

CarTrawler Thought Leadership Series on Revenue and Loyalty for 2017

2016 Top 10 Airline Ancillary Revenue Rankings

CarTrawler-sponsored analysis shows ancillary revenue continues to move forward with an even larger footprint on financial statements and the products offered to consumers

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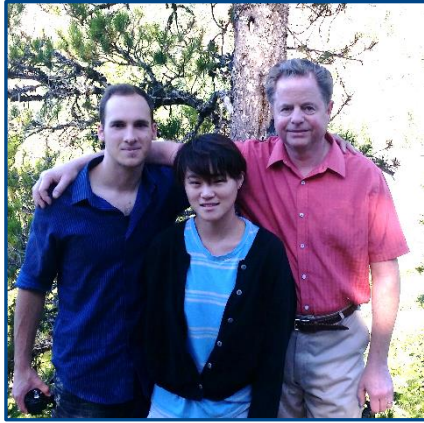
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About Jay Sorensen, Writer of the Report

Jay Sorensen's research and reports have made him a leading authority on frequent flyer programs and the ancillary revenue movement. He is a regular keynote speaker at the annual MEGA Event, spoke at IATA Passenger Services Symposiums in Abu Dhabi and Singapore, and has testified to the US Congress on ancillary revenue issues. His published



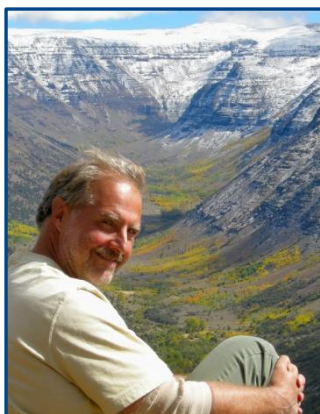
Jay, with son Aleksei and daughter Annika, in North Cascades National Park in Washington.

works are relied upon by airline executives throughout the world and include first-ever guides on the topics of ancillary revenue and loyalty marketing. He was acknowledged by his peers when he received the Airline Industry Achievement Award at the MEGA Event in 2011.

Mr. Sorensen is a veteran management professional with 30 years experience in product, partnership, and marketing development. As president of the IdeaWorksCompany consulting firm, he has enhanced the generation of airline revenue, started loyalty programs and co-branded credit cards, developed products in the service sector, and helped start airlines and other travel companies. His career includes 13 years at Midwest Airlines where he was responsible for marketing, sales, customer service, product development, operations,

planning, financial analysis and budgeting. His favorite activities are hiking, exploring and camping in US national parks with his family.

About Eric Lucas, Editor of the Report



Eric Lucas is an international travel, culture and natural history writer and editor whose work appears in Michelin travel guides, *Alaska Airlines Magazine*, *Westways Magazine* and numerous other publications. Founding editor of *Midwest Airlines Magazine*, he is the author of eight books, including the 2017 *Michelin Alaska* guide. Eric has followed and written about the travel industry for more than 25 years. He lives on San Juan Island, Washington, where he grows organic garlic and heirloom corn; visit him online at TrailNot4Sissies.com.

Eric, at his favorite summer retreat, Steens Mountain, Oregon.

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2016 Top 10 Ancillary Revenue Rankings

The importance and prevalence of ancillary revenue continues to move forward with an even larger footprint on airline financial statements and the products offered to consumers. Back in 2007 the top ten airlines, as rated by total ancillary revenue, generated \$2.1 billion. Fast forward to financial results of 2016 (shown in Table 1) and the top ten tally has leapt to more than \$28 billion. Yet, the challenges faced by the world’s economy reinforce the need for airlines to rely upon ancillary revenue as a tool to serve the needs of consumers and investors.

Table 1: Top 10 Airlines – Total Ancillary Revenue (US dollars)			
Annual Results – 2016		Approximate Sources of Revenue	
		Frequent Flyer Program	A la Carte Such As bags Travel Retail Commissions
\$6,222,000,000	United	48%	52%
\$5,172,400,000	Delta	52%	48%
\$4,901,000,000	American	43%	57%
\$2,832,800,000	Southwest	80%	20%
\$2,100,771,801	Air France/KLM	33%	67%
\$1,982,255,301	Ryanair	None	100%
\$1,355,078,078 *	easyJet	None	100%
\$1,349,812,715 *	Lufthansa Network	57%	43%
\$1,193,698,000	Qantas (excludes Jetstar)	90%	Limited disclosure
\$1,179,131,138	Air Canada	45%	55%

2016 carrier results were based upon recent 12-month financial period disclosures.
 * IdeaWorksCompany estimate based upon updated past disclosure and other sources.

Total ancillary revenue is presented in a different manner this year to emphasize how airlines produce it. Most top ten airlines earn their place on the table through the robust revenue contribution of a frequent flyer program. Specifically, these billion-dollar amounts are generated by the sale of miles or points to banks that issue a carrier’s co-branded credit card. But on this table of giants, Ryanair and easyJet are the exception; their ancillary revenue ranking occurs through a reliance on a la carte fees and the commissions earned from travel retail activities at the website, such as car hire bookings and travel insurance sales. The full description of ancillary revenue is offered on the next page.

Financial documents for 138 airlines were reviewed

Every year since 2007, IdeaWorksCompany searches for disclosures of financial results which qualify as ancillary revenue for airlines all over the globe. Annual reports, investor presentations, financial press releases, and quotes attributed to senior executives all qualify as sources in the data collection process. Of the 138 airlines reviewed, 66 were found to reveal financial results related to ancillary revenue. This represents a nearly threefold increase from the 23 airlines which disclosed ancillary revenue 11 years ago.

IdeaWorksCompany offers a definition of 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.

IdeaWorksCompany further defines ancillary revenue using these categories:
 1) a la carte features, 2) commission-based products, 3) frequent flyer activities,
 4) miscellaneous sources such as advertising, and
 5) the a la carte components associated with a fare or product bundle.

From this list, total airline revenue and ridership data were collected to determine the top ten airlines in overall ancillary revenue, as a percentage of company revenue, and on a per passenger basis. The results for the 66 disclosing airlines will be released in September 2017 as the annual *CarTrawler Yearbook of Ancillary Revenue by IdeaWorksCompany*.

Ancillary revenue as a percent of total revenue favors low cost carriers

It's a logical corollary that airlines with low average fares achieve the best "percent of total revenue" results. Table 2 is dominated by the leading low cost carriers in the world, and nearly all demonstrate sizeable increases since 2011. Measurement by percentage is a reliable indicator because it removes the factor of global currency fluctuations.

Table 2: Top 10 Airlines – Ancillary Revenue as a % of Total Revenue

Annual Results – 2016		Ancillary Source	Compared to their 2011 Results	
46.4%	Spirit	Various	33.2%	↑13.2 points
42.4%	Frontier	Various	7.7%	↑34.7 points
40.0%	Allegiant	Various	27.0%	↑13.0 points
39.4%	Wizz Air	Various	27.9%	↑11.5 points
26.8%	Ryanair	Various	20.5%	↑6.3 points
26.0%	Jet2.com	Various	27.1%	↓-1.1 points
24.3%	Volaris	Various	9.5%	↑15.3 points
24.0%	Hong Kong Express	Various	Carrier began operations in 2013	
22.0%	Jetstar	Various	15.3%	↑6.7 points
22.0%	Pegasus	Various	10.1%	↑11.9 points

2016 and 2011 carrier results were based upon 12-month financial period disclosures.

Let's examine the results for Frontier Airlines as a very robust example. Thanks to Frontier's 2017 filing for an initial public offering of shares, there are new disclosures of the carrier's ancillary revenue prowess. The carrier's systemwide total revenue per passenger was a modest \$114.75 for 2016. That's the average revenue associated with a passenger and includes about \$49 generated by ancillary revenue. A good portion of this amount includes the optional extras passengers can buy such as checked bags, seat assignments, and snacks onboard. A small portion of the \$49 is also composed of revenue produced by Frontier's frequent flyer program and commissions from car hire and hotel bookings.

The airline was remade as an ultra low-cost carrier (ULCC) during 2014 after Indigo Partners acquired Frontier.¹ For 2013 the airline carried 10.8 million passengers² and for 2016 this jumped to 14.9 million on the strength of new ownership, management, and the low fares made possible by the a la carte method. Numbers reveal the truth – consumers embrace the choices delivered by the branded fare approach. They can click to choose maximum savings or buy up to add comfort and convenience.

Worldwide the a la carte approach long embraced by low cost carriers has been adopted by network airlines. Within the US, American, Delta, and United recently introduced basic economy fares (sometimes called seat-only fares) to compete with Frontier and Spirit. These fares reduce the product to a minimalist experience with fees charged for bags and early seat assignments, no elite upgrades, and a ban on flight changes. Yet when presented with higher fare, better service options, the majority of consumers opt to spend more.

Recent comments by Scott Kirby, the President of United, reveal 60 to 70 percent of passengers buy a higher fare when presented with the Basic Economy option.³ American disclosed similar results with 50 percent of customers buying the Main Cabin product when presented the opportunity to consider the lower priced Basic Economy branded fare.⁴

Elsewhere in the world, the practice has been adopted by Air France/KLM, British Airways, and Lufthansa as these airlines compete with the likes of Ryanair, easyJet, and Norwegian. In other regions of the world, basic fares remain a concept to be considered for the near future. That's the revenue power implicit when consumers are offered a choice to save money or spend more . . . most often they spend more.

The ancillary revenue pie is unique for every airline

In the process of collecting data for this report, IdeaWorksCompany makes note when details regarding the sources of ancillary revenue are identified. The activity associated with each of the 66 airlines will be presented in the annual *CarTrawler Yearbook of Ancillary Revenue* which will be released later this year in September. For some airlines, such as British Airways, Delta, and easyJet, the range of disclosure from financial filings and government data provides a rather complete picture of ancillary revenue. Some airlines, such as Hong Kong Express, have chosen to directly disclose their ancillary revenue to IdeaWorksCompany for inclusion in the *Yearbook*.

¹ Frontier Group Holdings SEC Form S-1 Registration Statement dated 31 March 2017.

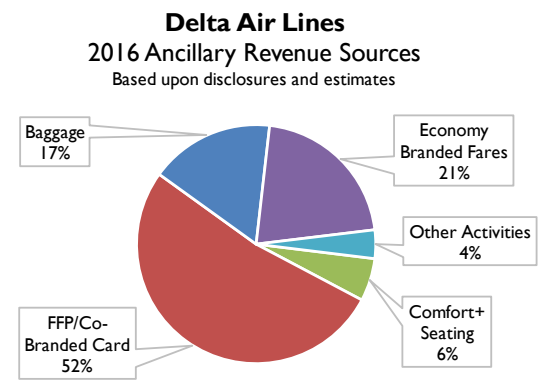
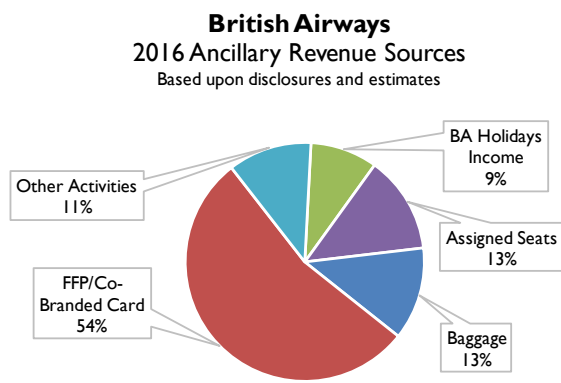
² Frontier Group Holdings SEC Form S-1 Registration Statement dated 31 March 2017.

³ SkyMoney section of *Airline Weekly* dated 12 June 2017.

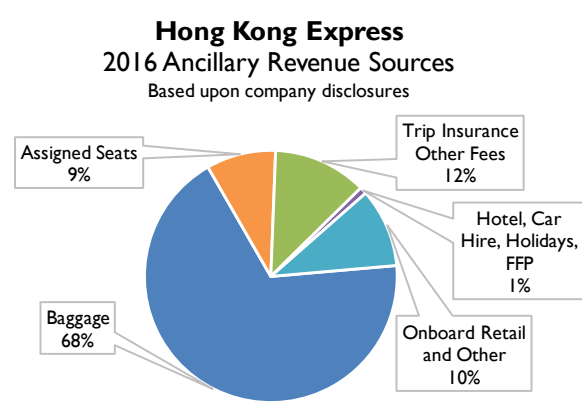
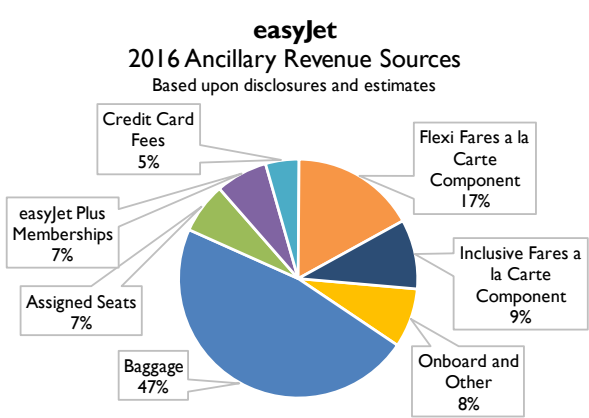
⁴ American presentation at Bank of America Merrill Lynch Conference dated 18 May 2017.

IdeaWorksCompany reviewed the data and made a few adjustments. For example, for British Airways, revenue information was found in the annual reports and investor presentations of IAG, British Airways Holidays, and Avios, and UK government data. “Other activities” were added to equal 0.5% of airline revenue to account for sources such as car hire and trip insurance commissions. Colors assigned to pie slices vary, however blue shading always designates baggage revenue with red for frequent flyer programs/co-branded credit cards.

Global Carrier Examples



Low Cost Carrier Examples



The large slices of blue demonstrate the importance of fees for checked baggage. The slices are smaller for global carriers which continue to include a checked bag on their long-haul routes, such as transatlantic flights. But where Delta and British Airways may have a smaller slice of bag revenue, they certainly generate lots of cash from their frequent flyer programs. The vast majority of activity occurs when airlines sell miles to the banks that issue co-branded cards such as the Delta SkyMiles card issued by American Express.

Branded fares, based upon the “good, better, and best” method of retailing, also contribute to ancillary revenue as shown in the Delta and easyJet examples. The entire fare is not counted as ancillary revenue, but rather the premium above the basic economy fare level is measured. Fees assessed for assigned seating are another method for airlines to boost the bottom line. These fees do tread close to the model defined by low cost carriers; adoption of this practice does pose a risk the perceived quality of global airlines.

Global and low cost carriers earn top ancillary revenue per passenger

The top performing airlines, when ancillary revenue is expressed on a per passenger basis, are a varied collection (Table 3 below). The definition of ancillary revenue includes the results produced by a carrier's frequent flyer program and this can provide a substantial benefit for global airlines such as Delta, Qantas, and United. For some airlines, this represents billions in revenue as shown in Table 4 (on the following page) and allows these airlines to remain competitive when ancillary revenue is measured on a per passenger basis.

Low cost carriers rely upon a la carte activity by aggressively seeking revenue from checked bags, assigned seats, and extra leg room seating. Some of the best in this category have extensive holiday package business with route structures built upon leisure destinations. Allegiant in the US and Jet2.com in the UK share the common bond of emphasizing leisure travel; these are essentially holiday package companies that own an airline.

Table 3: Top 10 Airlines – Ancillary Revenue per Passenger

Annual Results – 2016 (in US dollars)**		Ancillary Source	2016 and 2011 Comparison (Both years in local currency – no conversion)	
Spirit	\$49.89	Various	19.5%	US dollars
Allegiant	\$48.93	Various	43.9%	US dollars
Frontier	\$48.60	Various	434.1%	US dollars
United	\$43.46	Various	19.2%	US dollars
Jet2.com	\$42.46	Various	18.9%	GB pounds
Qantas Airways	\$42.38	Mostly FFP	8.2%	AUS dollars
Virgin Atlantic *	\$42.25	Mostly FFP	2011 comparison not available	
AirAsia X	\$34.41	Various	+12.2%	Malaysian ringgit
Korean Air	\$32.59	Various	+12.8%	Korean won
Alaska Air Group	\$31.41	Various	+27.6%	US dollars

*2016 and 2011 carrier results were based upon 12-month financial period disclosures.
* IdeaWorksCompany estimate based upon past disclosure updated for current report.*

Significant fluctuations of global currencies suggest using the US dollar as the basis of comparison does not effectively convey historical trends. The left side of Table 3 displays 2016 ancillary revenue in US dollars, while the right side expresses the 5-year increase without currency conversion. For example, the 2011 per person ancillary revenue for AirAsia X is compared to 2016 based upon Malaysian ringgit results. This provides a pure comparison without the influence of a strong or weak dollar during the time period.

The results demonstrate the onward march of ancillary revenue on a per passenger basis for these ancillary revenue giants. Frontier's eye-popping increase is largely based upon the carrier's conversion to the ULCC (Ultra Low Cost Carrier) model described earlier in this report. Other factors are at play here too. Airlines are beginning to manage a la carte fees in the same manner as air fares. Lowering some fees might produce more overall revenue if it encourages more consumers to say "yes" to buy a product. Likewise, prices might be increased if consumers demonstrate they "gotta have" a particular service at any price.

This is the classic rule of demand and supply — the invisible hand of the marketplace defined by the economist Adam Smith. Technology is rapidly being promoted to support what is called dynamic pricing; this is the ability to make prices conditional upon a defined set of factors. But caution is warranted here. Just because you can do it . . . doesn't mean you should. Consumers, employees, regulators, and investors need to be on board with these changes through careful — not careless — communication and training.

FFPs are a monetary mileage marvel

Table I at the beginning of this report showed how some carriers truly benefit from the revenue boost of a frequent flyer program with a powerful co-branded portfolio. Table 4 adds detail to this presentation by carving out the frequent flyer revenue data from a few select airlines.

Table 4: Ancillary Revenue Attributed to Frequent Flyer Programs		
Program Name	FFP Revenue	Per Passenger
United MileagePlus	\$3,022,000,000	\$21.11
Qantas Frequent Flyer	\$1,088,173,600	\$21.14
Avios – IAG (BA & Iberia)	\$539,109,946	\$5.36
Azul TudoAzul	\$218,633,950	\$10.60
Japan Airlines Mileage Bank	\$198,887,813	\$4.86
Aeroflot Bonus	\$185,062,151	\$4.26
South African Voyager	\$59,446,855	\$8.59

2016 results based upon recent 12-month financial period disclosures and IdeaWorksCompany calculations.

The co-branding strength of some global regions is apparent with big per passenger results posted by airlines in the US, Australia, and Brazil. The power of these programs is readily apparent when per passenger numbers are evaluated with United and Qantas scoring an average of \$21+ for every passenger carried. Adding another detail, such as program membership, Qantas Group realizes more than \$95 per member based upon 2016 program membership of 11.4 million. The Group backs this result with an amazing statistic: “35 percent of credit card spend in Australia is on Qantas co-branded credit cards.”⁵ It’s an almost otherworldly achievement to have so much of a nation’s commerce pass through an airline marketing program.

Quo vadis? Or, where is your airline going?

The pace of change can be overwhelming, and it can be easy to lose one’s way. In the political arena, what once seemed impossible now seems probable. The same has become true for airlines and the travel industry. Look at what the past 12 months have brought us: 1) Lufthansa is absorbing a good-sized portion of airberlin, 2) IAG has started a long-haul low-cost airline, 3) American, Delta, and United have adopted the basic fare products of their ultra low-cost competitors, and 4) Norwegian Airlines is planning a domestic airline in Argentina. It’s an unpredictable world.

⁵ Qantas Investor Day Presentation, 05 May 2017, page 75.

But wait, there's more. As of preparation of this report, Qatar Airways has been isolated geographically and economically from neighboring countries. The bright futures of Emirates, Etihad, and Turkish have been tarnished by unplanned incidents ranging from a Trump Administration laptop ban to an attempted government coup. Management is often called upon to respond quickly to change, but this can also be called being "reactionary."

It's exactly times like these that call for a diligent and thoughtful pace. Don't add a la carte fees because your airline needs the cash. Embrace the ancillary revenue path only if your airline brand and employees are aligned with it. IdeaWorksCompany offers the five steps below for your consideration.

How to find your ancillary revenue path in 5 steps

1. **Understand the opportunity.** Ensure top management understands the need for ancillary revenue and the many options for implementation. Get outside help to innovate and illuminate.
2. **Brand the mission.** Create a robust ancillary revenue branding statement for your airline as it applies to customers, employees, and investors. This should support the carrier's core brand.
3. **Lead the initiative.** Staff the ancillary revenue function with a diplomat who will encourage others to build, manage, and maximize their ancillary revenue portfolios.
4. **Listen to employees.** They represent the wisdom of those who touch the customer; earning their support will create happy customers and better revenue.
5. **Focus, focus, focus.** Take care in selecting products which are important to customers, represent natural advantages for your airline, and are difficult for your competitors to match.

Has your airline done all of these, or have some been skipped for the sake of expediency?

Successful, vibrant, and progressive organizations — be they corporate or political — work to establish clarity in direction, culture, and ethics. This allows anyone in the organization to instinctively know which path to take when crossroads are approached. *Quo vadis* then becomes a question to which everyone in the organization knows the answer.

Please note: CarTrawler and IdeaWorksCompany will release a 90+ page compilation of results and overall rankings from the 66 disclosing airlines during September 2017. A companion report, scheduled for November 2017, will use these results to extrapolate the total ancillary revenue generated by a global list which exceeds 180 airlines.

Airlines disclose financial information in a variety of currencies. Unless otherwise noted, the information provided in this report is based upon US dollars, which requires the conversion of results for airlines reporting in other currencies. Exchange rates are based upon 01 July 2016 (midyear of the 2016 reporting period).

Alaska



Rapid Revenue Learning

"IdeaWorksCompany helped us sharpen our game, and offer choice to our guests.

"Alaska Airlines leads the way in offering technology that takes the hassle out of air travel and delighting our guests. One way we do that is by offering choice. Our ancillary revenue management was good, but the acquisition of Virgin America required us to be better. Jay Sorensen worked with our cross-functional team from marketing, product, finance, customer service, pricing, and planning to understand benchmark methods used by the best airlines around the globe. With Jay's help, we've sharpened our game."

Toni Freeberg, Director of Distribution & Ancillary Strategy, Alaska Airlines

Airlines everywhere choose IdeaWorksCompany for a revenue boost.

IdeaWorksCompany is a leading consulting resource for ancillary revenue and loyalty marketing. Our client list spans the globe – Europe, Middle East, Americas, South Pacific, and Asia – and every type of carrier.

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