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LOW-COST AIRLINE WORLD

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THE FALLOUT:

How will LCCs cope post-volcanogate?

PLUS: Interviews with Gatwick Airport and Ryanair

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EDITOR
Daniella Horwitz: Daniella.Horwitz@ubmaviation.com
Tel:+44 (0) 207 579 4847

JOURNALISTS
Mary-Anne Baldwin: Mary-Anne.Baldwin@ubmaviation.com
Tel: +44 (0) 207 579 4843
Sarah Morgan: Sarah.Morgan@ubmaviation.com
Tel: +44 (0) 207 579 4853

SPECIAL CONTRIBUTORS
Alex Derber, Donal Hanley, Nathan Smith, Richard Cushing

PRODUCTION
Kalven Davis: kalven.davis@ubmaviation.com
Tel:+44 (0) 207 579 4851

DISPLAY ADVERTISING
Simon Barker: simon.barker@ubmaviation.com
Alan Samuel: alan.samuel@ubmaviation.com
Tel: +44 (0) 207 579 4845/6

GROUP PUBLISHER & SALES
Anthony Smith: Anthony.Smith@ubmaviation.com
Tel:+44 (0) 207 579 4875

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E-EDITOR & CIRCULATION MANAGER
Paul Canessa: paul.canessa@ubmaviation.com
Tel: +44 (0) 207 579 4873

All subscriptions enquiries to:
paulcanessa@ubmaviation.com
Tel: +44 (0) 207 579 4873
Fax: +44 (0) 207 579 4848

Website: www.ubmaviationnews.com

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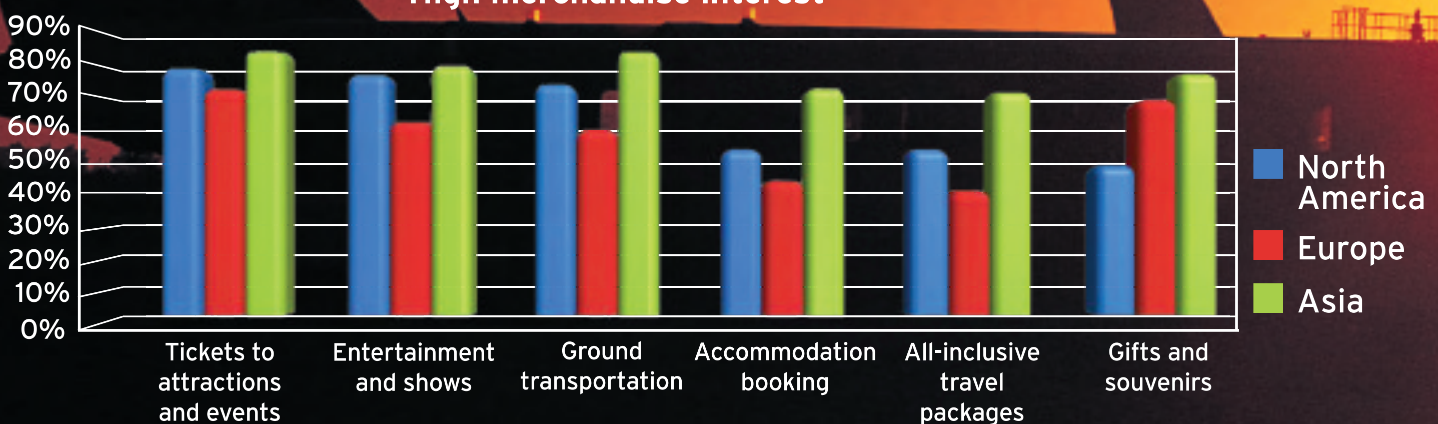
How airline profits can soar with an onboard store

Ancillary revenues are the leading growth segment among airlines and across the world they are seeking ways to maximise their return on investment in this area. For most airlines, this will mean a move away from unsustainable, fee-based ancillaries into areas such as onboard retailing. **Richard Cushing**, VP and general manager at GuestLogix EMEA, has over 30 years of retail and supply chain experience including nine years developing and managing retail programmes at British Airways. He guides us through the benefits of onboard retail.

High merchandise interest

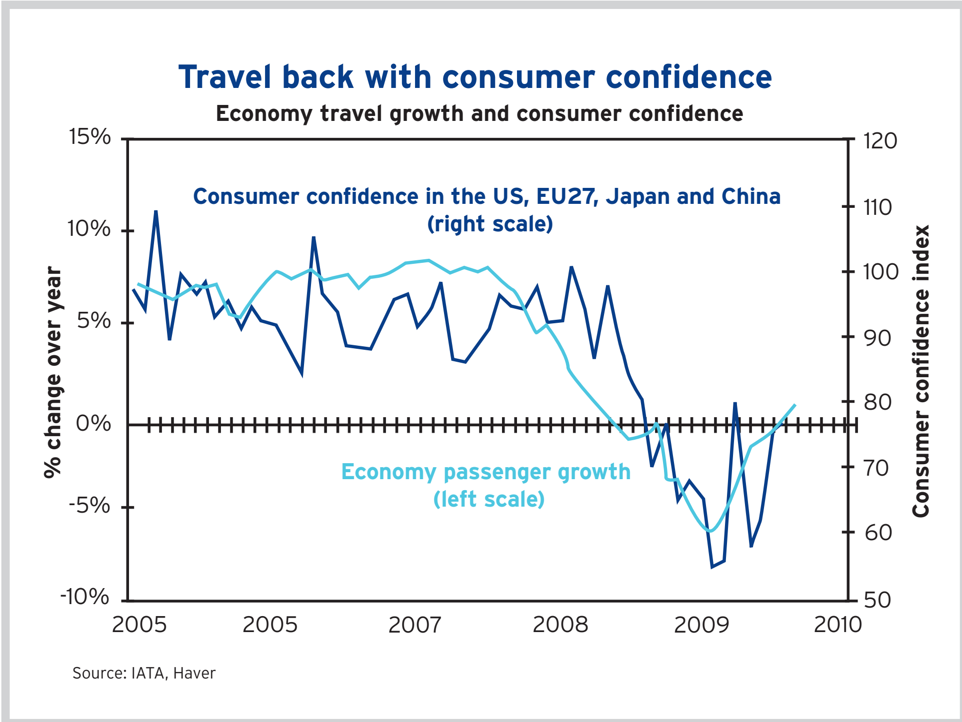


ANCILLARY REVENUE HAS BEEN an important driver in the success of low-cost carriers (LCC). À la carte pricing, which was pioneered by Air Canada and introduced at major North American carriers, has helped regain profitability with United Airlines, boosting revenue by £483m ($690) in 2009 with baggage fees and other add-on charges.

A full 20 per cent of Ryanair's overall revenue comes from ancillary services and easyJet earns nearly 40 per cent of its per-seat revenue from ancillary sources. easyJet saw its ancillary revenue per seat increase 38.2 per cent between 2008 and 2009, with most of that growth driven by a 53.3 per cent increase in baggage revenue and a 43 per cent increase in speedy boarding and discretionary revenue.

Revenue streams from non-ticket related sales (including cargo) have grown from £20bn ($29bn) in 2006 to £38bn ($54bn) in 2009 according to the Air Transport Association (IATA) and the Centre for Asia Pacific Aviation (CAPA). Airlines are earning additional revenue from services including preferred seating, checked bags, blankets, food and are now seeking to find ways of selling Wi-Fi access onboard in sufficient volume to offset capital costs. It's a trend that is helping carriers get back to black after the major economic slump.

While most attention paid to ancillary revenues is on fees imposed on travelers (i.e. checked baggage fees), many airlines are realising the significant revenue potential represented by in-cabin sales. Far more sustainable in terms of growth than à la carte fees, in-cabin sales are poised to be the future of airline ancillary revenues, and those airlines that are early to this onboard party are already carving out a substantial profit and competitive advantage.



Source: IATA, Haver

Non-fee ancillary revenue sources – of which in-cabin sales are a principal component – have many advantages over both fee imposition and core seat sales. When a new service gains traction with consumers airlines can receive scalable gains, and when they address unmet needs they can also create a better brand

THINKING BEYOND THE TICKET

Every airline is looking at non-ticket revenue to contribute towards profit and growth. There are many options but the downside to most is travelers' perceptions that the airline is relentlessly chipping away at service and amenities at customers' expense, and thereby undermining service, value and longer-term loyalty. In many cases, airlines have already gone as deep as they can go with cost-cutting and are now at the mercy of potential fuel cost increases as they battle to achieve profits. An effective way to drive non-ticketed revenue is to offer consumers a reason to consider the airline as a choice for the purchase of products and services that add value to their trip. Tailoring these to individual travelers, by destination and by type of travel, is a powerful way to build loyalty to the airline brand.

To succeed, airlines must re-think their traditional relationship with travelers. Airlines must master the art of selling more than just tickets. The relationship must shift from carriers and passengers to marketers and consumers. Passengers that are encouraged to become consumers ultimately become long-term buyers and a consistent source of non-ticketed revenue.

Repositioning themselves as retailers, airlines can offer new services and raise their profile as a carrier of choice. By viewing travelers as consumers, airlines can transform the cabin into an 'onboard store', benefiting stakeholders, the airline, travelers, content providers and investors.

Many airlines already use their websites and networks for ancillary revenue development, and extending this usage to broaden the reach of the 'onboard store' is a logical step. As airlines build consumer awareness and loyalty for the selection of products and services offered onboard, they will be able to drive greater differentiation and preference for their brand. This enables the airline to become an integrated provider of travel services by extending the onboard store outside the aircraft, providing relevant services to travelers throughout their journey – not just during flight.

The question airlines must resolve is not 'to sell or not to sell' but rather 'what to sell and how to sell it.' Airline travelers may be a captive audience, but nothing will compel them to buy unless a product or service is presented to them properly. It is important to remember an old statistic about movie theatres and theme parks: less than 50 per cent of sales happen at the door; the rest is from concessions sold to a captive audience.

The market for non-ticket direct sales to consumers was £7.7bn ($10.3bn) in 2008, according to Ideaworks; however Guestlogix's analysis shows that the average purchase per passenger was only a very modest £1.26 ($1.08). Real value for both the consumer and the airline can only occur when the airline focuses on the customer; only at this point can an airline hope to meet its customers' needs and begin to build consumer – not traveler – loyalty.

Building a customer relationship through onboard retailing means adopting some concepts that are familiar to traditional, ground-bound retailers and marketers. These include: consumer insight – airlines will need to identify what travelers want to buy and how they prefer to shop; merchandising – airlines will need to develop products tailored by consumer segments and destinations and find new partners that bring real value; and promotions – airlines will need to offer promotions to engage potential customers.

THE ONBOARD RETAIL STORE MODEL

The 'onboard store' concept emphasises the airline's ownership of the marketplace inside the aircraft. Recreating that space as a retail store allows an airline to gain

revenue from 'impulse' and 'captive spending', monetising and capturing the consumer behaviours of 'impulse' and 'captivity'. The onboard store operates in a strictly contained shopping environment 30,000 feet in the air. The 'store' has locked doors with shoppers strapped inside for a fixed amount of time, often with no distractions, and often with plenty of idle time. With the average consumer visit to a supermarket at 20 minutes or above, imagine the market potential of an onboard store populated by shoppers on a two to four hour flight.

A key aspect of capitalising on consumer captivity is streamlining the purchasing process. The current approach relies on the flight attendant as the facilitator to the sale, but the application of technology can shift the sale to become more passenger-centric. The most powerful onboard customer experience is one that is focused on passengers and highly relevant to their immediate wants and needs. Products and services sold onboard should center on consumers, where they are going and what they are doing when they get there.

Airline passengers are among the greatest consumers in the world. They are focused shoppers with a strong appetite to purchase. Business travelers are time-starved and anxious to make the most of their down-time in a new destination. Leisure travelers are in the mindset of personal indulgence and self-reward. Analysis shows that 58 per cent of frequent flyers are high income males and the majority of those (61 per cent) are in the 25-54 age bracket – that with the highest purchasing potential. About half of all travelers want to buy destination-related items onboard and leisure travelers are more likely to be brand loyal with seven in 10 belonging to loyalty programmes.

A wealth of information exists about the purchase intent and habits of airline passengers – available and accessible through frequent flier program data or through general demographic research, which means there are ample opportunities to personalise product and service offerings, which can include: tickets to attractions and events such as theme parks and museums; ground transportation to and from the airport; accommodation and bookings at hotels, restaurants and spas; travel packages for getaways; gifts and souvenirs and in-flight entertainment.

"The question airlines must resolve is not 'to sell or not to sell' but rather 'what to sell and how to sell it.' Airline travelers may be a captive audience, but nothing will compel them to buy unless a product or service is presented to them properly."

CLIMBING ONBOARD

Because ancillary revenue development is still relatively young and onboard retailing still younger, decisions made today on these opportunities can lead to clear competitive advantages.

For LCCs, which already derive a significant percentage of their operating revenue from ancillary sources, the importance of a strong and effective onboard retail presence is even more pronounced. With the total onboard retail spend estimated at between £2-3bn ($3-4bn) last year, it is clear that there is much potential in this area. LCCs competing with legacies on the basis of fare price need a robust onboard retail strategy – as well as efficient overall ancillary revenue strategies – in order to preserve their competitive edge.

The 'onboard store' may be a long way from the traditional brick-and-mortar retail experience, but with more airlines willing to view passengers as consumers, the 'store' will increase its relevance in leaps and bounds. The true value of passengers as consumers is beginning to define the airline marketplace. Will your airline be ready to soar?