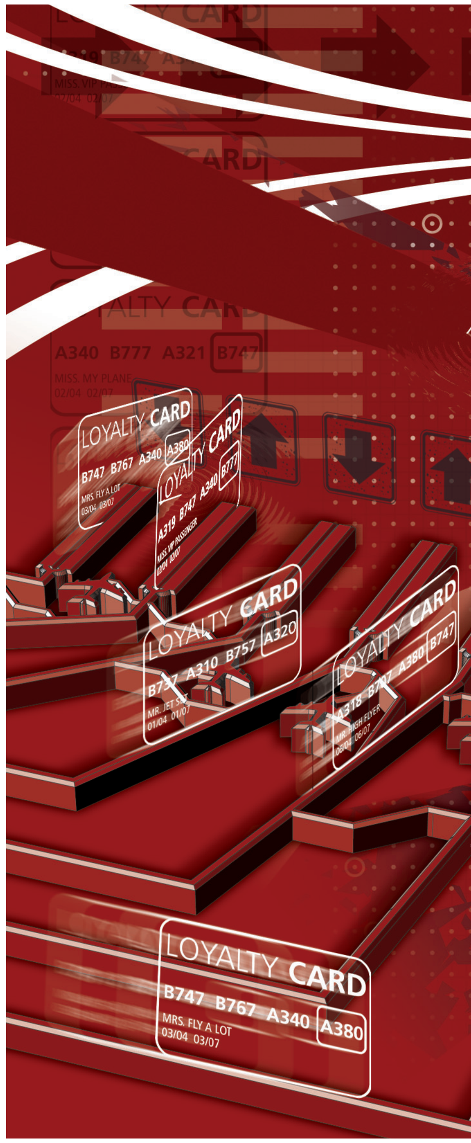
BY **RAVINDRA BHAGWANANI** AT **GLOBAL FLIGHT MANAGEMENT** IN **OFFENBACH**

Profits and loss



Carriers are under pressure to earn more and spend less on their frequent flyer programmes, but that should not be at the expense of keeping customers loyal

For followers of the frequent flyer programme (FFP) the good news is that they are still alive and well. As the FFP approaches its 25th anniversary next year, few would seriously question the contribution of one of the industry's most successful marketing tools. But less encouraging is evidence that loyalty programmes, like much else in today's environment, are often being run for maximum cash and minimum cost. The risk is that with the focus elsewhere, the customer is forgotten.

There is, of course, nothing wrong in sound cost management nor an attempt to make profit out of an FFP. But it may become dangerous if such objectives are allowed to obscure the wider role that loyalty schemes are designed to play as part of an airline's customer relationship management (CRM). After all, the reason why FFPs exist is to keep customers coming back.

It is true that an increasing number of carriers are successful at operating their schemes profitably, often contributing significantly to their bottom line. So it is tempting to look for ways to increase this profitability as a means of subsidising less-profitable areas of the business. There seems to be almost unlimited room to do so. Eric Platteau, vice-president relationship marketing at European independent SN Brussels Airlines, confirms this attitude: "Our FFP, Privilege, is profitable, but we are always looking for more. Any contribution to make our profit more significant is, of course, welcome."

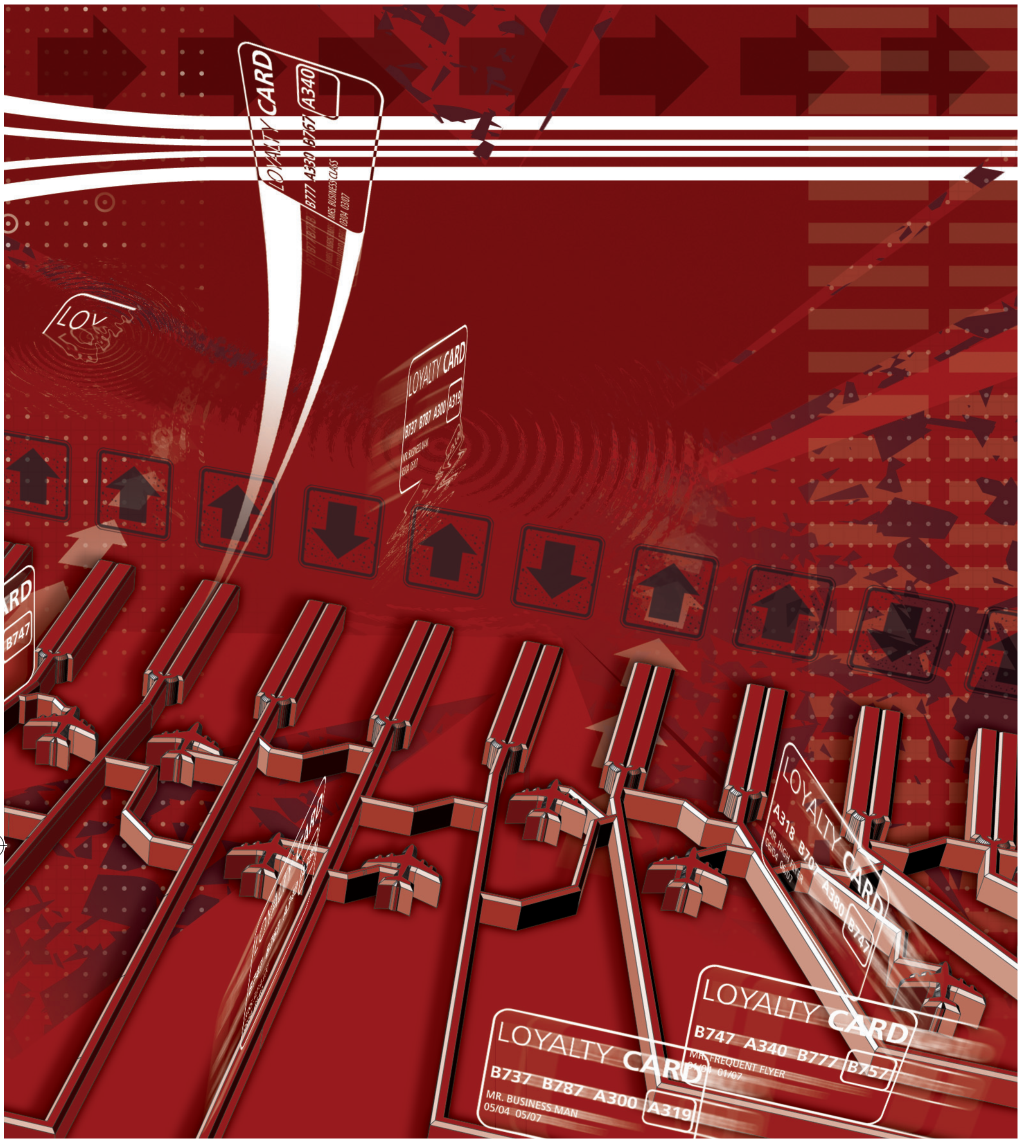
Increasing revenues

Increasing revenues can be done in two ways. The traditional method is to expand the sale of miles to partners. There is no issue with this from a customer perspective unless increased demand for award flights leads to airlines offering fewer attractive redemption opportunities than before.

The second method, newer and potentially more risky, is to raise revenues from the travellers themselves when they redeem their points. Long gone are the days when carriers such as KLM would even absorb the airport charges when its frequent flyers booked their reward flights. Airlines now expect passengers to pay for such routine charges. Yet some now go a good deal further in finding ways to charge their members with a host of service fees for using paper tickets and call centres, or for making changes and cancellations to award flights.

Air Canada is among the most active here, perhaps not surprisingly given the fact that its Aeroplan programme has been outsourced to an independent company, whose aim is to maximise its profit. Such a move makes good sense from the perspective of a carrier striving to make money, but it also suggests that the FFP may no longer be so closely aligned to the overall strategic interests of the airline. For instance, the latest round of fee increases includes the stipulation that award bookings can only be cancelled up to three weeks before departure, with the penalty of a C$135 ($109) fee or the forfeit of the miles. Yet such penalties may alienate customers from the programme and eventually even from the airline. Although Aeroplan positions itself as an independent loyalty programme without any visible link to Air Canada, the connection remains in the mind of the public. Negative impressions must fall back on Air Canada.

More subtle revenue sources are fees for award bookings made through a call centre rather than online. This



might be acceptable in the case of British Airways, where a fee of €35 ($46) only applies to award bookings on BA that could otherwise have been made online. But if such a fee is levied for all partner airline awards, as is the case for Swiss International, even when it is not possible to book these awards online, customers are left facing a fee that they cannot avoid. The critical balance between fair and unjustified fees needs to be found before customers lose faith in the programme.

Cost reduction

The other way to increase profitability is, naturally, to reduce costs in three key areas:

- customer service costs, including employee training and call centre staffing;
- marketing collateral, such as newsletters and promotional material; and
- operational management, with the inevitable downward pressure on employee numbers.

Reducing customer service costs results directly in a deterioration of quality

Reducing customer service levels can clearly cause direct damage to the quality of a programme. Longer waiting time in call centre queues, agents who know less about the loyalty scheme than the clients or the lack of any direct contact with service staff are all potential causes of customer dissatisfaction. While members may understand the need for cost reduction to a certain degree, there are limits. Frequent flyers are traditionally high worth individuals who may well feel that they should be treated accordingly by their airline.

That is just as true in the area of marketing collateral. Some airlines have pushed hard to ensure that all marketing takes place online. But while it may be much cheaper to send an e-mail rather than a printed newsletter the customer may have a different view. It may be unfashionable to raise the point, but even now not everyone has internet access and there may well be executives, especially in the lucrative over-50 bracket, who prefer not to read marketing e-mails.

SN Brussels was one of the first airlines to eliminate all printed collateral material. Eric Platteau presented his experiences at the first FFP conference in Madrid *(see panel over page)*. But he agrees that there is a danger that such a pure cost focus may have a negative impact on the way customers perceive an FFP. "The balance between an airline's objectives and customers expectations is vital," he admits.

Negative impact

Therefore, it is important to react flexibly and eventually withdraw measures that seem to have a negative impact. Once such drastic measures have been implemented, however, the question remains whether an airline would really turn back the clock and increase costs again – and whether the FFP management would admit that there had been a negative impact at all if no external performance audit is implemented.

The last area not immune from cost cutting is, in common with other areas of airline life, in management. Cutting back employee numbers here often results in a situation where remaining staff are overburdened with operational tasks and left without sufficient capacity to develop the programme further from a strategic perspective. An FFP run under such conditions is unlikely to provide the value to its parent airline as it should.

No doubt all three areas can produce substantial upfront savings. But the longer term revenue losses should be balanced against them. These are not always obvious since such losses often do not impact the FFP cost centre itself, but show up elsewhere in the business.

Airlines pursuing only profits from their FFP will not be able to ignore the real problems for ever. One such is a permanent decrease in the activity rate of members. The preferred explanation from carriers tends to be that more infrequent travellers become programme members, but that may not tell the whole story. The truth is that customers often become less loyal and start to shop around. It is all too easy to put this down to the ease of the internet, but the underlying problem is that a number of FFPs have lost a degree of their loyalty effect.

If that is true, then airlines may have to take a broader view of the FFP, not as a standalone issue, but part of their overall CRM approach. As such it will have an impact on customer behaviour and, ultimately, on revenues. Indeed, such a holistic approach seems to be the way forward. The traditional organisational structure that splits responsibilities between the FFP and CRM results in a lack of an overall vision and often acts as a block to other carriers in taking a broader view.

The customer experience

A carrier might be successful at various CRM activities and manage to build a positive relationship with its passengers across the whole customer experience. But the FFP, with its pure profitability mantra, does not necessarily fit into that picture.

With the FFP being one key element between the airline and the customer, this risks diluting the whole relationship. A look at corresponding online frequent flyer forums can be instructive in gaining an impression about the importance of FFPs in the overall perception of airlines. There is little doubt that there is a negative effect on customer behaviour from a loyalty programme that seems less attractive or friendly.

While cost control is a necessary exercise, it is important to take a wider view. Indeed, for example, many airlines have looked into lowering the cost base by eliminating printed newsletters, for example, but have decided instead to view them as an additional investment – rather than a cost – helping to build a better relationship with the customer. Contemplating the FFP in a wider CRM context has led them to offer their customers what they want, rather than what the airlines want them to want.

Taking a step back, two factors become clear. First, no airline ever survived just because it managed to cut costs unless it also managed to generate revenues. From the various tools at an airline's disposal, FFPs are certainly among the more effective in helping to retain high spenders.

There is a negative effect on customer behaviour from FFPs that seem less attractive or customer friendly

By definition, FFPs are situated on the revenue rather than on the cost side of the equation. Once this is taken on board, the second factor becomes clear. Frequent flyers tend to be responsible for a large part of a carrier's revenue and of an even larger part of its profits. Drastic cost-cutting when dealing with this crucial customer group might not be a wise idea. If loyal high-yield customers are not at the base of any airline's financial difficulties, why should they have to pay to subsidise unprofitable customer segments or even associated businesses?

In fact, cutting FFP costs beyond the point of customer acceptance has a dual negative impact. FFP members feel upset while fixing the real problems in other areas is postponed further.

The way forward is to exploit the strengths of this wonderful invention and use it as an intelligent part of CRM applications to increase the loyalty effect and revenues. Otherwise, the danger exists that an FFP could become a burden for airlines as the declining loyalty of customers has a faster impact on revenues than the cost-cutting measures transform the bottom line.

It is encouraging that airlines have remained committed to the existence of FFP during the harshest of times, but a commitment is not enough in the long run. A clear strategic vision for the future direction of the FFP is essential. And this can only happen in a CRM context, with the airline putting its best customers in the centre of its attention – rather than making them feel like an annoying cost factor. ■

Rewarding the loyal for less

Frequent Flyer Programmes (FFPs) are no longer merely an extravagant luxury for major carriers. That is the the message that emerged from the first FFP conference taking place in Madrid on 17-18 February. The event was co-organised by Global Flight Management, a consultancy set up in 1996 as specialist in loyalty programmes, and was supported by this magazine.

Around 150 delegates from more than 60 airlines worldwide gathered to debate current FFP issues, along with a number of leading suppliers offering an increasing range of loyalty products. Several IT suppliers now offer reasonably priced solutions that allow airlines of all sizes, including low-cost carriers, to consider an FFP. Some solutions are web-based, but even ASP (application service provider) or licence solutions can be obtained for far lower prices than in the recent past. Upfront costs well below $100,000 are easily achievable.

Most airlines launching new loyalty schemes these days are low-cost carriers, but it is particularly important for them not to approach the FFP topic from a pure cost perspective, but from the more holistic CRM approach described. Several suppliers are strategically focusing on airlines in this growing market segment with their FFP and customer relationship applications, such as HITIT Computer Services, SEDITEL or SITA.

About the author

Ravindra Bhagwanani, who authored this article, is general manager with Global Flight Management, which offers a range of management-related services to airlines in the FFP and CRM field.
www.globalflight.net