CEO, Ideaworks and leading authority on ancillary revenues
Ancillary Revenue Boosts the Bottom Line

Ignore the opportunity provided by a la carte fees, ancillary revenue, and unbundled products at your own peril.

Jay Sorensen – President of the IdeaWorks Company
The agenda for this presentation.

- Let’s begin with a definition and manifesto
- Selections from a worldwide a la carte buffet
- Checked bag fees are coming your way
- Seeking your own ancillary revenue bliss
- Time for questions
About me

- Part of the Midwest Express start-up team, was Director of Marketing, threw bags, cleaned aircraft, and was an early believer in ancillary revenue.
- Started IdeaWorks in 1996 to “Build Revenue through Innovation.”
- When my kids complete school, my family will have visited every major national park in the USA.

Volunteering at Cumberland Gap National Historic Park in Kentucky.

IdeaWorks

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What is ancillary revenue?

Revenue beyond the sale of tickets that is generated by direct sales to passengers, or indirectly as a part of the travel experience.

IdeaWorks further defines ancillary revenue using these categories: 1) a la carte features, 2) commission-based products, 3) frequent flier activities, and 4) miscellaneous sources such as advertising.

Source: Ancillary Revenue Guide by IdeaWorks
This genie is not going back into the bottle.

- A la carte fees are an economic necessity.
- Airlines are implementing fees for services that once were included in the price of a ticket.
- Consumers **pick and choose** the services and features they want based upon the desire to **maximize convenience** or minimize price.
- Business models are changing to emphasize customers who are willing to **pay for perks**.
- Savvy carriers have quickly embraced the idea and seem to now “**ask for the sale**” at every opportunity.
Oil prices are the catalyst.

February 2008 – United was the first US-based major airline to announce baggage fees for the 2nd piece.
Using the fare lever has become difficult.

- Changes must be filed in thousands of markets.
- Sometimes the industry marches in lockstep; sometimes airlines take the opportunity to inflict pain in hotly competitive markets.
- Major carriers must worry about those pesky low cost carriers that invariably ignore industry-wide pleas for saner pricing.
- Fare comparisons on shopping sites display the unblemished truth of lowest fares.
The Orbitz pricing matrix excludes fees.

Consumers may click the “Additional baggage charges may apply” for a list of carrier-specific fees.
United Airlines became a believer in 2008.

Glenn Tilton - Chairman, President and CEO:

“We led the industry toward unbundling and ancillary revenue growth, with our January announcement of second bag charges and our new product launches throughout the year.

In 2009 we expect to generate in the area of $1.2 billion from fees and ancillary revenue, up about $300 million from 2008.

Unbundling works. The revenue generated from these products and services is now a proven and meaningful contributor to United's bottom line.”

Allegiant Airlines defines its ancillary revenue mission.

“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.

We aim to continue to increase ancillary revenue by further unbundling our air travel product.

We also generate revenue from third party products through the sale of hotel rooms, ground transportation, attraction and show tickets.”

Source: Allegiant 2010 Annual Report
A la carte is served at hotels, car rentals, and cruises.

- Norwegian Cruise Line’s new 4,200 passenger cruise ship “Epic” delivers “freedom of choice” with more dining options.
- $18 upgrade for Moderno, an Argentine-style churrascaria.
- $20 upgrade for French Le Bistro.
- $25 upgrade for Cagney's steakhouse.
- Many consumers will happily pay a premium when offered more choices.

The Shanghai noodle bar on the Epic is 100% a la carte.
Let’s consider this ancillary revenue manifesto.

- Define your **airline brand** first and use this to steer your ancillary revenue customer strategy.
- Create a **sales-oriented culture** that respects your front line employees.
- Base your a la carte sales on principles that support your brand, respect **your culture**, honor **customer choice**, and provide a good return for investors.
It’s a revolution that has global traction.

<table>
<thead>
<tr>
<th>Annual Financial Disclosures of Ancillary Revenue</th>
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<tbody>
<tr>
<td>2010 Results Posted by 47 Airlines  €15.11 billion ($21.46 billion)</td>
</tr>
</tbody>
</table>

Source: Amadeus Review of Ancillary Revenue Results by IdeaWorks issued 31 May 2011.
Today’s a la carte selections include legacy, hybrid, and low cost airlines.
Air France – Fare lock before purchase.

- “Time to Think” option to hold a reservation and price for up to 14 days.

  The Time to Think option: 15 € per passenger.
  Payable now by credit or debit card (non-refundable).
  Reservation guaranteed until Friday 16 September 2011 - 22:00
  You must pay for your ticket in the “Manage your reservations” section of our website

- €10 for Voyageur class reservations on all flights within Europe, and Europe – North Africa.
- €15 for reservations in all cabin classes (except La Première) on all other routes.
- IdeaWorks estimates revenue of €0.50 to €1.25 per passenger.
Wizz Air – Las Vegas style payouts.

- Consumers buy “Delay Warranty” protection from late flights; the carrier pays a penalty if the flight arrives late.

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Benefit from your delay!
Purchase a delay warranty together with your flight and get EUR 100 credit should your flight be delayed by 2 hours or more.
To purchase this service you must be a registered customer. To login, please use the box on the left hand side. To register please go back to the contact page to provide the necessary information.
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- Wizzair charges €10 per passenger per flight for the benefit of €100 per passenger if arrival is delayed more than 2 hours.

- IdeaWorks estimates revenue of €0.05 to €0.10 per passenger.
Wizz Air does not gamble with consumers.

**list of service fees**

If you purchase certain services at the airport you may be required by the agency of Wizz Air to pay extra fee in addition to the service fee defined below. Information about the extra fees is available at the airport.

<table>
<thead>
<tr>
<th>name of the fee</th>
<th>calculation method</th>
<th>amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>Booking fee</td>
<td>Per flight per passenger</td>
<td>5 EUR / 4 GBP</td>
</tr>
<tr>
<td>MasterCard, Visa, Diners Club</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Booking fee</td>
<td>Per flight per passenger</td>
<td>2.5 EUR / 2 GBP</td>
</tr>
<tr>
<td>Solo, UK Maestro &amp; Bank transfer</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Call Centre fee</td>
<td>Per flight per passenger</td>
<td>10 EUR / 9 GBP</td>
</tr>
</tbody>
</table>

Wizz Air offers the most thorough online disclosure of a la carte fees.
Vueling – Every seat is precious.

IdeaWorks estimates revenue of €0.25 to €2 per passenger.
Southwest – The overhead bin fee.

- The airline sells Early Bird check-in which provides a priority boarding position and earlier access to overhead bin space.

Would You Like to Add EarlyBird Check-In?

- We'll automatically check you in and reserve your boarding position before regular check-in begins so you'll have a better seat selection.

- Automatic Check-In
- Better Boarding Position
- Earlier Access to Overhead Storage

*Conveniently print your boarding pass with pre-assigned boarding position anytime within 24 hours of departure.

- Southwest charges $10 per passenger one way.
- IdeaWorks estimates revenue of €0.50 to €1.50 per passenger.
Be certain you can deliver what you sell.

- EasyJet: “Where passengers are bused to the plane, we cannot guarantee Speedy Boarders will be first off the bus. Where busing is frequent on a route, this is reflected in the Speedy Boarding price you pay.”

- Ryanair: Very likely allows more than 40% to purchase early boarding.

One customer posted online, “It’s a total rip-off when a bus is used for boarding.”
Ryanair – An incentive to check in online.

- The airline charges €40 or £40 per passenger to print a boarding pass at the airport.

- The airline admits 99.9% of passengers check in online. The fee was deemed illegal by a Spanish court.
- The fee is designed to reduce operating costs -- not generate revenue.
American Airlines – VIP for a fee.

- American’s “Five Star Service” provides personal attention by an airline employee to assist during passenger arrival, transfer, and departure.
- Includes Admiral’s Club.
- IdeaWorks believes the service generates $30,000 revenue per day.
## FFPs – Revenue exceeding checked bags.

<table>
<thead>
<tr>
<th>Airline</th>
<th>2010 Revenue Disclosed</th>
<th>Per Passenger</th>
</tr>
</thead>
<tbody>
<tr>
<td>United Continental</td>
<td>$3,000,000,000</td>
<td>$20.59</td>
</tr>
<tr>
<td>Delta</td>
<td>$1,600,000,000</td>
<td>$9.84</td>
</tr>
<tr>
<td>Qantas Group</td>
<td>$1,141,240,000</td>
<td>$27.55</td>
</tr>
<tr>
<td>TAM</td>
<td>$505,764,144</td>
<td>$14.64</td>
</tr>
<tr>
<td>Alaska</td>
<td>$372,800,000</td>
<td>$15.98</td>
</tr>
<tr>
<td>South African</td>
<td>$49,956,000</td>
<td>$7.42</td>
</tr>
<tr>
<td>Iberia</td>
<td>$23,430,000</td>
<td>$0.93</td>
</tr>
</tbody>
</table>

*Source: Amadeus Yearbook of Ancillary Revenue by IdeaWorks, 2011*
Where the world is heading.

Consider for 2012 whether to:

- Charge fees for checked baggage systemwide.
- Offer premium seat choices for a price.
- Provide early boarding benefits.

Consider for the future whether to:

- Link your frequent flier program to ancillary revenue activities.
- Create annual products for a la carte services.
- Sell upgraded meal options.
You will likely begin with bag fees.

- Baggage fee revenue jumped above $3.4 billion for 2010, a year that saw the full effect of a mature fee environment in the US.
- According to a US government study, when faced with fees, travelers checked 40% to 50% fewer bags on some carriers.

Source: Billions of Dollars in Baggage Fees Travel the Globe IdeaWorks report, August 2011.
Checked baggage has become the million dollar decision.

Per passenger annual revenue estimates by IdeaWorks:

- $0.51  British Airways (23 kg. free allowance, Europe)
- $0.80  jetBlue (fee for 2nd bag, 1st bag free)
- $0.84  Air Berlin (20 kg. free allowance)
- $4.54  American (system wide)
- $7.98  easyJet (70% passengers check bags)
- $8.25  Ryanair (€20 average, 1/3 passengers pay)
- $8.26  Allegiant

*Based upon 2009 financial and traffic disclosures by carriers.*
Airline CEOs found the holy grail.

“First bag is down about 15%, second bag is down 50%, for a combined drop of 25% in total checked baggage . . . it has allowed us to do a much better job of what our customers want us to do.”
– Doug Parker, US Airways

“I think that we’re seeing very moderate friction on the fees in the unbundling.”
– John Tague, United Airlines

“We’re not remotely regretful of our competitive position nor our decision.”
– John Tague, United Airlines
United expands baggage fees to more global destinations.

<table>
<thead>
<tr>
<th>For travel between US/Canada &amp;</th>
<th>Prior to new fee</th>
<th>Travel after 15 August 2011</th>
</tr>
</thead>
<tbody>
<tr>
<td>Asia (except Japan and Hong Kong)</td>
<td>Free</td>
<td>$70</td>
</tr>
<tr>
<td>Australia/New Zealand</td>
<td>Free</td>
<td>$70</td>
</tr>
<tr>
<td>Micronesia</td>
<td>Free</td>
<td>$70</td>
</tr>
<tr>
<td>Middle East</td>
<td>Free</td>
<td>$70</td>
</tr>
<tr>
<td>Africa</td>
<td>Free</td>
<td>$70</td>
</tr>
</tbody>
</table>

Bringing on baggage fee bliss.

- Create a product, not another fee.
- Begin modestly and test price levels.
- Provide a 25% to 50% discount for pre-payment.
- Strive for simplicity – avoid complex fee schedules.
- Introduce subscription pricing.
- Provide an online baggage fee calculator.
- Include bag perks for your elite members.
Alaska creates a product, not a new fee.

- Delivery is guaranteed within 20 minutes after arrival at the gate.
- If Alaska fails to deliver, the passenger receives their choice of a $20 savings voucher or 2,000 frequent flier miles.
- It’s an approach that added value for the consumer and placed a price on slow.
- Delta added FedEx-style online bag check April 2011.
United offers annual bag subscriptions.

- Premier Baggage provides a year of first and second bag fees for one year for $349.
- United MileagePlus Explorer credit card provides first bag free, priority boarding, and two annual United Club passes each year. The annual fee is $95.
Emirates makes bag fees easy.

- The airline provides an easy-to-use online baggage fee calculator.
- 20% discount for pre-payment online.
Spirit aggressively collects bag fees.

<table>
<thead>
<tr>
<th>Categories</th>
<th>Booking</th>
<th>Web Check-in</th>
<th>Airport</th>
<th>Gate</th>
</tr>
</thead>
<tbody>
<tr>
<td>$9 Fare Club</td>
<td>$18</td>
<td>$23</td>
<td>$38</td>
<td>$45</td>
</tr>
<tr>
<td>All Others</td>
<td>$28</td>
<td>$33</td>
<td>$38</td>
<td>$45</td>
</tr>
</tbody>
</table>


- Online booking process is interrupted with savings on checked baggage, and consumer confirmation of the carry-on policy.
- “$9 Fare Club” charges a $59.95 annual fee for amenities and benefits.
Southwest offered another path in 2008.

- No 1st or 2nd bag fees
- No change fees
- No fuel surcharges
- No snack fees
- No aisle or window seat fees
- No curbside check-in fees
- No phone reservation fees
Both sides of the debate claimed success.

- “Our passenger revenues were up over $240 million or 10.8% . . . We continued to believe we are gaining market share with our steadfast commitment to our Bags Fly Free.”
  - Laura Wright, Southwest Airlines Q1 2010 Earnings Call.

- “We don’t see the share shift . . . Southwest is the only one gaining a whole bunch of different small shares from the airlines. It becomes enough that they can see it in the numbers.”
  - Scott Kirby, US Airways Group, Inc. Q3 2009 Earnings Call.
Finding ancillary revenue bliss.

- Always begin the journey by defining your **brand**.
- A la carte pricing should **support the brand**, not change it.
- Link fees to your **business model**, not to cost increases.
- Seek wisdom from **customers** and front line **employees**.
- Create a new **product**, not a new fee.
- Anticipate change - - don’t be surprised when it arrives through **alliances** and partnerships.
- Ancillary revenue is **not an ad-hoc project**, it’s meaningful cash flow.
Time for Questions

Go placidly amid the noise and the haste, and remember what peace there may be in silence. Speak your truth quietly and clearly; and listen to others. If you compare yourself with others, you may become vain or bitter, for always there will be greater and lesser persons than yourself. Enjoy your achievements as well as your plans.

*Excerpts from "Things to be Desired" by Max Ehrmann*
About IdeaWorks: IdeaWorks was founded in 1996 as a consulting organization building revenue through innovation in product, partnership and marketing. Its international client list includes the airline, hotel, marine, railroad, and consumer product industries. The firm is a leading expert on creating ancillary revenue opportunities for airlines. IdeaWorks has worked with airlines on ancillary revenue projects in Europe, the United States, and South America. The consulting firm has helped create frequent flier programs and develop co-branded credit cards in the USA, Europe, and South America. Learn more at: IdeaWorksCompany.com

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